S. HRG. 109–177

Senate Hearings

Before the Committee on Appropriations

Departments of Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies Appropriations

Fiscal Year 2006

109*th* CONGRESS, FIRST SESSION

H.R. 3058

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
DEPARTMENT OF THE TREASURY
DEPARTMENT OF TRANSPORTATION
EXECUTIVE OFFICE OF THE PRESIDENT
NONDEPARTMENTAL WITNESSES

Departments of Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies Appropriations, 2006 (H.R. 3058)

S. HRG. 109–177

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE

COMMITTEE ON APPROPRIATIONS UNITED STATES SENATE

ONE HUNDRED NINTH CONGRESS

FIRST SESSION

ON

H.R. 3058

AN ACT MAKING APPROPRIATIONS FOR THE DEPARTMENTS OF TRANSPORTATION, TREASURY, AND HOUSING AND URBAN DEVELOPMENT, THE JUDICIARY, DISTRICT OF COLUMBIA, AND INDEPENDENT AGENCIES FOR THE FISCAL YEAR ENDING SEPTEMBER 30, 2006, AND FOR OTHER PURPOSES

Department of Housing and Urban Development
Department of the Treasury
Department of Transportation
Executive Office of the President
Nondepartmental witnesses

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DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

TUESDAY, MARCH 15, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:35 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Bennett, Cochran, Stevens, Domenici, Burns, Murray, Byrd, and Dorgan.

DEPARTMENT OF TRANSPORTATION

OFFICE OF THE SECRETARY

STATEMENT OF HON. NORMAN Y. MINETA, SECRETARY

ACCOMPANIED BY:

JEFFREY A. ROSEN, GENERAL COUNSEL

PHYLLIS SCHEINBERG, ACTING ASSISTANT SECRETARY, BUDGET AND PROGRAMS, AND CHIEF FINANCIAL OFFICER

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning and welcome. The Subcommittee on Transportation, Treasury, the Judiciary, HUD, and Related Agencies, now commonly known as "THUD," will come to order.

This is the first hearing of the newly reconstituted appropriations subcommittee. It is quite a mouthful and, in many ways, it is just as diverse and complex as the VA/HUD Appropriations Subcommittee that I most recently chaired before the Appropriations Committee was restructured.

But I acknowledge and welcome my new ranking member, Senator Murray. I think everyone knows of my high regard and close working relationship I had with Senator Mikulski, with whom I exchanged the gavel on VA/HUD Appropriations. Senator Mikulski is a close friend, and because of my high regard and friendship, we were able to forge an excellent bipartisan working relationship. Things change in life and time marches on. We take on new responsibilities and challenges. Certainly there is no lack of challenges in this restructured appropriations subcommittee. I look forward to developing a relationship and strong friendship with my new ranking member, Senator Murray.

This is going to be a demanding subcommittee with diverse and divisive issues. I know we are both pragmatists. We are here to do a job and that job is to pass an appropriations bill. I know we will get that done.

We welcome Transportation Secretary Norm Mineta, appearing before us today to testify on the administration's budget request for the Department of Transportation for fiscal year 2006. We are old friends, and for the last several years, we have been working together with others from my perch as chairman of the Senate Subcommittee on Transportation and Infrastructure of EPW on reaching a consensus on highway spending. I am disappointed that reaching a consensus on highway spending has proved to be so elusive and that passage of the highway authorization bill has been delayed for 3 years primarily due to disagreements over funding levels.

To be clear, I am an infrastructure Republican who supports funding for highways and transportation. Our Nation's network of roads keeps communities and families connected to one another and serves as the primary system for moving goods and products that are the lifeblood of our economy, and a good transportation system is necessary to reduce the fatalities we have in transportation in too many areas.

I also take great pride in the national highway system that began with Highway 70 in St. Charles, Missouri in 1956. Our highway system soon will reach its 50th anniversary, which only underscores the need for more than a facelift as we move further into the 21st century. There are new demands created by a global marketplace that require we move our goods and products more quickly and more efficiently. For the United States to compete, we have to make the necessary investments in our highways, waterways, and airways.

Beyond the necessary movement of goods, investing in transportation also benefits jobs and stimulates the economy. The Department of Transportation has estimated that every $1 billion of new Federal investment creates more than 47,500 jobs. Moreover, according to the Associated General Contractors, failure to enact a 6-year transportation bill could result in the loss of some 90,000 jobs.

To that end, I am pleased to see that the budget request adjusts the total spending level for the 6-year transportation authorization bill to $284 billion. The willingness to increase the funding level for the reauthorization bill by $28 billion is a step in the right direction. Nevertheless, this accommodation on the part of the administration, in my view, still falls short of the investment that is needed to maintain and repair our Nation's crumbling infrastructure, much less to construct the new roads to reduce time spent in traffic and make needed safety improvements in rural and urban roadways.

Secretary Mineta, as you know, I speak from the twin pulpit of both the primary Senate transportation authorizing and appropriations subcommittees in seeking your support and commitment to reach an accord with adequate funding for a 6-year highway bill.

I expect this bill to complement our efforts and funding decisions on this subcommittee.

Consequently, I am disappointed the administration is proposing some $59.5 billion in new budgetary resources for DOT which is a decrease of $2.1 billion or 4 percent from the enacted level of the current year. While I respect and support the efforts of the administration to reduce the deficit, I do not believe it appropriate to balance the Federal books on the back of critical transportation infrastructure programs.

For example, the Airport Improvement Program is slated for one of the largest reductions in the entire fiscal year 2006 budget, despite the proven track record that enhances airport safety, capacity, and security. After the program received high marks in the OMB PART process, I am at a loss to understand why this program remains in the sights of the budget gnomes.

This is not to say that transportation spending should automatically be spared from the budget axe, but I do believe we must continue to increase the Nation's investment in transportation, especially highways and roads. To be blunt, this investment means a strong economy, safety, especially for the youth of our Nation, increased employment, decreased congestion, and enhanced security.

In particular, the Department of Transportation's Conditions and Performance Report estimates that Federal investment in roads must increase by 17 percent per year simply to maintain our Nation's existing highway and bridge system. Improving the system would require some 65 percent more than currently invested. I think our own eyes and experiences speak directly to this issue. We live in one of the most affluent and economically prosperous areas of the country and every day we are confounded by unflagging traffic congestion, often during non-rush hour time, as well as unavoidable and significant potholes and other road damage, which is often covered with steel plates, if we are lucky. Our bridges are often down to one lane. Unfortunately, we have little in the way of options to avoid either the congestion or other road problems. It has gotten worse over the last few years and will likely continue to worsen without substantial investment.

More troubling, some 43,000 people are killed on our roads and highways each year. In Missouri alone, traffic fatalities have increased from 1,098 in 2001 to 1,123 in 2004. We cannot eliminate all traffic fatalities, but we must make our highways and roads safer, and we can only do that through investment.

Finally, I am very concerned about the reductions throughout DOT's fiscal year 2006 budget request. For example, regardless of my position, elimination of funding for Amtrak seems politically unlikely, not practical. However, assuming the adoption of real reforms, I do not see where the needed funds can come from without putting some other program or priority at risk.

I am thankful that the administration has included $146 million to support the Federal Railway Administration's rail safety activities, an increase of $8 million over the fiscal year 2005 level. While helpful, this increase seems to underestimate the real needs. In the last 9 weeks alone, there have been more railway accidents than at any time since FRA began tracking the data.

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

I have much to learn about the funding needs of DOT, but I have a pretty good guess right now. I will have questions for today, for the record and in the future. Mr. Secretary, I look forward to your testimony today and to our future dialogues.

It is now my pleasure to turn to my new ranking member, Senator Murray.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

The subcommittee will come to order. This is the first hearing of the newly reconstituted Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD, and Related Agencies. It is quite a mouthful and is, in many ways, just as diverse and complex a subcommittee as the VA–HUD Appropriations Subcommittee that I most recently chaired.

First, I want to acknowledge and welcome my new Ranking Member, Senator Murray. I think everyone knows of my high regard for Senator Mikulski, with whom I exchanged the gavel at the VA–HUD Appropriations Subcommittee. I consider Senator Mikulski a close friend and because of my high regard and friendship we were able to forge an excellent, bipartisan working relationship. However, as with all things in life, time marches on and we take on new responsibilities and challenges. I look forward to the new responsibilities and challenges of this restructured appropriations subcommittee. I also look forward to developing a new relationship and hopefully a strong friendship with my new Ranking Member, Senator Murray. This will be a demanding subcommittee with many diverse and likely divisive issues. However, I know we are both pragmatists; we are here to do a job and that job is to pass an appropriations bill and I know we will get this job done.

I welcome Transportation Secretary Norman Mineta for appearing before us today to testify on the administration's Budget Request for the Department of Transportation (DOT) for fiscal year 2006. We are old friends and, for the last several years, we have been working together with others from my perch as Chairman of the Senate Subcommittee on Transportation and Infrastructure of the EPW Committee on reaching a consensus on highway spending. I am disappointed that reaching a consensus on highway spending has proven to be so elusive and that passage of the highway authorization bill has been delayed for 3 years primarily due to disagreements over funding levels.

To be clear, I am an infrastructure Republican who supports funding for our highways. Our Nation's network of roads keeps communities and families connected to one another and serves as the primary system for moving goods and products that are the lifeblood of our economy. I also take great pride that our national highway system was born in St. Charles, Missouri in 1956. Our highway system will soon reach its 50th anniversary, which only underscores the need for more than a facelift as we move further into the 21st century—there are new demands created by a global marketplace that requires that we move our goods and products quicker and more efficiently. For the United States to compete, we must make the necessary investments in our highways, waterways and airways.

Beyond the necessary movement of goods, investing in transportation also benefits the creation of new jobs and stimulates the economy. DOT estimates that every $1 billion of new Federal investment creates more than 47,500 jobs. Moreover, according to the Associated General Contractors, failure to enact a 6-year transportation bill will result in the loss of some 90,000 jobs.

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This is not to say that transportation spending should automatically be spared from the budget axe, but I do believe that we must continue to increase the Nation's investment in transportation, especially highways and roads. To be blunt, this investment means a strong economy, safety for families, especially the youth of the Nation, increased employment, decreased congestion and enhanced security.

In particular, the Department of Transportation's Conditions and Performance report estimates that Federal investment in roads must increase by 17 percent per year simply to maintain our Nation's existing highway and bridge system. Improving the system will require some 65 percent more than currently invested. I think our own eyes and experiences speak directly to this issue. We live in one of the most affluent and economically prosperous areas of the country and every day we are confounded by unflagging traffic congestion, often during non-rush hour time, as well unavoidable and significant potholes and other road damage which is often covered with steel plates if we are lucky. Our bridges also are often down to one lane. Unfortunately, we have little in the way of options to avoid either the congestion or our other road problems. It has gotten worse over the last few years and likely will continue to get worse without substantial investment.

More troubling, more than 40,000 persons are killed on our roads and highways each year. In Missouri alone, traffic fatalities have increased from 1,098 in 2001 to 1,123 in 2004. While we cannot eliminate all traffic fatalities, we must make our highways and roads safer and we can only do that that through investment.

Finally, I am very concerned about reductions throughout DOT's fiscal year 2006 budget request. For example, regardless of my position, elimination of funding for Amtrak seems politically unlikely, not practical. However, even assuming the adoption of real reforms, I do not see where the needed funds can come from without putting some other program or priority at risk. I am thankful that the administration has included $146 million to support the Federal Railway Administration's rail safety activities, an increase of $8 million over the fiscal year 2005 enacted level. While helpful, this increase seems to underestimate the real needs. In the last 9 weeks alone, there have been more railway accidents than at any time since FRA began tracking this data.

I have much to learn about the funding needs of DOT. I will have questions for today, for the record and in the future. Mr. Secretary, I look forward to your testimony today and to our future dialogues. I now turn to my new Ranking Member, Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Well, thank you very much, Mr. Chairman.

Today signals a new day in the history of this subcommittee. We have broad, new responsibilities, including the funding needs for housing and for the judiciary. The subcommittee now has a complement of 19 members and only the Defense Subcommittee has more members than we do.

I have to say that I am sorry to see my longtime friend and partner, Richard Shelby, move on to another subcommittee. Senator Shelby was a thoughtful and considerate chairman of this subcommittee and he consistently sought to produce a balanced, bipartisan bill that the maximum number of Senators could support. His leadership on this subcommittee will be missed.

At the same time, I very much look forward to working with Senator Bond in tackling these new responsibilities. Chairman Bond has demonstrated a longstanding commitment to the Nation's transportation and housing needs. In addition to chairing the VA/

HUD Subcommittee for several years, he has earlier served as the chairman of the Banking Subcommittee with authorizing jurisdiction over the housing programs and now serves as chairman of the Environment and Public Works Subcommittee with authorizing responsibility over our highway programs. Senator Bond's considerable expertise in both of these areas, as well as that of his staff, will be a great asset as we work together to assemble an appropriations bill that addresses all the disparate challenges that face us.

With that goal in mind, I am sorry that the President's budget for fiscal year 2006 does not provide us with a better starting point. The Bush administration's budget for the Department of Transportation has a number of unjustified funding cuts, as well as some gaping holes.

Over the course of the last year, air traffic has expanded beyond the levels we were experiencing prior to September 11, 2001. All indications are that air traffic will continue to grow, but the administration has decided that now is the time to impose dramatic cuts in our investment at improving safety and expanding capacity at our airports.

Despite the fact that the Federal Aviation Administration is well behind its own goals for replacing our outdated air traffic control system, the administration is again proposing funding cuts to the FAA's modernization effort. Between the cuts already imposed for the current year and the cuts proposed for next year, the administration is seeking to cut almost half a billion dollars out of this effort.

Also in the area of aviation, the administration is proposing to cut in half funding for the Essential Air program, endangering the continuation of commercial air service to dozens of rural communities across the Nation.

Clearly the largest gaping hole in the President's budget is the request to zero out the annual subsidy to Amtrak. While documents accompanying the President's budget speak of the merits of pushing Amtrak into bankruptcy, Secretary Mineta has stated in recent weeks that a bankrupt Amtrak is not the administration's goal.

It appears that the administration wants to play a game of chicken with Congress, threatening to push the railroad into bankruptcy if we do not enact the President's proposed Amtrak reform bill. I think the administration's game of chicken with Congress is reckless and irresponsible. It will undermine the opportunity for a meaningful discussion of reforms. This debate should not take place with the threat of imminent bankruptcy hanging over the railroad, its 25 million passengers and its almost 20,000 employees.

Personally, I would welcome congressional action on the Amtrak reform bill. I do not say that because I think we should acquiesce to the administration's threats. I say that because I believe a meaningful and thorough debate over Amtrak and its finances would bring a number of important facts to the surface, facts that many people are either unaware of or have sought to ignore.

A thorough debate on Amtrak would require policy makers to admit that Amtrak's largest liability, both in the short and long term, is not the cost of subsidizing long-distance trains but rather the cost of maintaining and modernizing the Northeast Corridor.

Just maintaining the corridor costs some $600 million a year. Parts of the corridor date from the early half of the last century. Secretary Mineta's own Inspector General has estimated the cost of deferred maintenance over the corridor exceeds at least $5.5 billion. With those huge costs looming, the administration now wants the States along the corridor to help pay them.

A thorough debate over an Amtrak reform bill would bring to the surface the fact that Amtrak currently carries huge long-term debts. Back in 1997, the Amtrak Reform Act required Amtrak to seek to become the only self-sufficient passenger railroad in the world. Congress steadily cut Amtrak's operating subsidy. As a result, Amtrak took on more and more debt to keep afloat. Amtrak's total long-term debt now exceeds $3.8 billion. This burden is not going to go away no matter how you reform or reorganize the railroad.

A thorough debate over an Amtrak reform bill would bring to the surface the fact that none of the reform plans being considered, including the administration's proposed reform bill, would save money in the near term. In fact, most of these reform plans require a substantial restructuring that would add to Amtrak's near-term costs, not reduce them. Indeed, when the Bush administration submitted its reform plan last year, it also submitted a budget that boosted the amount of spending for 2006 and beyond to $1.4 billion annually. That is $200 million more than we currently invest in Amtrak.

A thorough debate over an Amtrak reform bill would bring to the surface the fact that the administration shares some of the credit and the blame for the current conditions of Amtrak, conditions that include the highest passenger count in history with the fewest number of employees in years. But when you review the administration's recent rhetoric on Amtrak, you would think that Amtrak is some independent renegade operation running amok with Federal dollars. The fact is that this Transportation Secretary and his predecessors have continually served on Amtrak's Board of Directors and have been party to most, if not all, of the railroad's strategic decisions.

While I would welcome congressional action on an Amtrak reform bill for the reasons I have stated, I have to point out that reform legislation is the responsibility of the Senate Commerce Committee, and I note that its chair is here today with us. It is not the responsibility of the Appropriations Committee.

The job of this subcommittee is to set Amtrak's subsidy level for the coming year. To date, the only resources the President has proposed for the coming year are $360 million to allow for the continuation of local commuter rail services only in the event that Amtrak ceases operations. And that is a very dangerous game.

The budget resolutions currently being debated in the House and the Senate set the overall levels for domestic discretionary spending at the level included in President Bush's budget. That proposal includes his anticipated zero for Amtrak's traditional subsidy and $360 million for continuation of commuter services. If this budget is adopted and that overall ceiling on discretionary spending becomes binding on the Appropriations Committee for the coming fiscal year, I do not know where this committee is going to come up with an extra billion dollars to keep Amtrak operating next year.

Let me say that while I have been critical of several proposals in the President's budget for transportation, there are some positive things to be found in this budget as well.

The administration is finally requesting funds to reverse the continuing attrition of our air traffic controller workforce. One of my questions this morning will focus on why the FAA is recognizing the need to replace its dwindling number of controllers but not its dwindling number of air safety inspectors.

PREPARED STATEMENT OF SENATOR PATTY MURRAY

Finally, I want to applaud the proposal in the administration's budget to boost funding for the FAA's Joint Planning and Development Office, which is charged with charting the course for the next generation of our aviation system. The JPDO, as it is known, is a critical initiative that will determine the extent to which America remains in a leadership role in aviation. One area where the administration and I agree is that this leadership position must never be ceded to others.

Thank you, Mr. Chairman.

[The statement follows:]

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Between the cuts already imposed for the current year and the cuts proposed for next year, the administration is seeking to cut almost half a billion dollars out of this effort.

Also in the area of aviation, the administration is proposing to cut in half funding for the essential air service program—endangering the continuation of commercial air service to dozens of rural communities across the Nation.

AMTRAK

Clearly, the largest gaping hole in the President's budget is the request to zero-out the annual subsidy to Amtrak. While documents accompanying the President's budget speak of the merits of pushing Amtrak into bankruptcy, Secretary Mineta has stated in recent weeks that a bankrupt Amtrak is not the administration's goal.

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In fact, most of these reform plans require a substantial restructuring that would add to Amtrak's near-term costs, not reduce them.

Indeed, when the Bush Administration submitted its reform plan last year, it also submitted a budget that boosted the amount of spending for 2006 and beyond to $1.4 billion annually—that is $200 million more than we currently invest in Amtrak.

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AIR TRAFFIC CONTROL WORKFORCE

The administration is finally requesting funds to reverse the continuing attrition of our air traffic control workforce.

One of my questions this morning will focus on why the FAA is recognizing the need to replace its dwindling number of controllers but not its dwindling number of air safety inspectors.

FAA JOINT PLANNING & DEVELOPMENT OFFICE

Finally, I want to applaud the proposal in administration's budget to boost funding for the FAA's Joint Planning and Development Office, which is charged with charting the course for the next generation of our aviation system. The "J.P.D.O.", as it is known, is a critical initiative that will determine the extent to which America remains in a leadership role in aviation.

One area where the administration and I agree is that this leadership position must never be ceded to others.

Thank you, Mr. Chairman.

Senator BOND. Thank you very much.

Senator STEVENS. I think we have to move sometime to have a limit on opening statements. Some of us have other committees to go to, and opening statements, when they go on and on, just delay us all.

Senator BOND. Thank you, Chairman Stevens. I have a lot to say about this as my first hearing on this, and we will keep our questions limited to 5 minutes each and ask that others make limited opening statements. But now, following practice, I will turn to the chairman of the full committee, Chairman Cochran.

STATEMENT OF SENATOR THAD COCHRAN

Senator COCHRAN. Mr. Chairman, let me congratulate you for your thoughtful and well-chosen remarks opening the hearing today, setting in context the challenges that we have before us with a limited amount of money available to this committee, to continue to support a massive transportation system for our country.

I cannot think any other person I would rather see running the Department, though, than Norm Mineta. I know he has the experience and the talent, the know-how, the background. I can remember when he and I were serving in 1973 as brand new members of the House of Representatives and we were assigned to the Public Works and Transportation Committee. Through work on the Surface Transportation Subcommittee and then the Aviation Subcommittee, it afforded a training ground for him that I know has served him well. He has turned in a distinguished record of service as our Secretary of Transportation, and I congratulate you, Mr. Secretary, for your good work and wish you well as you carry out the mandate of the Congress with the funding that we will provide for you and our transportation system.

Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Cochran.

Now, I turn to the ranking member of the full committee, Senator Byrd.

STATEMENT OF SENATOR ROBERT C. BYRD

Senator BYRD. Mr. Chairman, I thank you, and I was very encouraged, by the opening statements. It seemed to me that "action" and "forward" and "excelsior" are the words that best typify the way you see your charge in the days ahead. I congratulate you for assuming the chairmanship of this very important subcommittee. Between your responsibilities as chairman of the subcommittee, as well as the chairman of the Surface Transportation Subcommittee on the Environment and Public Works Committee, you, Mr. Chairman, will chart the future course of transportation in America.

I believe that you will recall the words of Isaiah who said: "Prepare ye the way of the Lord. Make straight in the desert a highway for our God. Every valley shall be exalted and every mountain and hill shall be laid low. The crooked shall be made straight and the rough places plain. The glory of the Lord shall be revealed and all flesh shall see it together."

I think you are going to make the rough places plain and the crooked straight. I want you to know that I admire your stick-to-it-iveness, your ability and the force of your seniority as chairman of this subcommittee is going to be felt. It is about time.

I also welcome Secretary Mineta to the committee this morning. I have to admit that I am happier to see him than to see his budget.

I am particularly concerned with the impact of the transportation budget on the rural communities and small towns of West Virginia and all of America. Mr. Secretary, rural America is hurting. Not everyone is caught up in the rosy scenarios of the White House. There are several States, communities, and towns that are continuing to see persistently high unemployment and a dwindling tax base. These places are stretching their public dollars to the breaking point. When I look at this year's budget request for the Department of Transportation, I believe the administration has turned the back of its hand to these communities.

By proposing to eliminate all direct subsidies to Amtrak and put the railroad into bankruptcy, the administration threatens to further isolate hundreds of communities that depend on Amtrak to link them with the rest of the Nation's transportation system. For that reason, I plan to introduce an amendment to the budget resolution that would increase the funding for transportation by $1.04 billion in fiscal year 2006. When combined with the $360 million that the President has requested for the continuation of commuter services in the event of Amtrak's termination, my amendment would bring total rail passenger funding up to $1.4 billion in 2006.

When President Bush submitted his budget request for fiscal year 2005, the President recognized that Amtrak funding should grow to $1.4 billion in 2006 and beyond. My proposal would help the President to reach his goal.

This administration's proposal for a reformed Amtrak seeks to require the States to pay all of their trains' operating losses for the first time. As such, the administration wants the States to take on these costs at the same time they are dealing with the skyrocketing costs of Medicaid, education, homeland security, and so much more.

It is no wonder that we have not seen too many Governors step forward in support of the administration's Amtrak proposal. While the President's budget proposes to zero out all direct subsidies for Amtrak, the administration does request $360 million to maintain commuter rail service in the largest cities in America. There again, you see greater focus on urban centers and benign neglect for the needs of small communities and towns.

In the area of aviation, the President's budget completely eliminates all funding for the small community air service program which has provided grants to several small airports, including airports in West Virginia, to recruit or retain their commercial air service. After zeroing out these small community initiatives, the administration also proposes to cut in half funding for the Essential Air Service. That program was an elemental part of the negotiated compromise that accompanied the deregulation of the airlines in 1978. As part of that compromise, the Federal Government agreed to provide full subsidy to ensure that certain communities would not lose all of their air service when the airlines streamlined their operations and changed their route structure. Now the administration wants to walk away from that deal. It does not want to play. It does not want to pay. But communities like Bluefield, West Virginia, and Beckley, West Virginia, do not have the kind of excess resources that would allow them to pay as soon as October 1 what is rightly the Federal Government's share.

Now, Mr. Chairman, I believe that this transportation budget is particularly punitive to our small communities and towns and those States that have continued to struggle economically. These places are ill-suited to put up matching funds for what have long been core responsibilities of the Department of Transportation. I hope that we will take a critical eye to these proposals as we move forward on the budget and appropriations for the coming fiscal year.

I thank you, Mr. Chairman. I thank our ranking member, and thank you, Mr. Secretary.

Senator BOND. Thank you much, Senator Byrd.

Senator Stevens.

Senator STEVENS. I shall wait for my time allocated for questions.

Senator BOND. Senator Dorgan.

STATEMENT OF SENATOR BYRON L. DORGAN

Senator DORGAN. Mr. Chairman, I believe that Senator Byrd's statement really covers much of what I would say, especially about Amtrak. I am very concerned about Amtrak funding and hope that there can be a bipartisan agreement here in the Congress to deal with the funding for Amtrak.

Essential Air Service is a very significant and serious issue.

There are many issues in the President's budget that I believe are particularly punitive to rural areas of the country.

So I will not take my entire time. I will be around to ask some questions, but let me associate myself with Senator Byrd's remarks with respect to the impact of the budget on rural areas.

Senator BOND. Thank you very much, Senator Dorgan.

Senator Domenici.

Senator DOMENICI. I will defer. I will be next.

Senator BOND. All right. We will go to Senator Burns.

STATEMENT OF SENATOR CONRAD BURNS

Senator BURNS. Thank you very much, Mr. Chairman. I just want to make a couple points and I want to thank the Secretary for coming today and dealing in an area that touches almost every American, and that is transportation.

There are three areas that I am principally interested in: the airport improvement program, the Essential Air Service, and Amtrak.

Essential Air Service, Mr. Secretary, you might want to sort of file this not 13. You might get halfway there, though. I think it is time we reassess our Essential Air Service, where those monies are going, and maybe we can save some. I know some areas that take advantage of a program and it is time to reassess or maybe have an oversight hearing on how we choose and how we fund EAS.

In another area, Amtrak—I think we should be thinking more about light rail. We cannot in our highway system outbuild America's love for the automobile. 395 down here from the beltway into Washington from 6 o'clock in the morning until about 9:00 is the world's largest parking lot. So we are going to have to find other ways to move people because we are a mobile society in those areas.

So we find ourselves with some big challenges ahead, and I cannot think of anybody any better to do it than you. I have a great deal of confidence and I think, as time moves along, we will overcome all these areas in which I have a great interest and which are very, very important to rural America. I thank you for coming this morning.

Mr. Chairman, congratulations in your new chairmanship. We are under good leadership here. So thank you very much.

Senator BOND. Thank you very much, Senator Burns.

Senator Domenici.

Senator DOMENICI. Are these opening statements?

Senator BOND. Opening statements.

Senator DOMENICI. I have none.

I was going to ask him, not to answer, but I was going to ask—let us see how the chairman responds—are you considering a change in the CAFE standards? Please do not answer.

Senator BOND. I would answer that, but I will not take the time.

Senator Bennett.

STATEMENT OF SENATOR ROBERT F. BENNETT

Senator BENNETT. Thank you, Mr. Chairman, and congratulations to you on your assuming this chairmanship.

The only opening comment I would make to Secretary Mineta is one of gratitude for him and his staff and the cooperative way in which they worked with us in Utah on our various challenges. We have had a lot of conversation about ADA problems with commuter rail, and I understand that we are about 99 percent of the way towards getting this resolved. The other 1 percent might fall into place if the Secretary's counsel, Jeffrey Rosen, should come to Utah and see for himself where we are. On behalf of the citizens of Utah, I extend a very warm invitation and a very rapid invitation. As quickly as you can get him out there to get that resolved, Mr. Secretary, we would appreciate it.

With that, Mr. Chairman, I will save anything else for the question period.

Senator BOND. Thank you very much, Senator Bennett.

And now, Secretary Mineta, despite everything, we are ready to have your opening statement. Please proceed. We will make your full statement part of the record.

STATEMENT OF NORMAN Y. MINETA

Secretary MINETA. Thank you very much, Mr. Chairman. Congratulations on becoming the new chair of this subcommittee, and I look forward to working with you.

Let me introduce with me, Jeff Rosen to my left, the General Counsel in our Department, and to my right, the Acting Assistant Secretary for Budget and Programs and Chief Financial Officer, Phyllis Scheinberg.

Mr. Chairman and members of the subcommittee, thank you very much for this opportunity to appear before you today to discuss the President's fiscal year 2006 budget request for the Department of Transportation.

In the context of an overall Federal budget that emphasizes, No. 1, spending restraint, and No. 2, directs resources to national priorities, items that President Bush spoke to in his State of the Union message. President Bush is requesting $59.5 billion for the Department of Transportation in fiscal year 2006, slightly more than his 2005 request.

SURFACE TRANSPORTATION PROGRAMS

The largest portion of the President's request supports surface transportation programs, including $35.4 billion in fiscal year 2006 for the Federal Highway Administration. As all of you know, the President has proposed a record-setting surface investment of $284 billion over the 6-year period life of the bill, an increase of 35 percent over the Transportation Equity Act for the 21st Century (TEA21). Under the Safe, Accountable, Flexible, and Efficient Transportation Equity Act (SAFETEA), increased funding will go to the States, along with greatly expanded flexibility to encourage private investment and achieve more efficient use of our highways. The administration is strongly committed to achieving enactment of these and other policy initiatives in SAFETEA and to do so before the current extension, which is the seventh one we are working on and which expires on May 31.

The administration is also proposing record support for transit programs in fiscal year 2006. Recommended funding increases by $134 million to $7.8 billion for transit projects that bring people to jobs and development to communities.

Funding for highway safety, through the National Highway Traffic Safety Administration and the Federal Motor Carrier Safety Administration, increases by $45 million in fiscal year 2006 and continues on an upward path throughout the life of the SAFETEA reauthorization. The Bush administration's unprecedented focus on safety is paying off. Even with more people driving more miles, we achieved the lowest highway fatality rate on record. SAFETEA must build on those successes.

INTERCITY PASSENGER RAIL

Turning to rail, perhaps the most widely discussed aspect of the President's transportation budget is the decision to request no further subsidies for Amtrak until and unless there is real and meaningful reform that puts passenger rail on the solid foundation to grow and deliver safe and reliable quality service that matches local needs.

After 34 years of Amtrak operating losses and $28 billion in taxpayer subsidies, it is clear that the current model of passenger rail service is flawed and unsustainable. Amtrak is on financial life support. In the last 4 years alone, annual Federal subsidies have more than doubled from $520 million in 2001 to $1.2 billion in fiscal year 2005. Yet, infrastructure is deteriorating and service declining as Amtrak continues to delay desperately needed maintenance of the infrastructure that it already owns, and starves investments in new and innovative services that would attract new riders and boost revenues.

Let me be very clear. The Bush administration remains committed to intercity passenger rail service and is prepared to commit additional financial resources if the Congress will join with us to create a sustainable model. I am hopeful that now that the debate has been opened, real reform will be on the congressional agenda this year.

FEDERAL AVIATION PROGRAMS

Finally, for aviation, the Bush administration plans major investment to keep up with growing demand as passengers return to the skies in record numbers and as air cargo continues to take off, as has already been indicated by the panel.

The President's 2006 budget requests $14 billion for the Federal Aviation Administration, providing major support for building new infrastructure and deploying technology that enhances the capacity and the safety of today's aviation system. The budget triples funding for the Joint Planning and Development Office where we are designing the Next Generation air transportation system in readiness for the dramatic changes ahead in the way we fly.

Within the total FAA budget, we request funding for the hiring of 1,249 air traffic controllers in fiscal year 2006. Specifically, the operations budget includes a nearly $25 million increase to fund 595 new air traffic controllers, in addition to replacing the 654 that are expected to leave the system through retirement. These additional controllers represent the first step in the FAA's plan that was announced in December to begin training the staff needed to replace future retirees and to meet the growing demand for air service. This is an initiative to streamline and modernize controller training to speed these new experts to their posts and to save money as well.

PREPARED STATEMENT

Mr. Chairman, thank you for this opportunity to share some of the key elements of the President's budget request for the Department of Transportation for fiscal year 2006. You will find additional details within my written statement that was submitted earlier, as well as our *Budget in Brief*. Mr. Chairman, I will now be happy to respond to questions of the subcommittee.

[The statement follows:]

PREPARED STATEMENT OF NORMAN Y. MINETA

Mr. Chairman, members of the subcommittee, thank you for the opportunity to appear before you today to discuss the administration's fiscal year 2006 budget request for the Department of Transportation. The President's request, which totals $59.5 billion in budgetary resources, includes major investments in our Nation's highways and roadways, airports and airways, railroads, transit systems, and other transportation programs that move the American economy. This budget makes a strong commitment to the infrastructure, technology, and research that will ensure that our Nation's transportation network remains a potent and capable partner as our economy continues to grow.

I am proud of the considerable progress that the Department of Transportation has made over the past 4 years in advancing the safety, reliability, and efficiency of our transportation system. Through the Bush Administration's unprecedented focus on safety, for example, we have achieved the lowest vehicle fatality rate ever recorded and the highest safety belt usage rate ever recorded. During the same time, we have helped bring about the safest 3-year period in aviation history.

Enactment of a 6-year reauthorization of surface transportation programs is a top priority. The administration's reauthorization proposal, the Safe, Accountable, Flexible, and Efficient Transportation Equity Act, or SAFETEA, provides a blueprint for investment that relieves gridlock and ensures future mobility and safety on the Nation's roads and transit systems. The 2006 budget includes a record investment of $284 billion in Federal resources over the 6-year life of the bill—almost $35 billion more than funding under TEA21, the previous surface transportation authorization. Continued delays in enactment of the reauthorization impede proper planning by States and communities and deprive them of the ability to use new flexibilities that the Bush Administration is proposing to encourage private investment and achieve more efficient use of the Nation's highways.

The budget request also reflects the imperative for reform of America's intercity passenger rail system, which Amtrak has been operating at a loss for 33 years. Amtrak has received more than $29 billion in taxpayer subsidies, including more than $1 billion in each of the last 2 years, despite the requirement of the 1997 Amtrak Reform Act that after 2002, "Amtrak shall operate without Federal operating grant funds appropriated for its benefit." In 2003, the administration sent to the Congress the President's Passenger Rail Investment Reform Act. This proposal would align passenger rail programs with other transportation modes, under which States work in partnership with the Federal Government in owning, operating, and maintaining transportation facilities and services.

Deteriorating infrastructure and declining service further the case that, without congressional action on the administration's reform proposals, continued taxpayer subsidies cannot be justified. Consequently, no funding is included in the 2006 budget for Amtrak. Rather, $360 million is budgeted to allow the Surface Transportation Board to support existing commuter rail service along the Northeast Corridor and elsewhere should Amtrak cease commuter rail operations in the absence of Federal subsidies. The President's budget is a call to action: The time for reform is now. If the administration's management and financial reforms are enacted, the administration is prepared to commit additional resources for Amtrak—but if, and only if, reforms are underway. We want to work with the Congress and with Amtrak to make meaningful reforms that will enable intercity passenger rail to achieve success and Amtrak to achieve financial independence. I am optimistic that these reforms can be accomplished this year.

The President's fiscal year 2006 budget includes nearly $14 billion for the Federal Aviation Administration to continue our investments both in building new infrastructure and in deploying technology that enhances the capacity and safety of the Nation's aviation system. The President's request for the FAA includes funding for the hiring of 1,249 air traffic controllers in fiscal year 2006. Specially, the operations budget includes nearly $25 million to fund 595 new air traffic controllers in addition to replacing the 659 that are expected to leave the system through attrition. This net increase above the current replacement levels is a first step in the FAA's plan announced last December to begin training the staff needed to replace future retirees and meet growing demand for air service.

Under the President's plan, the airport improvement program would receive $3 billion. These resources are sufficient to fund construction of all planned new runways, which are the single-most effective way to add capacity. This funding level is robust by historical standards. As recently as 2000, the Airport Grant program was funded at $1.9 billion. In addition to funds in the airport improvement program, airports can meet infrastructure needs through revenues generated from passenger facility charges. Many airports do not take full advantage of this legal authority to charge user fees which FAA estimates could produce an additional $350 million annually for airport development needs. The President's plan also triples funding to $18 million for the Joint Planning and Development Office. The work of this office supports the development of plans for transforming the future of the National air space to address growing capacity needs.

Our maritime network also finds itself in greater demand, both at home and abroad. The President proposes to increase funding for the Maritime Security program by $58 million to $156 million. This increase will fully fund an expanded fleet of 60 ships to provide sealift capacity to carry equipment and supplies to those charged with defending our freedom and expanding liberty.

We are grateful to the Congress for enacting the Department's reorganization proposal, and in accordance with that legislation, we have created two new administrations in place of the Research and Special Programs Administration (RSPA). The new Research and Innovative Technology Administration (RITA) promises to bring new energy and focus to the Department's research efforts and expedite implementation of cross-cutting, innovative transportation technologies. The new Pipeline and Hazardous Materials Safety Administration (PHMSA), has responsibility for the safe and secure transport of hazardous materials throughout the transportation network. The 2006 budget provides $130.8 million for PHMSA's first full year of operations and $39.1 million for RITA. In addition, RITA is expected to receive over $300 million for transportation research conducted on behalf of other agencies on a reimbursable basis.

Finally, I want to highlight the fiscal year 2006 President's budget request for the new Department of Transportation headquarters building project. We are pleased that the Congress has provided $110 million in funding over the last 2 years. Today, construction is well under way and we are requesting your support of $100 million to continue the next phase of this project. Under the terms of our lease, the Department has only until June 2007 to vacate our current building without incurring substantial penalties. For that reason, fiscal year 2006 funding is critical to ensure a timely and smooth transition for the Department's more than 5,600 headquarters employees.

The fiscal year 2006 budget request recognizes that the transportation sector is the workhorse that drives the American economy, providing mobility and accessibility for passengers and freight, supplying millions of jobs, and creating growth-generating revenue. The President's budget reflects a fiscally responsible plan for the Department of Transportation to help America better meet its 21st Century transportation needs. The Federal transportation budget must adequately fund our workforce and our programs despite the continuing funding challenges of national and homeland security needs. President Bush and I are committed to working with the Congress, and with our public- and private-sector partners to ensure that our transportation network can keep America moving confidently into the future.

Thank you again for the opportunity to testify today. I look forward to working closely with all of you, and with the entire Congress, as you consider the fiscal year 2006 President's budget request and I look forward to responding to any questions you may have.

SURFACE TRANSPORTATION REAUTHORIZATION

Senator BOND. Thank you very much, Mr. Secretary. I appreciate your strong statements about the importance of the many transportation issues facing us in this committee and in other committees as well. I appreciate knowing about the national priorities the President has set. I would have to say that Congress has a different view of the importance of the priorities than OMB seems to have.

I would encourage you, as the ranking member suggested, to submit a proposal for the restructuring of Amtrak that would be considered by the appropriate authorizing committee, the Commerce Committee, rather than achieving a death sentence by a cleaver in the appropriations process.

Turning now to highways, I note with interest that the revised reauthorization financing plan assumes $5.6 billion through 2009 in new highway trust fund revenues from reforming the structure of certain fuel tax refunds. When the Senate Finance Committee made this same proposal in 2004, it was criticized as a general fund transfer, violating one of the administration's three principles.

To set the record straight, does this proposal meet with the funding principles, or has the administration recognized that transfers such as this are appropriate?

Secretary MINETA. First of all, we did not change the principles that were laid out and I do not believe that we are violating them. But this was before we had the benefit of substantial discussion about the issue with the leadership and members of the respective committees.

While the goal is the same, in the House Statement of Administration Policy (SAP), we decided that it would be more beneficial for Congress if we provided as much clarity as possible. The SAP clearly states that the President will support up to the $283.9 billion. That is why we are so anxious to see the legislation being considered by the House and Senate brought to completion in conference.

But we do hold to the $283.9 billion, which is a $28 billion increase from where we were last year. Some of that funding, as you know, comes from the ethanol provision, as well as the enforcement of the collection of the sales tax as it relates to the gasoline and fuel taxes.

REVENUE ALIGNED BUDGET AUTHORITY

Senator BOND. Thank you very much, Mr. Secretary.

In the administration's original SAFETEA proposal, there was a modification of the revenue-aligned budget authority, or RABA, which claimed to moderate the wide swings in spending that resulted from the RABA mechanism. But the administration's 2006 budget proposes to eliminate RABA, which some may recall was adopted as a result of what is known, I think, as the Chafee-Bond legislative proposal of 1998. Why has the Department chosen to eliminate that provision?

Secretary MINETA. In TEA21 there was linkage between Highway Trust Fund revenues and expenditures. To the extent that that linkage does not exist, there is no need for the RABA provision.

RABA was effectively eliminated a year or 2 ago. RABA took care of the ups as well as the downs. About 2 years ago we had a real serious downturn in trust fund receipts and RABA was not applied at that time. This year, since there is no linkage between trust fund revenues and expenditures, there is really no need for the RABA adjustment.

Senator BOND. Well, despite my personal interest in and pride in the RABA authorization, I welcome your comments that Federal Highway Trust Fund funding is no longer constrained by Highway Trust Fund receipts. We will take that under consideration in our actions.

Secretary MINETA. The reason being, Mr. Chairman, is that we are drawing deeper into the trust fund balances in order to make sure we have the adequate funds to keep the program——

AIRPORT IMPROVEMENT PROGRAM

Senator BOND. Changing to the other area that is of high priority, the FAA improvement program reductions. Enplanements have rebounded after 9/11, which has renewed interest in the need to add capacity to the national airspace system. Considering that adding runways is one of the most, if not most, effective ways to add capacity, how do you justify a $500 million reduction in the AIP?

Secretary MINETA. Well, we believe that $3 billion for the Airport Improvement Program (AIP) is sufficient to take care of the applications that we have pending before the Department for capacity building, that is runways, taxiways, and tarmacs.

In addition, the airports themselves have available to them passenger facility charges (PFC's), and to that extent, many airports still have not triggered their own ability to finance some of those improvements through the use of PFC's. We believe that about $350 million to $400 million is still available to airports if they were to exercise the use of PFC's.

Senator BOND. Thank you, Mr. Secretary.

Senator Murray.

INTERCITY PASSENGER RAIL SERVICE

Senator MURRAY. Thank you, Mr. Chairman.

Mr. Secretary, during your recent appearances on Amtrak, you often point to the success of the Cascadia Corridor trains that are in the Pacific Northwest. I am also very proud of what we have accomplished in my State with the Cascadia trains.

But your public statements have implied that the State of Washington pays all of the operating costs of that train, and that is just not true. Amtrak still pays the full operating costs of one of the three daily Seattle-Portland trains and a considerable amount of overhead costs for all the Cascadia trains.

Your Amtrak reform proposal assumes that Washington and Oregon would take on 100 percent of the operating costs of these trains, and the only help they would get from the Federal Government is matching grants for capital expenses. Are you aware that Washington State would have to significantly increase its investment just to maintain the status quo if your reform bill was enacted?

Secretary MINETA. We know that there is going to be an added burden on the States through the reform legislation. But we also recognize that there are some 24 or 25 States that do provide passenger rail services. In fact, just yesterday I met with a group that is called States for Passenger Rail, and there are some 24–25 member States in that organization. The vice chair of that program, in fact, is the director of the rail program in Washington State, Ken Uznanski. They are generally supportive of the Amtrak reform proposal that we have before Congress. The group is chaired by the Secretary of Transportation of the State of Wisconsin. We had a very good discussion about why there is need for Amtrak reform. They feel the uncertainty of the present program is something that the States cannot afford to have continue because they go through the roller coaster of whether or not there is going to be Amtrak funding.

Senator MURRAY. That is true, but the States would have to take up considerable costs——

Secretary MINETA. We recognize that there would be——

Senator MURRAY [continuing]. Including Washington State that you——

Secretary MINETA [continuing]. Including Washington State. But Missouri, for instance, is part of the Midwest Regional Rail Initiative, which consists of the States of Michigan, Wisconsin, Minnesota, Illinois, Missouri, Nebraska, Iowa, Indiana, and Ohio.

Senator MURRAY. Right.

Secretary MINETA. We know that there are States that are interested in rail. This way they would be able to get 50 percent capital grants that they are not getting right now.

Senator MURRAY. Well, you know that last year the director of the rail division of the Oregon Department of Transportation testified on your reform bill, and she was not very enthusiastic. She said in her testimony that "the Pacific Northwest is touted because Oregon, Washington, and British Columbia appear to exist as an operating entity, and in fact, there is no formal compact. We exist only because Amtrak exists." It was Amtrak that put the years of effort into bringing those three entities together to start a viable cost-sharing arrangement. Under your reform proposal, States will be required to pay for all of the operating losses of their trains, not just a portion as is now done in the Pacific Northwest.

So tell me, even if you could get the States of the Nation to take on this new obligation, what entity is going to gather all these States together to negotiate those arrangements?

Secretary MINETA. We are in the process of trying to find what is the best way to come to some agreement.

Senator MURRAY. So we do not know that. We do not have an entity today.

So the second question I would have is, how soon would the States be required to put up the funding to cover those operating losses?

Secretary MINETA. Under our reform legislation, we have a transition period of 6 years.

Senator MURRAY. Have you ever considered advocating flexibility for the use of Federal highway funds so the States can use a portion of those dollars to fund the operating losses on Amtrak?

Secretary MINETA. Not to that extent. We have modeled our reform legislation after the way that the Federal Government relates to States and localities on highway programs, transit and aviation. We provide the capital grant funding to local and State governments. The States for Passenger Rail said that they would like to see this program modeled after the highway approach.

Senator MURRAY. Let me ask one last question. I sent you some questions recently, and in your answers to them on Amtrak bankruptcy, you said that “if Amtrak were to seek bankruptcy protection, Amtrak would do well to emulate the airlines and file at a time when it has substantial cash balances.” You estimated that if we wait until the end of this year, Amtrak would only have a cash balance of $75 million, which would only allow the company to operate for a few weeks.

Since you are a member of the Amtrak Board of Directors, you have got to be intimately familiar with its finances. Is it possible that the Amtrak Board of Directors is going to declare bankruptcy sometime in this fiscal year even while Congress continues to work on our budget in the reform bill?

Secretary MINETA. I do not believe so, but let me ask Jeff Rosen, our General Counsel, who is my representative on the board of Amtrak. They will be meeting this week and I will be meeting with them as well.

Mr. ROSEN. Senator, I think the answer to your question is that the Amtrak board is engaged in a strategic planning process, attempting to look at places where costs can be reduced, where revenues might be enhanced, and where there would be some opportunities to improve the operation and financial performance of the company.

Senator MURRAY. Do you foresee them declaring bankruptcy sometime this fiscal year?

Mr. ROSEN. That is not the object or intention. Obviously, everybody has to adapt as they go, but that is not the current plan.

Senator MURRAY. Well, Mr. Chairman, I hope at some point we can have a hearing on Amtrak so we can hear about the financial situation from the Amtrak Board of Directors.

Senator BOND. I think one may be needed in the Commerce Committee as well.

Senator Stevens.

TRANSPORTATION INFRASTRUCTURE IN ALASKA

Senator STEVENS. Mr. Secretary, I find it strange we meet today on the day we are probably going to consider the question of whether or not we will open up the North Slope of Alaska for oil. I note that the price of aviation fuel has gone up three times since 1999 and that the problem really with the airline industry is that it is just being put out of business because of high energy prices. A $1 increase in the price of fuel, I am told, for aviation costs 5,300 airline jobs. It is interesting that some people here criticize the administration for its budget when they refuse to recognize the need for purchasing as much oil as we can at home. The export of dollars to OPEC is just a hemorrhage.

Today they meet in Iran. OPEC meets in Iran today. The estimates of some experts say by the end of the year it will be $80 a barrel. Today it is $54.95 a barrel.

Now, I think it is high time some people start thinking about what causes the problems of transportation, particularly aviation. I would hope that you and the administration would start moving in on the question of the cost to the system by forever having these increased costs of buying so much oil abroad. It will be 60 percent by the end of the year they tell me. We will be buying 60 percent of our oil abroad, primarily from unstable countries that are today meeting in Iran. I cannot think of anything that is more difficult for the transportation industry than to face the costs of fuel.

I have a question, though, and that relates to my problem about where I live. We have, as you know, a State that has half the coastline of the United States. Because of the withdrawals that were made by President Carter in 1980, we cannot build highways, north or south or east or west. That was the total plan at the time, was to prevent Alaska from being able to have ground transportation. We have only air transportation and that by sea. We have been able to build air terminals, thanks to a long process, but we now have some 230 small airports, most of them maintained by the State, but some of them by the Federal Government. Our reliance on water transportation increases now as freight gets heavier going into the rural communities. I find we just do not have docks. We do not have the capability to bring this equipment ashore in these small villages and small towns.

I have been trying to find a way to develop small dock projects, and I want to urge your assistance to see if we cannot find some way to do this. We created the Denali Commission, formed after the Appalachian Commission that Senator Byrd started. We think that if we had some way to take funds and allow the Denali Commission to start building docks, we could cut the cost of delivery of freight to those small villages in half.

So I am not asking a question. I am just making a plea that you assign some of your people to start working with us. How can we get docks for the small villages along the rivers and along the sea that have never had docks? They have had to load their stuff in small boats, 30-foot boats. That is just not possible to get it in. The airports are small airports. They are flying 19-passenger planes in those areas and they cannot carry freight. The only freight they get is really by water, and it is very limited as to what we can do to help them modernize until we can freight ashore.

So, my friend, I just plead with you that you help me find some way to meet the transportation needs of rural Alaska.

Thank you, Mr. Chairman.

Secretary MINETA. Mr. Chairman, we have AIR21 and now Vision 100 related to aviation. We have had TEA21 related to surface transportation. Right now we are putting together a program called SEA21 for maritime transportation. This is a way of dealing with short sea shipping, using smaller ports and looking at the inland waterway system of the United States to see what we can do to enhance the movement of people and goods through the water system that we have. It is used extensively in Europe. You can travel all the way from Rotterdam to the Black Sea on barges or even on passenger-type vessels. Again, we feel that the potential is here. So we are now looking at SEA21. I am quite sure that that would fit in very well with what you were envisioning.

Senator STEVENS. Good. We look forward to working with you. Your friend and mine, the Congressman from Alaska, was a riverboat captain. We used to have riverboats but we do not have them any longer because they are not constructed any longer. We may have to look to the basic concept of acquiring new types of boats that can be used in the rivers of Alaska, if you want to go that way. But I thank you for your response.

Senator BOND. Thank you very much, Senator Stevens.

Mr. Secretary, we appreciate your comments about the importance of inland waterways transportation, and we will need your help on a little bill called WRDA.

Senator Byrd.

INTERCITY PASSENGER RAIL SERVICE

Senator BYRD. Thank you, Mr. Chairman. Senator Stevens, as Alaska's Senator of the 20th Century, we will get it done, and we will do what we can to help get those little ports.

Regarding one of your so-called reform proposals, how did you arrive at your plan to have the States, Mr. Secretary, rather than the Federal Government absorb all of the operating costs on Amtrak? Why do you think that the States collectively are in a better position to fund the operating losses for Amtrak than the Federal Government?

I notice in The Washington Post of March 15, these words, which I excerpt from the article. "As Northern Virginia drivers spend more time in their cars on bottlenecked highways, money to expand the State's road and transit network is disappearing fast, transportation experts said yesterday. The shortage is so serious that by 2014, Virginia will have trouble matching Federal transportation grants, jeopardizing funding for construction and maintenance, a top State official told a gathering of the region's transportation leaders. And by 2018, so much of the State's transportation fund will have been shifted to maintenance and general spending that money to build new roads will be nonexistent." So this is the condition that the State and local subdivisions and communities are being placed in.

So, let me say again, Mr. Secretary, how did you arrive at your plan to have the States, rather than the Federal Government, absorb all of the operating costs on Amtrak trains?

Secretary MINETA. The basis of the reform measure was how we currently approach highway programs, transit, and aviation. In every one of those cases, the operating costs of those systems are borne by States and localities. The Federal Government does participate in funding the capital infrastructure costs. We felt that Amtrak should not be treated any differently than other modes of transportation. That was the basis for our using the States as the way of structuring the reform on Amtrak.

Yesterday I met with the group States for Passenger Rail. One of the people participating in that meeting was a woman by the name of Karen Ray who is the director of rail for the Commonwealth of Virginia. They already have Virginia Railway Express (VRE) that goes from Fredericksburg to the District of Columbia, but they are also planning on rail from Richmond to the tidal area of Roanoke and Hampton Roads. They are also thinking of passenger rail service from Bristol, Virginia all the way to Washington, DC. They already have an agreement between Virginia and North Carolina, and that will be part of a system that will eventually go through South Carolina and on to Georgia. The States recognize the need for rail as an alternative form, and I think that we are not out of step in terms of the initiative that the States are already taking on their own.

Senator BYRD. Mr. Secretary, I say most respectfully that you would make a fine U.S. Senator if we are able to continue to filibuster, if they do not stop us.

But you still have not answered my question. I listened very closely. Why do you think, given the States' financial situation, that they are in a position to start absorbing the cost of Amtrak service?

Secretary MINETA. Again, I would say that the States are taking the initiative to promote their own rail services. Right now they are paying for it fully on their own. This way we would participate 50–50 with them on their capital costs. They are already absorbing the operating costs right now. I would assume that that would continue in the future and that we would participate with them on the capital physical infrastructure costs.

Senator BYRD. Thank you, Mr. Chairman. My time is up.

Senator BOND. Thank you, Senator Byrd.

Senator Domenici.

HIGHWAY SAFETY

Senator DOMENICI. Mr. Secretary, first, I am hopeful that I will be here when the meeting ends because I have a matter pertaining to how your office is handling certain Federal events in my State, and I would rather state those to you privately. If I miss you this morning at the end of the meeting because I have left, I would appreciate it if you would note that I need a call from you about something rather urgent.

Secretary MINETA. Great.

Senator DOMENICI. Mr. Secretary, you mentioned that deaths were down on the highways. Could you state for the record how many deaths there are, even though they are down? How many people die on the highways?

Secretary MINETA. The total is about 42,600, and this is down from over 43,000 the year before. We have not only had a drop in the total number of deaths, but we also have had a drop in the fatal accident rate even given the increase in vehicle miles traveled.

Senator DOMENICI. Well, I did not come here prepared to talk about that, but it is amazing. In other situations that occur in the United States, McDonald's and their hamburgers, whatever, when we talk about obesity and death, we get all worked up over 300 or 400 deaths, and we have 42,000 on the highways. Yet, what kind of advertisements do you see by the automobile manufacturers? Have you seen very many yet that do not emphasize how fast the cars can take off, how fast they can go? It is amazing to me, with this kind of thing happening on our highways, why we are promoting speed as a reason for buying cars. That is just my view. It is nobody else's.

INTERCITY PASSENGER RAIL SERVICE REFORM

You also mentioned that Amtrak is not eliminated, rather it is held in abeyance pending reforms. You know, I have been hearing that for so long. Would you tick off three or four reforms that you think ought to be made? I do not want you to use a lot of time, but what are the reforms?

Secretary MINETA. That we are proposing under our bill?

Senator DOMENICI. No. You are saying Amtrak must make reforms to continue the operating subsidy. What kind of reforms?

Secretary MINETA. I think there are a number of cost savings that they can——

Senator DOMENICI. What are they?

Secretary MINETA. For instance, dining car services.

Senator DOMENICI. Okay, that is one.

Secretary MINETA. That costs something like $84 million a year. I think again this is an area in which they ought to be taking some action.

Senator DOMENICI. Well that is not very much.

Secretary MINETA. It is like anything else. Everything does add up to a bottom line.

Senator DOMENICI. Mr. Secretary, are the railroads, including Amtrak, still immune from workmen's compensation laws and they apply their own liability under straight tort liability for injuries?

Secretary MINETA. I think that is under a different kind of law. There are special laws that apply to——

Senator DOMENICI. I cannot help but believe that that would be a rather expensive liability situation. I would assume that might be one of the reforms being contemplated. Is that correct? Could you answer it, sir?

Mr. ROSEN. Senator, that is not a piece of the reform legislation that the administration sent up in 2003, but you are correct that it is an expensive piece of the puzzle for railroads.

Senator DOMENICI. Why is it not a suggested reform? Are we scared of somebody?

Mr. ROSEN. Not that I know of, but I think that may be a useful suggestion for us to look at.

Senator DOMENICI. I think it is because you are scared of somebody. You are scared of the unions. That is why.

I noticed the other day there was an accident on a railroad. The story said that the cars tipped mildly, did not even turn or anything. Three days later, 12 railroad employees filed suits for injuries not under workmen's comp, but under straight tort liability. Who knows how much those cases were settled for. You know about that, Mr. Chairman. That is not workmen's comp. Just as if somebody was negligent, you recover under straight liability like anybody else in an automobile accident. That is a pretty costly item.

Well, I did not really come to talk about that. I came here to talk about two things.

INDIAN RESERVATION ROADS

Mr. Secretary, I have been part, for the last 10 years, of seeing to it that the Indian people of the United States get some roadway money. We passed three sets of legislation with each highway bill, setting aside a small portion of highway taxes for Indian roads. I know you cannot right here, but could you, for the record, tell us how that program is going, how much money has been put out each year by the Department, through the BIA or otherwise, under that piece of the law which sets aside a portion of the highway funds for Indian roads?

Secretary MINETA. We will respond for the record.

[The information follows:]

On July 19, 2004, after approximately 5 years of negotiated rulemaking between representatives of Indian tribes and the Federal Government, the Indian Reservation Roads (IRR) Program Final Rule (25 CFR Part 170) was published. This rule established policies and procedures governing the IRR Program. It expanded transportation activities available to the tribes and provided guidance for planning, designing, constructing, and maintaining transportation facilities. It also established an IRR Coordinating Committee of 12 tribal representatives to provide input and recommendations to the Bureau of Indian Affairs (BIA) and the Federal Highway Administration (FHWA) on the IRR program.

In addition, the Final Rule established a funding distribution methodology for IRR Program funds. As a result part of the negotiated rulemaking, the entire IRR inventory of 63,000 miles contribute towards the amount of IRR Program funds the tribes receive. The limitation on the growth of the inventory has been eliminated.

IRR Program Funds are distributed by tribal allocation. The formula methodology used to determine each tribe's allocation is composed of three factors. The largest contributing factor is a tribe's "cost to construct," which contributes 50 percent. A tribe's "vehicle miles traveled" (VMT) contributes 30 percent, while its "population" contributes the remaining 20 percent. Each tribe's allocation is then calculated by its percentage of these factors as compared to the nationwide total. However, the actual distribution of the funds has been affected by the different continuing resolutions and extensions to the Transportation Equity Act for the 21st Century (TEA21).

The following funding amount has been made available for the Indian Reservation Roads Program during the past four highway authorizations:

—Surface Transportation Assistance Act of 1982 (STAA): $418 million;

—Surface Transportation and Uniform Relocation Assistance Act of 1987 (STURAA): $400 million;

—Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA): $1.069 billion; and

—TEA21: $1.47 billion.

The current annual funding level is $275 million for the IRR program. After application of statutory and regulatory takedowns, the available funds are re-allocated from FHWA to the BIA, which is the only agency that receives these funds. The BIA then distributes the funds either directly to the tribes through self-governance agreements/compacts or to the BIA Regional Offices. If the funds are distributed to the BIA Regional Offices, they in turn provide the funds to the tribes through Indian Self Determination Education Assistance Act (Public Law 93–638) contracts, Buy Indian contracts, or perform the work themselves on behalf of a tribe. It should be noted that the Indian Reservation Roads Bridge Program (IRRBP), established under TEA21, has dedicated $13 million of each year's IRR Program funds to the rehabilitation or replacement of deficient bridges within the IRR System. There are over 4,640 bridges on the IRR System. Approximately 1,050 of these are deficient. To date, these funds have been utilized for work on over 125 IRR bridges.

Finally, as a result of TEA21, FHWA developed by rule requirements and guidelines for three new management systems to assist BIA and tribal governments in identifying and prioritizing quality and quantifiable projects. In addition, FHWA, BIA, and tribal governments are working together both to develop an integrated transportation planning process to help the tribes work with the State and metropolitan planning organizations, and to improve their ability to facilitate long range advance funding for projects. There has also been considerable success with the tribes to develop safety audits and initiatives in cooperation with State and local governments.

Senator DOMENICI. Will you also give us an overview, through your experts, on where we are, how much are we accomplishing, how much do we have still to get done? That would be an interesting thing for us. That is a big number now. We have got it up to almost $300 million a year. It will be more in the next bill.

[The information follows:]

One of the greatest single recent accomplishments of this program was the publication of the Indian Reservation Roads (IRR) Program final rule (25 CFR Part 170). This accomplishment involved 5 years of negotiated rulemaking between representatives of Indian tribes and the Federal Government and expands transportation activities available to the tribes by providing guidance for planning, designing, constructing, and maintaining transportation facilities.

Over the 7 year period of fiscal year 1998 through fiscal year 2004, approximately $1.745 billion has been made available for the IRR Program. These funds have been spent on improving thousands of miles of IRR facilities across the country as well as rehabilitating or replacing 125 IRR bridges. However, the backlog of needs for the IRR Program remains high at $15.7 billion as a majority of the IRR road mileage remains in fair to poor condition and more than 1,000 bridges are still deemed deficient.

Another accomplishment of the program is that it has enabled the tribes to administer their own projects. Today tribes, through either self-governance compacts or Indian Self Determination Education Assistance Act (Public Law 93–638) self-determination contracts with the Bureau of Indian Affairs (BIA), administer approximately 50 percent of the funding made available under this program. This has provided local employment for tribal forces and an opportunity for significant local resources to be used.

CORRIDORS AND BORDERS PROGRAM

Senator DOMENICI. My last question has to do with money that goes to the so-called border. We have the Borders and Corridors program. It was instituted, as you know, to alleviate problems along the borders that need upgrades on existing highway structures where we have a lot of traffic between Mexico and America and Canada and America. Would you provide the committee with an update on the Borders and Corridors program, which is important to many States, including mine? Would you also tell us if it has had any positive effects, and then where do you think the program is going? By that, I mean what are the problems out there that you think might be addressed.

Senator BOND. Thank you very much, Senator Domenici. We will ask those questions for the record.

Secretary MINETA. We will respond to that.

[The information follows:]

The Federal Highway Administration (FHWA) prepared a report on the first 5 years (fiscal year 1999-fiscal year 2003) of the program under TEA21. This report, The National Corridor Planning and Development and Coordinated Border Infrastructure Program (NCPD/CBI): History, Evaluation and Results, found that during the first few years of the program, the demand for grants under the program have outpaced the available funds. Through the years, most of the funds appropriated for the program have become designated by the Congress, and most of those funds have been designated for corridor projects. Five States, West Virginia, Texas, Kentucky, California, and Washington accounted for over 40 percent of the awards in the first 5 years of the program.

Many projects are longer term, so their benefits have not been assessed during the short life of this program. Also, many projects are more costly than reflected in the grant allocation, and require contributions from other sources. However, anecdotal evidence from some recent success stories in Texas, New York, California, and Washington State indicates that the program has some very positive effects such as alleviating congestion, improving highway/railroad crossing safety, and expediting project implementation. These success stories are highlighted in the report, and a brief narrative of each follows:

World Trade Bridge, Laredo,Texas

Mexico-U.S. trade increased in the 1980's and with it the traffic on the downtown Laredo Juarez-Lincoln Bridge. By the end of this decade, the State of Texas, the City of Laredo, the Mexican government, the City of Nuevo Laredo and others were discussing how to address this situation. In 1991, detailed coordination began for a new bridge outside the central business district that would carry commercial traffic. By 1993, projects were placed on the Texas multi-year transportation improvement program and in 1995 a comprehensive funding agreement had been reached. The total cost of the new bridge and related improvements was about $100 million.

The NCPD/CBI contributed about $6 million of this total through one of the fiscal year 1999 awards.

The new bridge opened on April 15, 2000. Downtown back ups disappeared and truck traffic was successfully diverted to the new bridge. Substantial job growth occurred in fiscal year 2001 and seems clearly related to the business opportunities created by the new bridge.

Commercial Vehicle Processing Center, Buffalo, New York

For a number of years, the Buffalo and Fort Erie Public Bridge Authority had been seeking to improve the operation of the border crossing at the Peace Bridge. In the late 1990's, a user group consisting of trucking associations, commercial carriers, brokers and the U.S. Customs Service developed ideas to meet this objective. One method that seemed promising was to develop procedures and train personnel to operate a Commercial Vehicle Processing Center (CVPC) on the Canadian side of the border. The CVPC would assist truck drivers with incomplete paperwork prior to the vehicles entering the inspection queue. Fewer vehicles failing the primary inspection would mean less congestion on the bridge. In fiscal year 1999, the FHWA awarded about $1 million in NCPD/CBI funds for developing procedures and training personnel for the CVPC. The Authority immediately began implementing this project and the CVPC opened in late fiscal year 1999. Within the first year, the number of vehicles failing the primary inspection fell from 36 percent to 15 percent. Border agencies and the U.S. Customs Service have recognized the CVPC as a success.

Freight Action Strategies Corridor (FAST), Seattle Metropolitan Area, Washington State

Beginning in 1994, local, State, port authority, private sector and Federal officials began developing plans to improve highway/railroad crossings and port access highways in the vicinity of the ports of Everett, Seattle and Tacoma, Washington. In 1997, a phased implementation plan was developed and in fiscal year 1999, the FAST corridor received the first of a number of awards from the NCPD/CBI program. From fiscal year 1999 through fiscal year 2003, FAST was awarded $32,000,000 in NCPD/CBI funds, including funds selected by the U.S. Department of Transportation (DOT) and funds designated by the Congress. The FAST project also received funds outside the NCPD/CBI Program, in Section 1602 of TEA21, in Section 378 of the fiscal year 2001 DOT Appropriations Act, and in Section 330 of Division I of the Consolidated Appropriations Act of 2003. The first complete grade separation project was completed in fiscal year 2001 and by January 2003, ten such projects were complete or nearly so. As projects have been completed, traffic backups disappeared, safety improved and railroad efficiency increased. Because a high percentage of jobs in the Seattle metropolitan area (as many as 1 in 3) are tied to international trade, systematic improvement of port access is seen as vital to the economic well being of the area.

Alameda Corridor East (ACE), San Gabriel Valley, California

Similar to the FAST program, local, regional, State and private sector parties have been working together since the late 1990's to improve highway/railroad grade crossings (including many grade separation projects) in an East-West corridor with high railroad traffic serving the Port of Los Angeles/Long Beach. The ACE corridor received funds from Section 1602 of TEA21 and corridor officials credit this with jumpstarting the ACE program. The same officials state that, in the first phase of the program, $3 have been leveraged for every Federal $1. The ACE corridor first received a NCPD/CBI award in fiscal year 2000 and subsequently received awards in fiscal year 2001, fiscal year 2002 and fiscal year 2003. These awards totaled $9,019,000. The first projects have resulted in less congestion, improved safety, and reduced emissions. This latter result is quite important because of the well-known air quality problems in the Los Angeles region. Without these improvements, increasing rail corridor traffic would worsen the congestion, safety and air quality problems as well as restrict economic development.

The administration has proposed to reauthorize the Corridors and Borders program. Under the administration's proposal, the corridor program would become a Multi-State Corridor Planning Program. The purpose of this program is to support and encourage transportation planning from a broader perspective, transcending traditional State and modal boundaries, to meet evolving freight and passenger transportation needs of the 21st Century. Similarly, the border program would become a Border Planning, Operations, and Technology Program. The purpose of this program is to focus on improvement to bi-national transportation planning, operations, efficiency, information exchange, safety, and security for the United States borders with Canada and Mexico.

Senator BOND. Senator Bennett.

INTERCITY PASSENGER RAIL SERVICE

Senator BENNETT. Thank you, Mr. Chairman.

Mr. Rosen, I had not realized you were here when I extended the invitation through the Secretary to you. I apologize. I extend it to you personally. We would be happy to entertain you in Utah in grand Olympic style.

This is a segue, I think, into this discussion about Amtrak because what we are talking about here in Utah is commuter rail and commuter rail from Salt Lake City north. It has nothing whatever to do with Amtrak. It has to do with the contribution of the State and the Federal Transit Administration.

I think we get hung up on Amtrak as some kind of holy grail that is the only solution to intercity rail traffic. I will be the first to say that we need intercity rail traffic along the western front of the Wasatch Mountains in Salt Lake County north of Davis County and into Weber County, but I frankly do not want Amtrak to have anything to do with it. I want it to be run by the Utah authorities that understand the needs and understand the situation.

If it would be of any help in resolving the Amtrak budgetary problem, I am happy to offer up Amtrak service in the State of Utah for immediate cancellation. This is not the Northeast Corridor. This is not an area between Washington and Boston where the trains carry as many people as the airplanes do. We have Amtrak service into Salt Lake City that arrives—I know this because I have met an Amtrak train where a family friend was coming in by train—at 2:30 in the morning. I think it arrives 3 whole days every week. On the occasion where the family friend got off the train, there were probably four or five other people that got off with her. To be spending the kind of subsidy that we are spending to maintain that sort of service, which is totally unsatisfactory, completely disruptive of the very few people who use it, when the money should be going into places where there is a legitimate need for intercity rail traffic is silly.

So if you want an elected official who is willing to sacrifice his Amtrak service for the greater good of the Nation and help hold down the deficit on Amtrak, I offer my State. I have not consulted with the mayor and I have not consulted with the Governor, and I do not know how much political trouble it is going to get me in. But knowing the number of passengers that disembark from Amtrak on those 3 days a week when it shows up, I do not think I am in much political trouble. We could handle that amount of passengers numerically with a single flight of a single 767 once a week, and all of the transportation problems would be taken care of. Now, I realize that is an oversimplification.

I am a strong supporter of Amtrak. As the Secretary knows, I was in the Department of Transportation and I was the lobbyist for the Department of Transportation that convinced the Congress to create Amtrak. I have got a nice certificate signed by John Volpe with a big award, the Secretary's award for outstanding achievement, for what I did to help create Amtrak. And I believe in Amtrak.

But I think the primary function here is that if you are going to have mass transit, you have to have a mass that needs to be transited. And for a very large percentage of the Amtrak route system, you do not have the mass that needs to be transited. The money should go getting people from Washington to Baltimore, getting Senator Biden back home to Delaware and Senator Specter back home to Pennsylvania. And in the areas in the Cascades where there is a mass to be transited, let us transit them by rail, and let us put the Federal money in to make sure that system works. But let us not, for romantic purposes, continue to talk about a nationwide rail network that some day we are going to need and pour money into it. We have been doing it for over 30 years. I left the Department of Transportation in 1970, and here we are in 2005.

The promise I solemnly made to the Congress, as I lobbied that bill through, that Amtrak would require Federal subsidies for only 3 years, has long since been broken by every administration from the Nixon administration, in which this thing was created, on down. And it is time to get serious about saying let us put the money where the passengers are and let the romance go into the novels that people can read on the airplanes as they are flying over the long distances.

Thank you, Mr. Secretary.

Senator BOND. Thank you, Senator Bennett. Confession is good for the soul.

We appreciate that purging of past sins.

Senator Dorgan.

Senator DORGAN. Well, Mr. Chairman, I am pleased I was here for that confession.

But let me be quick to say I would not offer up my State with respect to its Amtrak service, and let me tell you why. I do not know the specifics, and I am not critical of Senator Bennett's position or statement with respect to Utah.

We have the Empire Builder that comes through North Dakota on the northern route. It connects Chicago to Seattle. We have 80,000 to 90,000 people get on and off in North Dakota. It is an important adjunct to our transportation system. It is very important. I happen to believe that it is worthy for us to subsidize Amtrak service. I just flat out believe that subsidizing rail passenger service is something that is all right with me. In terms of the set of priorities of investments, I think that is a good thing to do.

Now, I do not see Amtrak as part of mass transit. That is perhaps where Senator Bennett and I disagree. Senator Bennett several times talked about mass transit. I do support mass transit. I come from a rural area. We do not have mass transit, but I support mass transit because our major cities need mass transit and the investment and the funds to advance mass transit. But Amtrak is not in my judgment mass transit.

I really feel strongly that we need to maintain a national rail passenger system. If we do what the administration suggests we do, we will have Amtrak service from Boston to Florida and the income stream from the masses who would use that service will perhaps justify, I am guessing, that service and perhaps even not require subsidy.

We subsidize every single form of transportation. Every form of transportation has some embedded Federal subsidy. So I am perfectly comfortable believing that a national rail passenger system is something we should subsidize.

Now, Senator Bennett does make a point. There may be some circumstances where you ought not stop or you ought not serve if there is nobody there.

But I am very disappointed, Secretary Mineta, once again that the administration believes that Amtrak as a national system is somehow unworthy. I really think that is the wrong approach and hope that those of us in Congress who will likely have an opportunity to vote on that in the coming days will be able to overturn that recommendation.

I would like to ask a question.

I do not mean at all to be critical of Senator Bennett. That was not my intention.

Senator BENNETT. Feel free.

ESSENTIAL AIR SERVICE PROGRAM

Senator DORGAN. Let me ask about the Essential Air Service program because there is a proposed 50 percent cut in the funding for the Essential Air Service program. You may have already answered this question. Can you give me the rationale for that? Because that also plays into the point that Senator Byrd made, I think, that this is a budget that is very punitive to rural areas.

Secretary MINETA. First of all, the total budget that we got, $59.5 billion, is shoehorned in as part of the overall Federal budget. The President outlined three priorities that he had in developing the budget: fiscal restraint, national defense, and homeland security. As OMB was putting the budget together following these three priorities, then everyone else either had a plus or a minus. Even with our $59.5 billion budget, we are still close to, I believe, a 2 percent increase from the previous year's request.

So one of the programs we had to shoehorn in, as you have mentioned, is Essential Air Service. We have proposed categories of airports that would get Essential Air Service funds based on how close they are to a large, medium, or small hub airport, or a non-hub airport that has jet service.

So we looked at how many airports fall into those categories and how much money we have, and then tried to figure out how to set the criteria for the program. In doing that, and given the amount of money we had for Essential Air Service, we are trying to maintain service to those airports, but under a different set of criteria.

Senator DORGAN. Mr. Secretary, my time is about up——

Senator BOND. Have one on me.

Senator DORGAN. All right. Thank you. A generous new chairman.

Senator BOND. Everybody else is taking one, so you might as well.

TRANSPORTATION CONNECTIVITY

Senator DORGAN. And congratulations, by the way, to you.

If we were to build the interstate highway today, I assume there would be some people that would say, well, how on earth can you justify building four lanes across North Dakota, connecting Fargo to Beach, North Dakota from the east to the west because out near Medora, North Dakota and Buffalo Gap and Alsen, there are not a lot of people out there and so not as much traffic. But, of course, as you know, connecting a four lane across North Dakota connects Minneapolis to Seattle, Chicago to Seattle. So the same is true with other forms of transportation. We can either decide this is a country or this is a series of very big cities, the income from which will support robust, aggressive transportation systems for people who live in big cities in the masses, and the heck with the rest of the country.

That is why I raise these questions about Amtrak, about Essential Air Service and believe that these investments more tend towards saying: where can you make a profit here? Where are the dollars and cents with respect to profitability? And with respect to transportation, whether it is AIP or EAS or Amtrak, sometimes you can know the cost of everything and the value of nothing, as some say. So there is value here in some of these decisions to make sure that our transportation systems help everybody in the country, connect everybody in the country.

Secretary MINETA. That was the purpose of the national defense highway program. One of the criteria was a four-lane highway. Originally the program was based on interconnectivity of the country, and the highway system was basically an east-west system. It was not until the Intermodal Surface Transportation Efficiency Act (ISTEA) in 1991 that we went north-south with the national highway system.

Today we are not talking as much about connectivity as we are congestion relief and increasing capacity as far as highways are concerned. We are trying to do the same thing in other modes of transportation, whether it is transit or aviation or, as I mentioned earlier, maritime in terms of inland waterways and short-sea shipping. We want to relieve some of the traffic that is on the highway and move it to water or to air or to other modes of transportation. It is not a one-system-fits-all.

Senator DORGAN. I would just finally observe there will never be congestion on the Gladstone intersection of I–94 in western North Dakota. But although congestion is not our issue, I understand congestion exists elsewhere. Access and capability is the issue in rural America, and access to reasonable transportation opportunity is just as critical for somebody that lives in a town of 900 people with no bus service and no other access as congestion is for somebody that lives in a city of 4 million people where they have parking lots.

Secretary MINETA. Absolutely. You were there in 1991 when Congress enacted ISTEA and we changed the name of the Urban Mass Transit Administration to the Federal Transit Administration because there were rural needs that had to be met by transit as well. We recognize the needs of rural communities, whether it be in air or transit or highways, and we have various parameters to meet the needs of the total country, regardless of the mode of transportation.

In the case of the Essential Air Service program, we had to build the criteria around the available funding in order to continue to serve those communities.

Senator DORGAN. Mr. Chairman, thank you very much.

CONDITIONS AND PERFORMANCE REPORT

Senator BOND. Thank you very much, Senator Dorgan.

Mr. Secretary, I mentioned in my opening statement your Department's Conditions and Performance Report said that Federal investment must increase by 17 percent just to maintain the current system, and to improve the system would require 65 percent more than currently invested. I would like to know what specific plans, both for the short term and long term, are being looked at by the Department to address the shortfall and ensure adequate funding to reduce congestion, meet our economic needs, and lessen the senseless loss of life, estimated to be one out of three traffic fatalities nationally—in my State it is higher—caused by inadequate highways for the traffic that they hold. This is a question of life and death in my State. How does the Department propose to meet it?

Secretary MINETA. First, let me address the Conditions and Performance (C&P) Report. The needs that are talked about in the report are not just Federal needs. They also include the requirements and the responsibilities that State and local governments have to maintain their road structure. So, the C&P report does not identify only the U.S. Department of Transportation's financial requirements.

Let me deal with the safety issue.

FUNDING FOR FEDERAL HIGHWAY PROGRAMS

Senator BOND. Let me just point out one thing. I understand that the States provide—at least my State provides—a lot more money than the Federal Government does, but I understood your Conditions and Performance Report to estimate the Federal investment. Federal investment alone must increase by 17 percent and improving the system would require 65 percent more.

Secretary MINETA. I was a co-author of ISTEA and the one who helped put together the SAFETEA proposal that the administration submitted to Congress. I was not here for TEA21. SAFETEA is a 35 percent increase over TEA21. Even in this year's budget, the administration is requesting $28 billion more for SAFETEA than we did last year in the 2005 budget. So we recognize the need for an increase in highway funding. I believe we were trying to meet the needs that we see facing us today and into the future during the 6-year authorization period.

The second point on safety. When I was briefing the President on SAFETEA in 2002, he looked at the 43,000 highway fatalities figure and he said that we have got to get that down. We have put together a multi-pronged program in the Department of Transportation and in SAFETEA to drive the number of fatalities and the fatality rate down.

Apart from SAFETEA, we think we have already turned the corner, given the programs in the National Highway Traffic Safety Administration and in the Federal Motor Carrier Safety Administration. As I said earlier, our annual traffic fatalities are about 42,600, whereas in 2002 they exceeded 43,000. So we have turned the corner.

Senator BOND. Mr. Secretary, I know those figures but in my State we are killing people on two-lane highways that have traffic that everybody recognizes requires four lanes. We do not have it. So I would just ask you to consider that because we are not solving that problem.

Secretary MINETA. Well, we are and in fact——

Senator BOND. The Federal role is not doing it.

Secretary MINETA. In fact, we have been asking Missouri to adopt the primary seat belt law. We know that primary seat belt laws have a very big impact on traffic deaths.

INTERCITY PASSENGER RAIL SERVICE

Senator BOND. All right. I am just about out of time.

Let me just ask you on Amtrak. We have talked about that. Senator Bennett confessed to his role in it. What is the administration going to provide in terms of reform for Amtrak? Are you going to include options for State or private passenger rail, competition with Amtrak? When do you expect to get a reform proposal up, and how is that going to impact the appropriations death sentence for Amtrak included in this budget?

Secretary MINETA. Mr. Chairman, our original proposal was submitted in July of 2003. We had no committee action on the proposal in 2004 so far in 2005. It was decided by OMB and DOT that in order to get action by the Congress, we would request zero funding for Amtrak. I think that has gotten everyone's attention. In fact, that is how I think I got this black and blue mark.

We will submit, probably within 1 week or 2, essentially the same legislation that we submitted in July of 2003, with some refinements in terms of what we ought to be doing.

Senator BOND. Thank you very much, Mr. Secretary.

Senator Murray.

FAA SAFETY INSPECTORS

Senator MURRAY. Thank you, Mr. Chairman.

Mr. Secretary, in 1996 the FAA significantly increased the number of aviation safety inspectors in light of that 90-day safety review that was conducted in the aftermath of the ValuJet crash in Florida. Unfortunately, the number of inspectors has been consistently below the standard of 3,297 that was set in that review. In fact, Mr. Secretary, I believe that the National Civil Aviation Review Commission that you chaired called for even higher inspector levels.

I understand that the FAA may lose as many as 250 inspectors this year through attrition and that the agency has no intention to back-fill for these positions. That really concerns me. Why are you not filling the vacancies for these critical safety positions?

Secretary MINETA. As I recall, we are increasing the number of safety inspectors by 197.

Senator MURRAY. We are losing 250 this year for retirements.

Secretary MINETA. I am not sure of the number that we are losing, but I know that given the foreign repair station issue and a number of other things that are coming up, we are increasing the number of aviation safety inspectors. I misspoke. It was not 197. It was 97.

Senator MURRAY. Right, at a time when we are losing 250.

Secretary MINETA. I will check on that.

[The information follows:]

During fiscal year 2005, staffing for FAA's Aviation Safety line of business (Regulation and Certification) will decrease from 6,429 to 6,187 due primarily to attrition, a net loss of 302 staff, including 256 safety inspectors and engineers. This decrease, which does not include air traffic controllers, is partially offset by a requested fiscal year 2006 budget increase of 97 safety inspectors and engineers to: (1) improve oversight of domestic and foreign repair stations; (2) oversee FAA's Air Traffic Organization (ATO); (3) establish a new safety oversight office in China; and (4) restore a small portion of the staff lost in fiscal year 2005. Safety will always come first, and the FAA will not reduce its oversight of the air carriers. Instead, the agency will reduce the number of staff who certify new products, and its aviation medicine and regulatory offices.

Senator MURRAY. I think you would agree with me when the airlines are struggling financially and we are outsourcing an increasing portion of the maintenance work, replacing these inspectors should be at the top of the priority list. So if you could get back to me on when you are going to fill those vacancies.

Secretary MINETA. Given the financial condition of the airlines, I told the FAA that I want to make sure that the inspection workforce is checking all of the maintenance records. I had a hearing, I think it was in 1988, on what we call pencil whipping, where inspectors were saying what they were doing, but that was not the case.

Senator MURRAY. Okay. Well, I am very concerned about that so I would like to hear back from you.

RAILROAD SAFETY

On another area—and, Mr. Chairman, you talked about some of the rail safety programs and concerns, and I hope that we can have a hearing on that at some point. But we do know that there were two very serious railroad crashes that resulted in several fatalities in January just a few months ago, one in South Carolina and one in California. Those crashes came right on the heels of an investigation by your Inspector General into whether your Federal Railroad Administration was exercising sufficient safety oversight of the railroads. I want to know from you what specific actions you are taking to step up enforcement.

[The information follows:]

The Federal Railroad Administration (FRA) enforces railroad safety laws and regulations vigorously. To accomplish this, FRA uses a variety of enforcement tools, including civil penalties, emergency orders, compliance orders, compliance agreements, individual liability, and criminal enforcement. FRA is accelerating development of a new National Inspection Plan that will help to deploy its inspection force of about 415, supplemented by 160 State inspectors, to the highest value safety targets. FRA is also reviewing extensive safety data and focusing inspections to achieve the maximum safety benefits. FRA is targeting its current efforts toward the leading causes of train accidents: human factors and track. On human factors, FRA is considering regulatory action addressing the leading causes of accidents. On track, FRA is continuing aggressive, focused enforcement efforts and conducting research on technologies that will assist in detecting hidden track defects.

Senator MURRAY. And I also want to press the fact that a number of press reports suggested that the FRA has been too close to the industry that it regulates, and the agency's Deputy Administrator resigned after the Inspector General found that she had not taken sufficient steps to avoid the appearance of inappropriate contact between her and the chief lobbyist for the Union Pacific Railroad. As a result, the agency has been without a confirmed Administrator or Deputy Administrator for several months, and I want to know when you are going to be appointing a new Federal Railroad administrator.

Secretary MINETA. The resignation of the acting FRA administrator came in December, and in about mid-February I submitted a name for administrator of FRA. That person is going through the background investigation right now, and it will take roughly 60 to 70 days to complete the investigation. As soon as the background investigation is completed, then the White House is in a position to forward the name to the Senate.

Senator MURRAY. I am very concerned about whether we can have a new attitude about safety and enforcement without somebody at the top.

Secretary MINETA. In the meantime, we are not letting rail safety go unnoticed or not dealt with. Robert Jamison, the Deputy Administrator of FTA, is now the acting Administrator of the Federal Railroad Administration. I have asked him to look at rail safety as the No. 1 priority. Just within the last week, we have had something like nine accidents and I will not put up with it. I said to him that we want to deal promptly with this issue. So Robert is working on the rail safety program.

And it goes back to the Graniteville, South Carolina accident. Robert Jamison was appointed as the acting administrator when his predecessor stepped down, and I think 7 hours later the Graniteville accident occurred. So safety is his No. 1 issue.

Senator MURRAY. I see that my time is up for this round, but there were nine fatalities in that accident. There were 11 in California. I think this is a serious issue.

Secretary MINETA. Absolutely, I agree with you.

Senator MURRAY. Mr. Chairman, I hope we can have a hearing on that as well.

Senator BOND. Senator Byrd.

ESSENTIAL AIR SERVICE PROGRAM

Senator BYRD. Well, thank you again, Mr. Chairman.

Mr. Secretary, you and I have been around transportation policy for a long time. I was chairman many years ago of this subcommittee.

We have been around long enough to remember the discussions and the arguments that surrounded airline deregulation. I voted to deregulate the airlines. That is one of the votes I have always regretted, Mr. Chairman. We paid for it immediately, for that bad vote. In West Virginia, my then colleague, Senator Randolph, voted the other way. That was a long time ago.

The establishment of the Essential Air Service was at the very heart of the compact that was made with the flying public when we agreed to deregulate the airlines. We said that the Federal Government would continue to pay to ensure the continuity of air service to communities, that the airlines might want to abandon. And you are now proposing to cut funding for the Essential Air Service in half and require that cut be made up through contributions from the communities themselves.

Now, Mr. Secretary, President after President after President, Democratic and Republican, have proposed to cut this program. I have, time and again, supported successfully the restoration of monies that were cut by an administration.

Why is this cost-sharing requirement not an example of the administration reneging on the commitment made by the Federal Government to these communities? Your answer please.

Secretary MINETA. Senator Byrd, first of all, the EAS program has essentially remained the same without any legislative change since 1978, the year of deregulation.

Secondly, as I was mentioning to Senator Dorgan, we are trying to maintain the number of communities that receive Essential Air Service, but by shoehorning those airports within the amount of money that we have available. We built the criteria for eligibility to be a part of the program based on a $50 million request.

Senator BYRD. Following this program of shoehorning, are we not being short-sighted? We are cutting air service to small communities, to rural communities, and this is vital to the communities. They cannot be O'Hare. They cannot be Dulles. They cannot be the Washington Reagan National Airport, but they serve the needs of people in areas such as Beckley, for example, and Bluefield, West Virginia. I cannot understand why the administration believes that communities the size of these two cities that I mentioned will have the resources to subsidize this airport. I think it is short-sighted. But as I say, it has happened under President after President after President.

Secretary MINETA. My philosophy is to protect the most isolated communities, given the amount of money we have available.

Senator BYRD. That is the point, given the amount of money we have. Why does the administration not push for an increase, or certainly we are going to try here to restore these monies. It is a philosophy, Mr. Secretary, I respectfully disagree with and have all along. We will be at it again.

I hope we will not use this term "shoehorn" to express our philosophy as to the way we are going to help people shoehorn it into the amount of money we have when, Mr. Secretary, your administration will oppose our efforts to restore this. We want something larger, a larger amount in which to shoehorn small communities like Beckley and Bluefield.

Thank you, Mr. Chairman. My time is up.

Senator BOND. Thank you, Senator Byrd.

We have had very interesting discussions. I am going to ask three more questions only. I know you will be disappointed. I will submit the rest for the record. Then we will turn to our ranking member and Senator Byrd for as many questions as they wish to ask here.

Senator BYRD. Mr. Chairman?

Senator BOND. Yes, sir.

Senator BYRD. Let me just thank you before you do that. I recognize the shortage of time. I am glad that we are going to submit questions to be answered for the record. I will join you in that. Thank you.

HOURS OF SERVICE RULEMAKING

Senator BOND. Thank you very much, Senator Byrd. We appreciate your questions and your leadership.

Mr. Secretary, in July 2004, a Federal court overturned the new hours of service rules for truckers because the FMCSA had not considered driver health. There were other concerns that the court raised. Congress has temporarily extended the new rule until 2005 to give FMCSA time to respond to the court's ruling. FMCSA reproposed the rule in 2005 after adding information. But the agency has also asked Congress to enact regulations in law during TEA21.

I would like to know your views on whether these new rules have improved safety. And a very real concern has been raised by the trucking industry as to the economic impact of this rule. Have you considered, first and foremost, the health and safety of the drivers and the impact on the economy by these rules?

Secretary MINETA. In 2001, the first person I had to head the Federal Motor Carrier Safety Administration was a gentleman by the name of Joe Clapp. He was the chairman and CEO of Yellow Freight, and fully understood and appreciated the impact of the hours of service (HOS) rule as it related to the safety and economics of the trucking industry.

His successor as the Administrator of the Federal Motor Carrier Safety Administration, Annette Sandberg, has developed a really good rule. It is supported by the American Trucking Association. They feel, even where the HOS rule was overturned, that it is the right approach.

But beyond that general response, let me ask our General Counsel on the specifics as to the timing of where we are going to go now.

Senator BOND. If you could give us a brief answer, Mr. Rosen.

Mr. ROSEN. I will try to be brief. The proposed rule was intended to use available science and data to improve safety but with a reasonable balance of the costs. The administration believes that it did that, and so we have asked the Congress to extend that 1-year allowance of the rule to stay in effect, to instead ratify that the rule would remain in effect on a permanent basis, subject to whatever improvements the administration could do thereafter.

The Federal Motor Carrier Safety Administration staff is looking at what other improvements or refinements could be achieved and, if need be, they will get themselves in a position to respond as the court had required. But our hope is that rather than have continued litigation and continued rounds of work on that, we could have the rule codified or ratified.

HIGHWAY CONGESTION RELIEF

Senator BOND. Thank you, Mr. Rosen.

Very briefly, Mr. Secretary, a year ago there was testimony that the FTA did not have an effective method to consider the congestion relief on highways that the new transit systems were intended to provide. FHWA and FTA were directed to work on a solution. Where is that solution? Have you come up with a new paradigm for that?

Secretary MINETA. Mr. Chairman, can I get back to you for the record on that please?

Senator BOND. We would be happy to do that.

[The information follows:]

FTA is working with FHWA to study the extent to which transit provides congestion relief. FTA has determined that that locally-developed travel models used in metropolitan areas seeking New Starts funds are incapable of producing reliable estimates of highway user benefits resulting from construction of the New Start. FTA expects to provide a report on the New Starts Rating and Evaluation Process—Congestion Relief—to the House and Senate Committees on Appropriations by June 1, 2005 as requested in House Report 108–671. By further Congressional direction, FTA provides monthly updates to Congress on the progress of the study.

FTA has identified possible causes of the unreliability of highway user benefits. These include: an insufficient number of iterations of capacity constraint in the highway assignment model; inconsistency between the decision rules used to find highway paths and make assignments of traffic to those paths; and the lack of attention to the resulting congested highway travel times. Potential remedies would include several hundred iterations of capacity constraint, consistent decision rules for highway paths and assignment, and improved quality control of congested highway travel times. These remedies are currently being tested in several different metropolitan areas. FTA's intent is to understand the value of the remedies in time for the June 1, 2005 report. The timing of implementation of the remedies will be dependent on the success of the tests and the degree of effort required by metropolitan areas to modify their travel models.

Senator BOND. Finally, the FTA last week delivered a letter instituting new criteria for ratings on every project in the pipeline and current ratings related to cost effectiveness. The letter says that no full funding grant agreement will be approved for a New Starts project that does not have a cost effectiveness rating of medium. Of the six projects other than full funding grant agreements recommended for funding in the budget request, four would be directly impacted by this proposal. The policy, while it may be prudent, came only 6 weeks after the projects had been rated for the year.

I am concerned that this drastic change in policy appears to be arbitrary. How can you respond to that? And are there any other changes to the New Starts rating process on the horizon?

Secretary MINETA. First of all, there are not any other changes in the process for the upcoming fiscal year. We are taking a look at all of the projects, and I am not in a position right now to say what we are going to do with them.

Senator BOND. Is it not arbitrary, on the short time frame just after you fund it, to then say no New Starts? How is that going to work?

Secretary MINETA. The reason I hesitated is that I did not know whether we had made the final decisions, but I have just been informed that we are going to grandfather some of them.

Senator BOND. Thank you.

Secretary MINETA. I knew we were talking about it, but I did not know whether we had actually come to that conclusion. So two projects will be grandfathered under the previous criteria.

Senator BOND. There will be a lot of people happy with that. Thank you, Mr. Secretary.

Senator Murray.

AVIATION FEES

Senator MURRAY. Thank you.

Mr. Secretary, I just have a few questions left and I wanted to ask you, because I am sure you are aware in the Homeland Security budget, the administration is proposing to increase the security fee paid by passengers by 120 percent next year from $2.50 to $5.50 a segment. As you are well aware, the airlines are complaining bitterly, and I think that this $1.5 billion tax increase will further undermine their ability to recover economically.

In your formal testimony that you submitted, you justify your half a billion cut in airport investments by arguing that several airports are not yet charging the full allowable passenger facility charge that they are allowed under law. You seem to indicate that the proper way to invest in airports is through another $350 million in fees instead of from appropriations from the Trust Fund.

Does the administration have any concern for the views of the airlines that air passengers are already over-taxed and that that level of taxation is undermining the airlines' financial viability?

Secretary MINETA. I was not part of that discussion, Senator, when the DHS and OMB were talking about the $2.50 to $5.50 increase. I did talk to some people afterward about that and the impact on the airlines, but I was not part of the discussion beforehand.

Senator MURRAY. Well, I guess my concern is that you are advocating a $350 million increase at the same time that the administration is advocating $1.5 billion in higher fees for airport security. That is kind of a double whammy to the airlines when they are all struggling.

Secretary MINETA. The PFC's were enacted in law as user fees. Some local airports are utilizing them and we still have a number that have not adopted the PFC as a user fee. I think of it as a pass-through to the passenger rather than something that is absorbed by the airline.

Senator MURRAY. Well, to the consumers and to the airlines, it does look like tax increases from two places in the administration.

CROSS-BORDER TRUCKING

Well, let me ask about an issue that I know the chairman of this committee remembers well, and that is the U.S.-Mexico negotiations on cross-border trucking. That was 3 years ago now, and we spent a lot of time working together to make sure that adequate safety measures were in place prior to the implementation of cross-border trucking between the United States and Mexico.

As required in that bill, the Inspector General continues to review and report to us the status of the safety provisions we included in the bill, and I understand that you still have not executed a memorandum of understanding with the Mexican Government which would allow the border to open. Why has it taken so long to reach an agreement with the Mexican Government on cross-border trucking?

Secretary MINETA. Mostly because of their own reluctance to do so. I have had a number of meetings with Secretary Cerisola, and every time I meet with him, I bring up this subject. We have had a memorandum pending in their office for over 2 years and we are trying to get this memorandum of agreement completed. We have not been able to bring this to closure. I know that we have suggested that this be a topic for conversation between President Bush, Mexican President Fox, and Canadian Prime Minister Martin when they meet.

Senator MURRAY. So you believe this is a reluctance on behalf of Mexico to move forward with cross-border trucking?

Secretary MINETA. I think they have had tremendous pressure from their own trucking association, Canacar, to move forward on this. You appropriated funds in 2002 to put our workforce in place, and we have done that. We are utilizing inspectors that are not on the border at other inspection points, but we are ready to move at any time that we get that memorandum of agreement signed to allow our inspectors to go to their terminals and to the maintenance facilities of their trucking companies.

ADDITIONAL COMMITTEE QUESTIONS

Senator MURRAY. Well, Mr. Chairman, thank you. Again, it is a pleasure to work with you on this committee and I look forward to that. I will submit any other questions I have for the record.

Senator BOND. Thank you very much, Senator Murray. This has been an interesting start for a very challenging subcommittee.

Secretary Mineta, as always, we appreciate your tolerance of the questions and your good responses. We will have further questions for the record. Obviously, we are going to be seeing a lot of each other in the months to come. I thank you and your staff.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

QUESTION SUBMITTED BY SENATOR CHRISTOPHER S. BOND

Question. A year ago, there was testimony that Federal Transit Administration did not have an effective method to consider the congestion relief on highways that new transit systems were intended to provide. The Federal Highway Administration and FTA were directed to work on a solution to this issue.

What steps have the agencies taken and when do you expect to have an improved method for identifying how much congestion relief will be provided by new transit systems?

Answer. Currently, locally developed travel forecasting procedures are incapable of producing reliable estimates of congestion relief due to the construction of a New Starts project. FTA has coordinated with FHWA to identify problems with these travel forecasting procedures, suggested remedies, and worked with several travel forecasters from areas considering New Starts projects to test these remedies. The success of these remedies will be understood once these local efforts are completed. Preliminary results indicate that there are significant barriers to implementation of these remedies nationally that will allow FTA to evaluate this highway congestion relief. However, a better understanding of the effort needed to overcome these barriers will be gained after additional testing is performed. The timing of implementation of improved methods will be dependent upon the extent of the problem with local travel forecasting procedures nationally and the magnitude of effort required to address these long standing problems. FTA plans to report findings of this research effort in the Summer of 2005.

QUESTION SUBMITTED BY SENATOR MIKE DEWINE

CRITICAL BRIDGE REPLACEMENT NEEDS

Question. Secretary Mineta, I am interested in knowing what plans the Department has this year and in future fiscal years to address critical bridge replacement needs throughout the country, particularly with respect to the functionally obsolete Brent Spence Bridge connecting Ohio and Kentucky along Interstate 75.

Answer. Replacing and rehabilitating deficient bridges is an important Departmental objective. The administration recommends increased funding for the bridge program in its surface transportation reauthorization proposal—the Safe, Accountable, Flexible, and Efficient Transportation Equity Act of 2003. The administration also recommends that preventive maintenance be eligible for Federal funding as a means to expanding the service life of existing bridges.

The Brent Spence Bridge services I–75 between Ohio and Kentucky. Replacement of the structure has received significant attention both locally and nationally. There are several program funds that the State could use to replace bridges, including the Highway Bridge Replacement and Rehabilitation Program (HBRRP) described in Title 23 United States Code, section 144. The HBRRP funds are apportioned annually to the States that have the responsibility for project-level decision making, setting priorities and allocating the available funds to the project. As a functionally obsolete structure, the Brent Spence Bridge is eligible for HBRRP funds. The needs of the Brent Spence Bridge compete with other projects for the funds available. Due to the size of the structure, funds have also been allocated to the Brent Spence Bridge through the Bridge Discretionary Program. In fiscal year 2004, $2 million was designated to this project through this program. In fiscal year 2005, $4 million in funds were designated through this program. As work progresses, the project continues to be eligible for HBRRP funding and other categories of highway formula funds.

QUESTIONS SUBMITTED BY SENATOR PETE V. DOMENICI

CORRIDORS AND BORDERS PROGRAM

Question. Secretary Mineta, as you know, Border States face unique transportation challenges arising from their proximity to foreign nations. For this reason, the Corridors and Borders Program was instituted to help alleviate these problems and to provide for much needed upgrades to existing highway infrastructure.

These programs provide funding for planning, project development, construction and operation of projects that serve border regions near Mexico and Canada and high priority corridors throughout the United States. New Mexico has been the recipient of this funding and has found it an invaluable resource in maintaining both of our high priority corridors.

Mr. Secretary, could you please provide this committee with an update on the Corridors and Borders program?

Answer. The Federal Highway Administration (FHWA) prepared a report on the first 5 years (fiscal year 1999–fiscal year 2003) of the program under the Transportation Equity Act for the 21st Century (TEA–21). This report, The National Corridor Planning and Development and Coordinated Border Infrastructure Program (NCPD/CBI): History, Evaluation and Results, found that during the first few years of the program, the demand for grants under the program outpaced the available funds. Through the years, most of the funds authorized for the program have been designated by the Congress, and most of those funds have been designated for corridor projects. Five States, West Virginia, Texas, Kentucky, California and Washington accounted for over 40 percent of the awards in the first 5 years of the program.

Question. What have been the positive effects of this program?

Answer. Many projects are longer term, so their benefits have not been assessed during the short life of this program. Also, many projects are more costly than reflected in the grant allocation, and require contributions from other sources. However, anecdotal evidence from some recent success stories in Texas, New York, California and Washington State indicates that the program has some very positive effects such as alleviating congestion, improving highway/railroad crossing safety, and expediting project implementation. These success stories are highlighted in the report, and a brief narrative of each follows:

World Trade Bridge, Laredo, Texas

Mexico-U.S. trade increased in the 1980's and with it the traffic on the downtown Laredo Juarez-Lincoln Bridge. By the end of this decade, the State of Texas, the City of Laredo, the Mexican government, the City of Nuevo Laredo and others were discussing how to address this situation. In 1991, detailed coordination began for a new bridge outside the central business district that would carry commercial traffic. By 1993, projects were placed on the Texas multi-year transportation improvement program and in 1995 a comprehensive funding agreement was reached. The total cost of the new bridge and related improvements was about $100 million. The NCPD/CBI contributed about $6 million of this total through one of the fiscal year 1999 awards.

The new bridge opened on April 15, 2000. Downtown back ups disappeared and truck traffic was successfully diverted to the new bridge. Substantial job growth occurred in fiscal year 2001 and seems clearly related to the business opportunities created by the new bridge.

Commercial Vehicle Processing Center, Buffalo, New York

For a number of years, the Buffalo and Fort Erie Public Bridge Authority had been seeking to improve the operation of the border crossing at the Peace Bridge. In the late 1990's, a user group consisting of trucking associations, commercial carriers, brokers and the U.S. Customs Service developed ideas to meet this objective. One method that seemed promising was to develop procedures and train personnel to operate a Commercial Vehicle Processing Center (CVPC) on the Canadian side of the border. The CVPC would assist truck drivers with incomplete paperwork prior to the vehicles entering the inspection queue. Fewer vehicles failing the primary inspection would mean less congestion on the bridge. In fiscal year 1999, the FHWA awarded about $1 million in NCPD/CBI funds for developing procedures and training personnel for the CVPC. The Authority immediately began implementing this project and the CVPC opened in late fiscal year 1999. Within the first year, the number of vehicles failing the primary inspection fell from 36 percent to 15 percent. Border agencies and the U.S. Customs Service have recognized the CVPC as a success.

Freight Action Strategies Corridor (FAST), Seattle Metropolitan Area, Washington State

Beginning in 1994, local, State, port authority, private sector and Federal officials began developing plans to improve highway/railroad crossings and port access highways in the vicinity of the ports of Everett, Seattle and Tacoma, Washington. In 1997, a phased implementation plan was developed and in fiscal year 1999, the FAST corridor received the first of a number of awards from the NCPD/CBI program. From fiscal year 1999 through fiscal year 2003, FAST was awarded $32,000,000 in NCPD/CBI funds, including funds selected by the U.S. Department of Transportation (DOT) and funds designated by the Congress. The FAST project also received funds outside the NCPD/CBI Program, in Section 1602 of TEA–21, in Section 378 of the fiscal year 2001 DOT Appropriations Act, and in Section 330 of Division I of the Consolidated Appropriations Act of 2003. The first complete grade separation project was completed in fiscal year 2001 and by January 2003, ten such projects were complete or nearly so. As projects have been completed, traffic backups disappeared, safety improved and railroad efficiency increased. Because a high percentage of jobs in the Seattle metropolitan area (as many as one in three) are tied to international trade, systematic improvement of port access is seen as vital to the economic well being of the area.

Alameda Corridor East (ACE), San Gabriel Valley, California

Similar to the FAST program, local, regional, State and private sector parties have been working together since the late 1990's to improve highway/railroad grade crossings (including many grade separation projects) in an East-West corridor with high railroad traffic serving the Port of Los Angeles/Long Beach. The ACE corridor received funds from Section 1602 of TEA–21 and corridor officials credit this with jumpstarting the ACE program. The same officials state that, in the first phase of the program, $3 have been leveraged for every federal $1. The ACE corridor first received a NCPD/CBI award in fiscal year 2000 and subsequently received awards in fiscal year 2001, fiscal year 2002 and fiscal year 2003. These awards totaled $9,019,000. The first projects have resulted in less congestion, improved safety, and reduced emissions. This latter result is quite important because of the well-known air quality problems in the Los Angeles region. Without these improvements, increasing rail corridor traffic would worsen the congestion, safety and air quality problems as well as restrict economic development.

Question. Where do you see this program going in the future?

Answer. The administration has proposed to reauthorize the Corridors and Borders program. Under the administration's proposal, the corridor program would become a Multi-State Corridor Planning Program. The purpose of this program is to support and encourage transportation planning from a broader perspective, transcending traditional State and modal boundaries, to meet evolving freight and passenger transportation needs of the 21st Century. Similarly, the border program would become a Border Planning, Operations, and Technology Program. The purpose of this program is to focus on improvement to bi-national transportation planning, operations, efficiency, information exchange, safety, and security for the United States borders with Canada and Mexico.

INDIAN RESERVATION ROADS PROGRAM

Question. Secretary Mineta, as you well know, the Indian Reservation Roads program is one that I have been intimately involved with since the early 1980's. In fact, it was in 1982, that leaders of the Navajo Nation came to me with the idea of allowing tribes to participate directly in the National Highway Trust Fund programs. I agreed with them and Congress agreed with me and the Indian Reservation Roads program was born.

Mr. Secretary, could you please update this committee on the Indian Roads program?

Answer. On July 19, 2004, after approximately 5 years of negotiated rulemaking between representatives of Indian tribes and the Federal Government, the Indian Reservation Roads (IRR) Program Final Rule (25 CFR Part 170) was published. This rule established policies and procedures governing the IRR Program. It expanded transportation activities available to the tribes and provided guidance for planning, designing, constructing, and maintaining transportation facilities. It also established an IRR Coordinating Committee of 12 tribal representatives to provide input and recommendations to the Bureau of Indian Affairs (BIA) and the Federal Highway Administration (FHWA) on the IRR program.

In addition, the Final Rule established a funding distribution methodology for IRR Program funds. As a result part of the negotiated rulemaking, the entire IRR inventory of 63,000 miles contribute towards the amount of IRR Program funds the tribes receive. The limitation on the growth of the inventory has been eliminated.

IRR Program Funds are distributed by tribal allocation. The formula methodology used to determine each tribe's allocation is composed of three factors. The largest contributing factor is a tribe's "cost to construct," which contributes 50 percent. A tribe's "vehicle miles traveled" (VMT) contributes 30 percent, while its "population" contributes the remaining 20 percent. Each tribe's allocation is then calculated by its percentage of these factors as compared to the nationwide total. However, the actual distribution of the funds has been affected by the different continuing resolutions and extensions to the Transportation Equity Act for the 21st Century (TEA–21).

The following funding amount has been made available for the Indian Reservation Roads Program during the past four highway authorizations:

—Surface Transportation Assistance Act of 1982 (STAA)—$418 million;

—Surface Transportation and Uniform Relocation Assistance Act of 1987 (STURAA)—$400 million;

—Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA)—$1.069 billion;

—TEA–21—$1.47 billion.

The current annual funding level is $275 million for the IRR program. After application of statutory and regulatory takedowns, the available funds are re-allocated from FHWA to the BIA, which is the only agency that receives these funds. The BIA then distributes the funds either directly to the tribes through self-governance agreements/compacts or to the BIA Regional Offices. If the funds are distributed to the BIA Regional Offices, they in turn provide the funds to the tribes through Indian Self Determination Education Assistance Act (Public Law 93–638) contracts, Buy Indian contracts, or perform the work themselves on behalf of a tribe. It should be noted that the Indian Reservation Roads Bridge Program (IRRBP), established under TEA–21, has dedicated $13 million of each year's IRR Program funds to the rehabilitation or replacement of deficient bridges within the IRR System. There are over 4,640 bridges on the IRR System. Approximately 1,050 of these are deficient. To-date, these funds have been utilized for work on over 125 IRR bridges.

Finally, as a result of TEA–21, FHWA developed through a rulemaking requirements and guidelines for three new management systems to assist BIA and tribal governments in identifying and prioritizing quality and quantifiable projects. In addition, FHWA, BIA, and tribal governments are working together both to develop an integrated transportation planning process to help the tribes work with the State and metropolitan planning organizations, and to improve their ability to facilitate long range advance funding for projects. There has also been considerable success with the tribes to develop safety audits and initiatives in cooperation with State and local governments.

Question. Are there things about this program that need to be changed?

Answer. The publication of the Final Rule is having major impacts on the way the Indian Reservation Roads program is administered. All of the new policies and procedures that came about through consensus in the negotiated-rulemaking process are in their first year of existence. These policies and procedures just need time to develop and function. For example, the inventory, long a contentious issue among the tribes, is now being updated electronically utilizing new software that leads the user through the process. The software has taken away much of the subjectivity of the reviewer as to what is or is not to be included in the inventory. Training for the BIA and tribes is taking place throughout the country. In addition, a Coordinating Committee composed of tribal and Federal representatives is being established to provide input and make recommendations to the Secretaries of the Interior and Transportation on ways to improve the delivery of the IRR Program. The duties and composition of the Coordinating Committee are clearly defined in the Final Rule, as well as the critical areas in which they are to concentrate their efforts.

Question. Finally, taking into consideration the unique situation of the Indian people and their infrastructure needs, how does the Department address the issue of Indian Reservation Roads in its highway reauthorization proposal?

Answer. SAFETEA, as proposed by the administration, includes many positive provisions addressing the infrastructure needs of the Indian people. These include:

—A substantial increase in the Indian Reservation Roads Program from $275 million/year to $333 million/year;
—Providing 100 percent obligation limitation to the IRR Program;
—Allowing design to be an eligible use of IRRBP funds;
—Allowing IRR Program funds to be used as the non-Federal match on any project funded under Title 23 and the transit chapter (53) of Title 49;
—Establishing a new Federal Lands Safety Program, which would provide approximately $7.2 million to the BIA and tribes to address specific safety related projects or issues on tribal transportation systems. In addition, FHWA and BIA are embarking on a cooperative outreach program focusing on capacity building and program development.

QUESTIONS SUBMITTED BY SENATOR PATTY MURRAY

SHOULD THE AMTRAK REFORM BILL BE PART OF THE SURFACE TRANSPORTATION BILL?

Question. Mr. Secretary, you said that you and the President believe that intercity passenger rail service is an integral part of the Nation's surface transportation system. The Congress is currently debating a surface transportation reauthorization bill. Last year, when that bill went to conference, the Bush Administration threatened to veto that bill for two reasons. One was the overall size of the bill; the other was the inclusion of any provisions related to Amtrak.

Why does the administration object to tackling the challenge of reforming Amtrak as part of the surface transportation reauthorization bill?

Answer. The issues surrounding the highway and transit programs are extremely complex as evidenced by the fact that it has now been 2 years since TEA–21's authorization expired. Similarly, the issues surrounding intercity passenger rail are extremely complex as evidenced by the fact that it has been 3 years since that authorization expired. However, the issues are not the same for all three. Intercity passenger rail has never before been considered as part of the reauthorization of the highway and transit programs, for a number of reasons, including the fact that Amtrak is a private corporation. To consider these complex and, in many ways unrelated, issues in one "omnibus" piece of legislation would add to the delay and uncertainty currently being experienced by the States, regional transportation authorities, and the traveling public, in addressing this Nation's mobility needs.

Question. If Amtrak is part of the Nation's surface transportation system, why are you so adamant that this legislation move separately?

Answer. The issues are sufficiently different that the Department believes that two separate pieces of legislation can be enacted more quickly and effectively than one. For instance, in the event one aspect of the intercity passenger rail reauthorization package is unacceptable, reauthorization of all modes will not be held up. In addition, the intercity passenger rail issues that Congress faces are not overlapping issues with other modes of transportation. For the other modes, unlike Amtrak, there is no question of ownership of infrastructure. There are already funding sources, and mechanisms in place for distributing those funds. These issues for Amtrak are significant and should not be lumped together with the issues facing the existing transportation programs.

OPERATING AUTHORITY VIOLATIONS

Question. In August 2002, you issued a rule requiring State inspectors to place out of service any commercial vehicles operating without proper authority. However, the Inspector General's January 2005 progress report stated that while nearly all of the States had taken steps to enforce operating authority violations, problems exist with the rule's implementation. Some States will place trucks out-of-service while others do nothing when they find a truck without proper operating authority.

What specific steps do you plan to take to make sure that operating authority violations are handled consistently across the Nation?

Answer. In August 2002, the Federal Motor Carrier Safety Administration (FMCSA) amended the Federal Motor Carrier Safety Regulations (FMCSRs) to require that a motor carrier subject to the registration requirements under 49 USC 13902 may not operate a commercial motor vehicle in interstate commerce unless it has registered with FMCSA. These motor carriers were further prohibited from operating beyond the scope of their registration. If an unregistered carrier's motor vehicle is discovered in operation, or being operated beyond the scope of the carrier's registration, the motor vehicle will be placed out of service and the carrier may be subject to additional penalties (49 CFR 392.9a).

The States are required to enforce registration requirements as a condition for receipt of Motor Carrier Safety Assistance Program (MCSAP) funding. States have 3 years to adopt all new FMCSRs in order to provide sufficient time for changes to State law. In some cases, States automatically adopt FMCSA's new requirements while in other States, changes to regulations are required and in others, actual legislation is required. The States are approaching the end of the 3-year grace period. FMCSA has provided guidance to Federal field and State MCSAP officers to standardize the identification, verification, and enforcement when appropriate. FMCSA is developing a State-by-State national program review to evaluate each State's MCSAP program for compatibility with the FMCSRs, and operating authority will be one of the major focus elements in this review. FMCSA has developed and deployed a system for roadside officers to access real-time data with regard to a carrier's operating authority and insurance coverage. The roadside officer can access this data through the Licensing and Insurance (L&I) website or a toll-free telephone number. To further standardize roadside operations, the Commercial Vehicle Safety Alliance (CVSA) will include 392.9a in their Out-of-Service criterion in the near future.

MAINTENANCE TECHNICIAN AGREEMENT

Question. Mr. Secretary, last year, a Federal arbitrator ruled that the FAA had not met the minimum staffing levels needed for the agency's air traffic control maintenance functions based on the agreement that was reached in fiscal year 2000 between the FAA and its unions. Your budget request includes $5.4 million to hire 258 additional technical employees in order to meet the minimum staffing level of 6,100 as required by the arbitrator. However, I understand that the FAA's staffing report from just last month indicates that the FAA would need to hire as many as 400 new technicians to reach the required level.

How do you explain the fact that there are nearly 150 fewer technicians than what was stated in your budget request?

Answer. Both FAA and the Professional Airways Systems Specialists (PASS) agreed to meet the 6,100 staffing level goal in fiscal year 2006. FAA is currently hiring technical employees and will be in compliance by the agreed upon date.

Question. Will you direct the FAA to be more aggressive in filling the vacant technical positions and reach the required level in fiscal year 2006? I have also been told that the attrition rate of safety-sensitive technician positions was 40 percent higher than average. This concerns me greatly as I hope it does you.

Answer. The FAA is aggressively working to hire and train technicians in order to reach the 6,100 level by the agreed upon date. DOT is unsure of how the 40 percent attrition rate was calculated by PASS. Historically the FAA has found that the attrition rate in the technical workforce has ranged from a high of 5.9 percent in fiscal year 2000 to 4.8 percent in fiscal year 2004.

Question. Shouldn't we be alarmed we are losing these highly skilled positions—specializing in safety—at such dramatic rate?

Answer. Historically, the months of December and January have had the greatest number of retirements. Both FAA and PASS agreed to meet the 6,100 goal in fiscal year 2006, and FAA is aggressively hiring and training technical employees in order to comply with this agreement.

Question. Since I understand it takes 3 to 5 years to fully train these safety-sensitive technicians, how can you assure us that safety won't be compromised given this potential void?

Answer. To address this increased hiring and the long time period that it takes to fully train safety technicians, FAA has ramped up its training capacity in 2005 by 300 percent at the FAA Academy in Oklahoma City, Oklahoma, to train new technicians. Once new technicians have successfully completed the training course, they will be placed in those locations that may be currently understaffed.

SEVERE CUTS IN THE AIRPORT GRANT PROGRAM

Question. Mr. Secretary, last year, the President's budget cut the FAA's air traffic modernization program by $400 million below the previous fiscal year. Much to my dismay, we went along with most of those cuts. This year, the President's budget proposes a smaller cut to the F&E account but slashes the FAA's airport grant program by $472 million or 13.5 percent below last year's level. When you compare your budget request to the levels in the Vision 100 authorization bill signed by the President, the cut to the airport grant program is even more dramatic—$600 million or nearly 17 percent.

Since air travel was down significantly over the last 3 years, the efficiency and capacity challenges that gripped the FAA prior to September 11 have not been as urgent. However, today, we find that air travel is now finally inching near or exceeding pre-9/11 levels and the need to reduce delays, build additional capacity and improve customer service may once again become a pressing matter.

How is it that you decided to cut the airport grant program at a time when air travel is now finally rebounding and airports are seeking to make capacity improvements?

Answer. The fiscal year 2006 budget proposal takes into account the needs and changing financial conditions in the airport industry. The FAA's latest estimates of capital development eligible for Federal funding for the period 2005–2009, as identified in its biennial National Plan of Integrated Airport Systems (NPIAS), is down 15 percent. Airports are scaling back or deferring their development plans because of financial uncertainty of the airline industry. Examples of development that are being scaled back generally include landside projects such as terminal and ground access. However, major capacity enhancing projects, such as new runways at major airports, are proceeding.

Industry Financial Experts report:

—Bond issues supporting new construction declined in the last 2 years and only modest increases are projected in the next 18 to 24 months.

—Airports will continue to exercise caution in committing funds for new capital development due to financial uncertainties of the commercial aviation segment.

The 2006 Budget addresses these industry findings:

—The administration's budget submittal reflects a good balance of meeting important airport infrastructure needs while taking into account fiscal reality.

—The $3 billion proposed budget is adequate to support all high priority safety and capacity projects. The budget request proposes a one-time adjustment to the Airport Improvement Program allocation formulas to assure a minimum discretionary amount of $520 million.

—The basic structure of the FAA's current formulas is retained, including doubled entitlements for primary airports and maintaining non-primary entitlement for general aviation airports. The budget also allows FAA to have the discretionary resources available to achieve national priorities for airport capital investments.

DECLINING TRUST FUND REVENUES

Question. The Inspector General's "top management challenge" report highlights the growing gap between the budget request of the FAA and the amount of revenue that is generated through the aviation trust fund. While passenger traffic is returning, the average cost of a plane ticket has gone down and therefore the ticket tax revenue has decreased as well. In the current budget environment, the competition for general funds will remain fierce.

Is the administration considering alternative funding mechanisms for the future financing of Federal aviation needs?

Answer. Yes. There is a need for fundamental change because there is a mismatch between the FAA's growing budget requirements and revenue sources that will hamper its ability to meet the demand for services. The FAA needs a stable source of funding that is based both on costs and the services provided so that FAA can meet its mission in an extremely dynamic business environment.

Question. What options are under consideration?

Answer. All options are on the table at this time, and the FAA has begun to develop a set of viable proposals. The areas the FAA is looking at include user fees and taxes, alternatives for funding long-term capital requirements, and an appropriate level of contribution from the General Fund.

IS FTA CHANGING THE RULES OF THE NEW STARTS GAME?

Question. Just last week, your Federal Transit Administrator notified the transit community that the Bush Administration no longer intends to support transit "new start" projects that don't have a "medium" or higher rating for cost-effectiveness. There are four projects that received a "recommended" rating from the FTA and received funding in your 2006 budget request that do not qualify under this new criteria: Beaverton, Oregon; Denver, Colorado; Dallas, Texas; and Salt Lake City, Utah.

Your budget requests a total of $158.8 million for six projects in the final design phase including the four I just mentioned. Also, you just sent up a Full Funding Grant Agreement for the project in Charlotte, North Carolina but that project wouldn't qualify under your new criteria either. Your budget requests $55 million for that project.

Based on the FTA's new announcement, do you still stand by your budget requests for these five projects? Under your new policy, will you continue to request funding for these projects in future years?

Answer. In the President's Fiscal Year 2006 Budget, four proposed projects identified as "Anticipated FFGAs" received specific funding recommendations and are not affected. This includes $55 million for the Charlotte, North Carolina project. However, as a general practice, the administration will target its funding recommendations in fiscal year 2006 and beyond to those proposed New Starts projects able to achieve a "medium" or higher cost-effectiveness rating.

The six projects listed under the category "Other Projects," including the four mentioned in your question, did not receive a specific funding recommendation in the President's Budget. In fact, as noted in the Budget and the Annual New Starts Report submitted to Congress in February, FTA did not anticipate that all six projects would ultimately receive a funding recommendation, and the President's Budget set aside only $159 million of the $260 million that could be utilized if all six projects were ready for funding by the time Congress takes up the fiscal year 2006 Transportation appropriations bill. FTA plans to advise the Appropriations Committees' prior to Senate mark-up of the administration's funding recommendations for these projects. Funding these projects beyond fiscal year 2006 will depend on the annual project rating and other factors.

The administration's reauthorization bill says nothing about this new policy change. The House- and Senate-passed reauthorization bills do not make this policy change.

Question. Why is DOT now imposing this new policy with no legislation in the middle of the year?

Answer. The change in how the administration will target its recommendations for funding to projects that achieve a "medium" or higher rating for cost-effectiveness does not require legislation. The President and his administration must make numerous tradeoffs and decisions as budget recommendations to Congress are developed. The issue was raised in the context of finalizing the fiscal year 2006 budget and annual New Starts report, and the change in policy was announced as soon as the decision was made. The policy change simply states that, as a general practice, the administration will no longer target funding to any project that receives a "medium-low" rating for cost-effectiveness. The actual project ratings (not recommended, recommended, and highly recommended) are not affected by this change. Also, the new administration funding recommendation policy does not apply to the four projects identified in the President's Budget under the category "Anticipated Full Funding Grant Agreements" or to the 16 projects that already have full funding grant agreements.

WHAT PROGRESS HAS BEEN MADE IN PIPELINE SAFETY RESEARCH AND ENFORCEMENT?

Question. Mr. Secretary, as you well know, I have been a strong advocate for funding increases for the Office of Pipeline Safety. Over the last few years, I have been pleased that we have been able to meet and/or exceed your budget request in the area of pipeline safety so that advances can be made in research.

With the relatively stable funding of $9 million for the R&D program since fiscal year 2002, what kind of progress have you been able to make in increasing the safety of pipeline operations in recent years?

Answer. Since fiscal year 2002, the PHMSA/OPS R&D Program has been working with industry to develop new and better tools to help operators improve their capability to inspect pipelines, measure internal and external corrosion, monitor the integrity of those lines which were "unpiggable", identify mechanical damage and improve damage prevention. All of these objectives relate directly to improving the operational safety of pipelines.

In less than 3 years, the program has made a total of 49 awards addressing technology development and demonstration to increase safety in pipeline operations and consensus standards. These have given rise to eight U.S. Patent applications that improve the path of new tools toward commercialization.

Some quantifiable enhancements are in-the-field inspection tools with a 50 percent increase in sensitivity to defects, capacity to inspect lines that are 30 to 50 percent smaller in size, and capability to identify defects on both longitudinal and circumferential welds of pipelines. The R&D Program has successfully developed and demonstrated new tools for: non-destructive testing of integrity of pipelines under roads; the mapping of all underground utilities with ground penetrating radar; and detection of leaks from medium altitude aircraft.

Other improvements being generated by PHMSA research investments include tougher pipeline materials; better ways to find and eliminate defects before they become hazardous; and better methods for constructing, operating, and maintaining pipelines.

Not only is this research program strengthening the industry's ability to effectively meet integrity management challenges but it is effectively addressing the public's demand for near-term solutions to public safety concerns. Research funding of the National Pipeline Mapping System results in increased public awareness of the location of pipelines and decreases the likelihood of their being damaged.

The R&D Program contributes directly to safer pipeline operations by fostering development of new technologies that can be used by operators to improve safety performance and to more effectively address regulatory requirements; strengthening regulatory requirements and related national consensus standards; and improving the knowledge available to better understand safety issues.

Question. Are there better inspection and analysis tools as a result of this funding? Please provide examples.

Answer. Yes. The PHMSA research program is improving pipeline inspection technology and analysis tools and strengthening industry's ability to effectively manage pipeline integrity. Results from the R&D Program also have driven improvements in operators' ability to prevent damage to pipelines and detect leaks improve oversight of operations and control functions, and access and select stronger pipeline materials.

—A significant outcome of the research program has been quantifiable enhancement the sensitivity of inspection tools. We now have tools capable of detecting defects that are at 5 percent of the material thickness. This is an improvement over 10 percent material thicknesses in the past.

—PHMSA research has resulted in a significant increase in the miles of pipelines that can be inspected with internal instruments. Smarter and smaller internal inspection tools can inspect pipes smaller than 24 inches in diameter with increased ability to manipulate through valves and sharper bends.

—New and enhanced tools for non-destructive inspection now can better detect deteriorated coatings; and use of non-intrusive tools to pass below roads is saving extensive construction costs and traffic congestion problems. Pipelines can now be inspected for internal and external defects up to 200 feet in length, an increase from only 25 feet in the past. To prevent mechanical damage, the R&D Program has worked with industry in the development and successful demonstration of new tools that utilize ground penetrating radar that can detect buried utilities 25–30 percent deeper through the earth than in the past and through reinforced concrete, critical to locating all below ground utilities before excavation projects.

Results from the R&D Program have accelerated the development and demonstration of technologies that enable decision makers to understand risks to the public more completely and to deal with them more effectively. The R&D Program continues to strengthen the knowledge base, technology tools and consensus standards that play a critical role in the steady decline in pipeline incidents, even while the pipeline system is expanding. The future of pipeline technology holds promise for a dramatic improvement in our ability to fabricate, construct, operate, and maintain the Nation's pipeline infrastructure.

Question. The Pipeline Safety Improvement Act of 2002 charged PHMSA to review and verify operator compliance with its new integrity management requirements, and, where appropriate, take enforcement action. Your budget justification states that the Pipeline and Hazardous Materials Safety Administration was surprised at the degree of difficulty that hazardous liquid operators had in complying with the new regulations and that more than 90 percent of the inspections resulted in enforcement action.

Why is this the case?

Answer. PHMSA's Integrity Management regulation required hazardous liquid pipeline operators to implement a comprehensive, systematic approach to the management of pipeline safety. The required structured set of program elements represented a fundamental change in the way most hazardous liquid pipeline operators manage pipeline integrity. PHMSA found that most operators needed to develop new or improved management and analytical processes (e.g., data integration and risk analysis), implement new methods and technologies, and expand the skills of their staff to effectively manage integrity. Even those operators with relatively mature programs needed to introduce more structure in procedures and documentation.

Operators identified about 80 percent of the hazardous liquid pipeline mileage as meeting the requirements for integrity protection, including testing. This is a far greater amount than either government or industry anticipated. Thus significant operator resources have been directed to complete the required testing and subsequent analysis of data. While this has paid huge dividends in repairing numerous integrity threats in pipelines, in some cases, the need to complete assessments of test data has diverted operators from other prevention and mitigation tasks.

The deficiencies that PHMSA identified most frequently during inspections are listed below. PHMSA is working with operators to make needed corrections:

—*Identification of preventive and mitigative measures to protect High Consequence Areas (HCAs)*.—The regulation requires pipeline operators to do more than assess their pipelines for defects. Operators must consider all threats to pipeline safety; identify additional measures to prevent failures that could result from such threats; and mitigate the consequences should such a failure occur. Fewer than half of the operators inspected (49 percent) had developed their risk analysis methods sufficiently to evaluate the effectiveness of their current protective measures and identify the most significant vulnerabilities. Further, they had not developed the management processes and implemented measures to address these vulnerabilities. Most operator efforts were focused on identifying pipeline segments that could affect HCAs and performing integrity assessments (in-line inspection and pressure testing) on the highest risk lines.

—*Considering all relevant risk factors in identifying potential pipeline integrity threats*.—The regulation requires operators to consider all relevant risk factors to identify integrity threats and names specific factors. For some operators, this data was not readily available or in a format that was useable in their risk analysis models. Operators needed to apply significant resources and time to assemble this information and incorporate it into their risk models. As a result, more than a third (36 percent) of the operators had deficiencies in this program element.

—*Evaluation of integrity assessment results by qualified personnel*.—The regulation requires that operator review of in-line inspection (smart pig) results be performed by individuals who are qualified to do so. Nearly half of the operators inspected (45 percent) had not addressed this requirement. Some operators had not established what skills and capabilities were required and thus could not demonstrate that their personnel reviewing assessment results had the required qualifications. In other cases, operators still needed to provide individuals with additional training, or even hire personnel with the requisite experience and background. A national consensus standard is now in place to guide operators on meeting this requirement.

—*Integration of other data in the evaluation of integrity assessment results*.—The regulation requires operators to integrate other pipeline data (corrosion control records, right-of-way encroachment reports, etc.) in their review of in-line inspection results to more fully understand and characterize pipe condition and integrity threats. Inspectors from the Office of Pipeline Safety within PHMSA found that nearly half of the operators (43 percent) had made little progress in being able to implement this crucial requirement. To do so, operators had to develop new analytical tools and data bases to utilize the vast quantities of data for their pipeline network. Often this work involved bringing together information from different sources and in different formats (e.g., written files, pipeline maps, different legacy databases), and putting it in common formats. A number of operators were in the process of developing sophisticated Geographic Information Systems for this purpose.

—*Use of local knowledge to identify High Consequence Areas (HCAs)*.—While the National Pipeline Mapping System identifies HCAs nationwide, operators must make use of their knowledge of local conditions around the pipeline to identify additional high consequence areas that should be protected (e.g., new residential developments near a pipeline). More than a third of the operators (38 percent) had not implemented this requirement at the time of the inspection. To meet this requirement, operators needed to define and communicate HCA information requests to their field personnel, and then integrate the information received from the field in all aspects of their program (e.g., identifying pipeline segments that could affect these areas, determining the most appropriate integrity assessment tools, etc.). For many pipeline operators this was a significant logistical challenge.

PHMSA took a vigorous enforcement posture on this rule to indicate to the industry that the agency was serious about the operators developing quality integrity management programs. PHMSA used a variety of enforcement tools to correct serious violations and program deficiencies, and to foster the continued development and improvement of integrity management programs.

HOW WILL THE RESEARCH AND TECHNOLOGY INNOVATION ADMINISTRATION HARNESS TRANSPORTATION TECHNOLOGY INNOVATION?

Question. With the passage of the "Norman Y. Mineta Research and Special Programs Improvement Act," you are in the process of standing up two new modal administrations—the Pipeline and Hazardous Materials Safety Administration and the Research and Innovation Technology Administration. The new research and technology agency is supposed to have greater control and input into the research and development that is conducted within the Department's agencies.

What does RITA plan to do differently in order to provide technological innovation?

Answer. As envisioned by Secretary Mineta, RITA will be a Departmental resource for coordinating and managing the Department's diverse research, development and technology (RD&T) portfolio. RITA will coordinate and implement strategies to facilitate cross-cutting solutions to America's transportation challenges. In doing so, RITA will work with the DOT operating administrations to ensure that RD&T initiatives reflect sound investment decisions. Mechanisms will be established by RITA to ensure research results in deployable applications and that there is a systematic and focused process for transforming research findings into marketable products that will improve our Nation's transportation system. This approach will help to ensure RD&T effectiveness, eliminate unnecessarily duplication, and accelerate transportation innovations.

Outside DOT, RITA will monitor research in other Federal agencies (e.g., Department of Energy and the Department of Homeland Security) that supports long-term transportation advances, and will identify opportunities for collaboration and potential applications of innovative technologies to crossmodal issues. RITA will also promote public-private partnerships to speed up the delivery of technological innovations to market. Finally, RITA will facilitate DOT participation in the national Science and Technology Council, including such efforts as the National Nanotechnology Initiative and the Hydrogen Initiative.

Question. Please explain how you will overcome any obstacles on the part of the modes in this regard since they have traditionally done their own.

Answer. DOT has already made significant progress in overcoming the obstacles of stove piping among the modes. On May 2, 2005, the Secretary signed DOT Order 1120.39A. This Order establishes the DOT RD&T Planning Council and RD&T Planning Team. It also describes the RD&T planning process that ensures DOT-wide coordination, integration, performance and accountability of DOT's RD&T modal and multimodal programs.

The RD&T Planning Council is chaired by the RITA Administrator and includes the heads of each DOT operating administration and the equivalent officials from the Office of the Secretary. This senior-level council sets broad RD&T policy and ensures RD&T coordination.

The RD&T Planning Team, chaired by the Associate Administrator for Research, Development, and Technology, includes representation from the across the Department, supports the Planning Council and provides coordination for those officials managing each operating administration's research program.

Transparency is a key element in achieving consensus and buy-off from the modes. These changes are not intended to take over the role of each operating administration in conducting research to supports its mission. The intent is to foster closer ties among the operating administrations and identify areas where collaborative efforts might improve performance and results.

Working through the RDT&T Planning Council and Team, the Department's RD&T agenda will be aligned with the DOT Strategic Plan and with Secretarial and administration priorities and policies. The operating administrations will continue to conduct RD&T activities based on their agency missions, input from stakeholder groups, knowledge of transportation systems, and technologies, within the overall framework of the Secretary's RD&T priorities and the Department's RD&T agenda.

DOT's RD&T planning process includes three elements: multiyear strategic planning, annual program planning, and budget and performance planning. This process was described in Research Activities of the Department of Transportation: A Report to Congress, dated March 2005.

SAFETY WORKFORCE

Question. In 1996, the FAA significantly increased the number of aviation safety inspectors in light of the 90-Day Safety Review that was conducted in the aftermath of the ValuJet crash in Florida. Unfortunately, the number of inspectors has been consistently below the standard of 3,297 that was set in that review. In fact, Mr. Secretary, I believe the National Civil Aviation Review Commission that you chaired called for even higher inspector levels. I understand that the FAA may lose as many as 250 inspectors this year through attrition and that the agency has no intention to back-fill for these positions. This greatly concerns me.

Why aren't you filling vacancies for these critical safety positions?

Answer. During fiscal year 2005, the FAA has been forced to reduce staffing, including our Flight Standards safety inspector workforce staffing. The reductions will be through attrition and will include both inspector and non-inspector positions. Since all reductions will be made solely through attrition, we cannot precisely predict what will occur in the safety inspector workforce and what will occur in the support workforce. In regards to reduction in the safety inspector workforce, we will make every effort to fill highly critical safety positions—such as principal inspectors assigned to major airlines—if such positions become vacant. Additionally, the fiscal year 2006 budget includes an increase of 97 safety and inspection engineers.

Question. Wouldn't you agree that we shouldn't be reducing the number of inspectors in an era when a number of airlines are struggling financially and outsourcing an increasing portion of their maintenance work?

Answer. The following steps are being taken to ensure that the cutbacks in the number of inspectors don't undermine the efficiency, competitiveness, and safety of the U.S. aviation industry.

—Safety will always come first, and the FAA will not reduce its oversight of the air carriers. Instead, the agency will reduce its ability to certify new operators, repair stations and aircraft components, so inspectors can focus on safety oversight rather than new certifications.

—The FAA will ensure that air carriers and air agencies will meet basic standards through a system safety approach. This includes analyzing data gathered through targeted inspections, focusing surveillance on high-risk areas and where appropriate, revising or developing policy and guidance materials.

—The FAA will delay or defer some new certification activities related to growth of existing operators, or applications for new operators or products in order to absorb these reductions without resorting to cuts in safety oversight.

QUESTIONS SUBMITTED BY SENATOR RICHARD J. DURBIN

AMTRAK

Question. Why did the administration only include a fraction of the funds Amtrak needs in the fiscal year 2006 budget when this level of funding will send the railroad into insolvency?

Answer. Since 2003, the administration has unsuccessfully sought to engage the Congress in a discussion about the perilous condition of intercity passenger rail service and the need to reform how this form of transportation is provided. The budget request was intended as a "wake-up" call that intercity passenger rail service as presently provided cannot be sustained, not just over the long-term, but in the short-term as well. Without meaningful reform legislation by the Congress and the administration, reform will come through the bankruptcy courts. That is a means of reform that the Department would prefer to avoid, but, unfortunately, cannot be ruled out.

Question. Does the administration support reauthorization of Amtrak? Or would the administration rather break the intercity passenger railroad up and privatize operations?

Answer. The administration supports authorization of a new approach to providing intercity passenger rail service that embodies five principles of reform: create a system driven by sound economics; require that Amtrak transition to a pure operating company; introduce carefully managed competition to provide higher quality rail services at reasonable prices; establish a long-term partnership between States and the Federal Government to support intercity passenger rail service; and, create an effective public partnership, after a reasonable transition, to manage the assets of the Northeast Corridor. While the administration's vision would encourage competition for contracts from States to provide specific services, that vision is not based upon privatization of operations.

The word "privatization" has been used too loosely in this debate to imply that the administration approach would remove government funding and involvement in the intercity passenger rail system. This is a misrepresentation. Regarding train operations, the administration's proposal is to allow States to compete services among qualified vendors, including potentially the existing Amtrak organization, private companies, or government transportation entities. States would spend their public funds on this function, similar to how they solicit contracts to private companies to build and maintain publicly-owned roads and bridges. This element of competition is intended to help control costs and to encourage the development of innovative services that meet a State's and, therefore, the particular transportation needs of the public. Similarly, for capital projects, the administration plan would allow States to conduct competitions taking bids from a variety of contractors. Like other Federal transportation programs, the Federal Government would make matching grants to States for the capital expenses. Ultimately, it is the States and interstate compacts that would oversee, manage, and help fund intercity passenger rail services, with the private sector potentially performing these functions under contract.

QUESTIONS SUBMITTED BY SENATOR BYRON L. DORGAN

ESSENTIAL AIR SERVICE COST-SHARING: BACKGROUND

Question. I was also disappointed that the President seeks to require all communities receiving EAS funds to provide non-Federal matching funds. Communities in North Dakota that participate in EAS, such as Devils Lake, Jamestown and Dickinson-Williston, are more than 210 highway miles from a medium or large hub airport, and will have to provide 10 percent. This is patently unfair and goes against the purpose of the EAS program to promote and protect air service to rural areas, and I will fight hard to prevent the President's plan from taking effect.

Given that Congress explicitly rejected such a harsh cost-sharing requirement in the FAA reauthorization process, why would the administration propose it now after the reauthorization bill has passed? Isn't this patently unfair to rural America?

Answer. Since deregulation of the airline industry, the Essential Air Service (EAS) program has gone without any fundamental change despite the major changes in the airline industry. The administration still believes that significant reform of EAS is necessary to bring the program into the 21st Century.

With respect to the cost-sharing aspect of the administration's reform proposal, local contributions could come from many sources, including local businesses, local governments, or the State.

Most Federal programs of this kind require some type of local contribution, and the EAS program has operated for 27 years without communities being required to make any contribution. The Small Community Air Service Development Program has shown us that small communities are willing and able to contribute funds for improved air service.

For too long, many communities—there are a few exceptions—have taken air service for granted as an entitlement and done little or nothing to help make the service successful. Requiring a modest contribution should energize civic officials and business leaders at the local and State levels to encourage use of the service, and as stakeholders in their service, the communities will become key architects in designing their specific transportation package.

AMTRAK

Question. I am very disappointed that Amtrak funding was essentially eliminated in the President's budget, including only $360 million to allow the STB to support commuter service if Amtrak should terminate its commuter services in the absence of subsidies. I am particularly concerned about the impact of any cuts to Amtrak on long distance trains, such as the Empire Builder.

Does the administration support intercity passenger rail? Does the administration have a plan that would continue long-distance Amtrak trains?

Answer. The administration does support intercity passenger rail service where such service can be based upon sound economics. The administration's legislative proposal, the Passenger Rail Investment Reform Act, helps improve the economics of intercity passenger rail by providing for a Federal/State capital investment partnership, limited competition to assure that the highest quality services are provided at the best cost, and a phase out of Federal operating subsidies to allow sufficient time for these initiatives to take hold. The Passenger Rail Investment Reform Act would continue intercity passenger rail services that can meet their operating expenses or that are viewed as important enough that a State or group of States will provide any needed operating subsidy.

QUIET ZONES

Question. The Federal Railroad Administration was directed to do a rulemaking in 1994 on locomotive horns, but still has not issued a final rule. The FRA has announced that interim final rule will take effect April 1, 2005 (this was delayed from December, 18, 2004).

Will the interim final rule indeed come out on April 1, and will that be considered a final rule, or might it be changed again? We have communities that are relying on final rulings from the FRA on this issue so they can move ahead with quiet zone planning.

Answer. The Federal Railroad Administration's final rule on "Use of Locomotive Horns at Highway-Rail Grade Crossings" was published in the Federal Register on April 27, 2005.

QUESTIONS SUBMITTED BY SENATOR TOM HARKIN

GASOHOL CONSUMPTION IMPACTS

Question. Many years ago the country adopted a national policy promoting the use of alternative fuels and our energy independence. The production and consumption of gasohol supported that national policy. However, support of that policy and the consumption of gasohol had a direct negative impact on the revenues attributed to the Highway Account of the Highway Trust Fund and a direct negative impact on the level of highway investment possible. Fortunately, Congress eliminated this impact last year. Producers of ethanol continue to receive an incentive—now through tax credits, and the Highway Account of the Highway Trust Fund is receiving the same revenues whether our vehicles are consuming gasohol or gasoline. These additional revenues are a welcome addition to the Trust Fund as we work to increase our much needed highway investments.

As of January 1, 2005 the Highway Account receives full revenue credit for gasohol consumption, and it should be possible for FHWA to revise the estimated State-by-State trust fund contributions.

When will FHWA revise its estimate of the trust fund contributions by State to reflect the most current information and use that information in the distribution of funds? And will those adjustments be done in time so that the revised analysis will be used for this fiscal year's allocations?

Answer. Pursuant to current law, FHWA uses the latest available data on contributions to the Highway Account of the Highway Trust Fund when apportioning funds to States. On October 1 of each fiscal year, the date that funds are to be apportioned, the latest available contributions data are for the fiscal year 2 years prior. As might be expected, data for the fiscal year that ended just 1 day earlier are not available at that time. Thus, fiscal year 2005 apportionment formulas that use Highway Account contributions as a factor, would use fiscal year 2003 contributions as the basis for apportionment.

TRANSPORTATION INVESTMENT LEVELS

Question. By virtually all measures, this country continues to under invest in our highway infrastructure as unfunded needs continue to grow. The Federal motor fuel user fee, accounts for over 90 percent of the Highway Trust Fund revenues. However, the buying power of the current motor fuel user fee rate has declined by over 21 percent since 1994.

What steps would the administration take to increase the level of revenue needed to keep up with inflation and also to address the future economic costs of under-investment in our surface transportation network?

Answer. The administration will continue to work with our State and local partners to advance best practices in the management of our surface transportation assets, so that the resources available can be utilized in a more cost-effective manner. Public-private partnerships and other innovative financing mechanisms the administration has encouraged represent an opportunity to leverage our public infrastructure investment without placing an excessive burden on taxpayers.

AIRPORT FUNDING—AIRPORT IMPROVEMENT PROGRAM

Question. Smaller communities are relying more and more on the availability of an airport capable of handling corporate jets to attract business. For these communities the Airport Improvement Program provides crucial funding to invest in airport improvements and expansions without which the area's opportunity to attract and even to keep businesses will be sharply reduced. Many States have also established State programs to complement the Federal funding. Many small and medium hub airports are also seeing significant construction needs.

I was very disappointed to see that the administration wants to reduce funding from $3.5 billion to $3 billion, at a time when we should be encouraging the expansion of job opportunities in communities and smaller urban areas in rural America.

Aside from the cuts in Amtrak, the administration appears to have singled out this program for a large cut.

For Carroll, a small town airport in Iowa, the Kansas Region is moving to stop a runway expansion project in midstream after local funds had been spent, an unusual action. What is the Department going to do to provide adequate improvements for general aviation airports if funding is reduced?

Answer. Carroll County requested Airport Improvement Program (AIP) funding to re-align, re-grade and pave its crosswind runway. In fiscal year 2004, the airport used $224,200 of non-primary entitlements to realign and re-grade the crosswind runway. The cost to pave the runway is $990,000 and paving the access taxiway is $274,500. Paving the crosswind runway is a low priority project and will not compete well against higher-priority primary runway projects.

FAA has offered to seed Carroll's crosswind runway and restore it as a turf runway. This option provides Carroll County with an improved, usable runway, which is consistent with FAA policy. Another option would be to use its non-primary entitlements to pave the runway in phases that establish usable lengths. There are other funding options that are available to the airport, including using state apportionment funds or approaching FAA with an innovative financing plan.

The FAA knew that with the reduction in AIP, it was important to preserve the basic structure of entitlement formulas developed in the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century (AIR–21) and continued under Vision 100—Century of Aviation Reauthorization Act to ensure a stable funding stream from entitlement funds. The FAA's proposal includes a request for Congress to enact special one-time legislation that would permit distribution of AIP funds using the "Special Rules" contained in Section 47114 of title 49, United States Code. This section provides for doubling entitlements and for continued entitlement funding for non-primary airports. This would be accomplished by incorporating specific statutory language in the fiscal year 2006 appropriations bill directing the use of the "Special Rules" notwithstanding a level of AIP funding below $3.2 billion. These entitlement funds, combined with discretionary funds when needed for high priority projects, will ensure continued funding for general aviation improvement projects.

Question. What impact does the Department see for a reduction in entitlement funds for small and non-hub airports?

Answer. With the reduction in AIP, it was important to preserve the basic structure of entitlement formulas developed in AIR–21 and continued under Vision 100 to ensure a stable funding stream from entitlement funds. Airports and the FAA have developed long-range investment plans based on these rules. The disruption to long-range investment plans could seriously interfere with the development of the national airport system and strain financial resources of many small airports that rely heavily on AIP grants to meet their needs.

The President's fiscal year 2006 budget request includes special one-time legislation that would permit distribution of AIP funds using the "Special Rules" contained in Section 47114 of title 49, United States Code. This section provides for doubling entitlements and for continued entitlement funding for non-primary airports. This would be accomplished by directing the use of the "Special Rules" notwithstanding a level of AIP funding below $3.2 billion.

Using this approach, airports will experience a very modest reduction in entitlement amounts. However, discretionary funding will mitigate this reduction, which will be used to: (1) meet the FAA's Letter of Intent (LOI) commitments; (2) entertain new LOI candidates; and (3) fund needed safety, security, and related projects.

TRANSIT BUS AND BUS FACILITIES FUNDING

Question. The administration's budget combines the Fixed Guideway modernization, Urbanized and non-urbanized formula programs, the Bus and Bus Facilities capital program, Planning and Research and a number of other programs, some of which are new programs, into a Formula Grants and Research Program. While most of the current activities retain some identity and specific funding within the Formula Grants and Research Program, it appears that what has been lost in the new program is the bus and bus facilities program.

What is the administration's position on the importance of a program to assist States and local agencies maintain and improve their bus fleet?

Answer. The administration agrees that it is important to assist States and local agencies maintain and improve the condition of their bus fleets, since 95 percent of the Nation's communities are served only by bus operations. We believe that is best done through including the funds in the formula programs rather than through a discretionary program. Formula funding would provide the funds to more communities nationwide and funding would be more predictable and stable. This would allow State and local agencies the means to better plan to meet their bus capital replacement and improvement needs. Because the formula funds are available for obligation for 3 (nonurbanized formula) or 4 (urbanized formula) years, grantees can accumulate funds to support major bus procurements or facilities projects. The transfer provisions proposed will allow flexibility to trade funds among programs, providing grantees support for one-time projects. FTA grantees can also take advantage of flexible funding provisions to use highway funds for transit capital projects.

INTERCITY BUS TRANSPORTATION

Question. Iowa has an excellent system of regional transit agencies that provide transit service in all counties of the State. However, while it is important to provide transit service to citizens within our urban areas, it is also important to provide options for service between our urban centers. People who do not have access to the personal auto for the trips of between 100 and 200 miles must often rely on the private sector through our inter-city bus carriers.

As the need to provide longer distance service to our rural non-drivers, the elderly and disabled increases; what do you see as the Federal role or responsibility?

Answer. The private sector has an important role to play in maintaining intercity service. Since the Intermodal Surface Transportation Efficiency Act of 1991, however, Federal transit legislation has recognized the need for Federal financial support to sustain some of the most vulnerable service. The nonurban formula program under Section 5311(f) requires States to use 15 percent of their annual apportionment under the nonurbanized formula program to support intercity bus service, unless the Governor certifies that the rural intercity bus needs of the State are adequately met. In a recent "Dear Colleague" letter, FTA encouraged the States to take full advantage of this provision to minimize the impact of recent and ongoing service reductions by the largest national intercity bus carrier. The States affected to date have worked successfully with regional intercity bus operators and with rural transit systems to maintain many of the discontinued routes.

We agree with your assessment of the importance of rural transit and intercity connections. The administration supported significant increases in rural transit funding in the Safe, Accountable, Flexible and Efficient Transportation Equity Act of 2003 (SAFETEA), and proposed to strengthen the intercity bus provision by requiring consultation with the private providers before certifying that needs are adequately met.

RURAL TRANSPORTATION NEEDS

Question. As the gap between the funding available for transportation investments and the national transportation needs continues to expand, there is the temptation to redistribute or redirect our investments and focus on the large urban centers. Whether it is highway, transit, aviation or rail passenger funding, the commitment to a national transportation system must be maintained.

Can we have your assurance that this country will retain a national transportation system—providing service to rural America as well as urban centers?

Answer. The Department is deeply committed to ensuring mobility in both rural and urban America, and we look to all modes to play a continuing role in meeting traveler needs.

Regarding the availability of long-distance service options, you may be aware that the Department is presently preparing a report to Congress that addresses Greyhound's recent service cutbacks, many of which have occurred in rural areas. Our preliminary findings are encouraging. First, many of the affected communities had few or no passengers riding Greyhound's buses during the past year; service cutbacks in those areas pose little or no impact. Second, where some passenger base (ridership) still exists but Greyhound has nonetheless found that service cutbacks are critical to sustaining its long-term operating strategy, other carriers have stepped in to provide service. The other carriers have lower operating costs and may have different route structures that allow them to provide the service more profitably. Similarly, some of these replacement carriers are in a better position to take advantage of available Federal capital and operating subsidies that help sustain service where it might otherwise be unprofitable even for them to operate. Finally, in addition to carriers stepping up to offer services, many affected States have been making greater use of available program support, notably FTA's 5311(f) program, and working more closely with alternative carriers to sustain service. The combination of carrier and State response is helping to mitigate effects of Greyhound's cutbacks—where there have been impacts at all. Many of these same resources are available to provide intercity travel wherever Amtrak cutbacks might occur.

The administration's SAFETEA proposals also increase long-distance travel options, especially for those dependent upon access to publicly available transportation, through expanded support for intercity bus service. SAFETEA's measures include funding of intermodal terminals used by intercity bus carriers; increasing Section 5311(f)'s funding for rural area intercity bus service and strengthening the Section's provisions for State and carrier cooperation; ensuring intercity bus access to publicly funded intermodal passenger facilities; and continued funding of lift equipment that helps carriers meet the Americans with Disabilities Act accessibility requirements. All of these measures seek improved access to the Nation's intercity travel network, and we are very hopeful that emerging reauthorization legislation preserves support for these measures.

The administration's passenger rail proposal, the Passenger Rail Investment Reform Act, includes a new Federal-State partnership to fund capital improvements, much like the successful programs relied on in other modes of transportation, especially the Federal Transit Administration's (FTA) Section 5309 New Starts Program. The Federal Government will offer 50–50 matching grants to States for development of infrastructure projects that improve passenger rail service. The matching grants will provide an incentive for States to make capital investments that support high quality, integrated regional rail services.

As in the Section 5309 New Starts Program, regional, State or local authorities will be empowered to make decisions about rail passenger service, planning where it is and what best meets their transportation needs; they will also be in a position as well to ensure rail operators are providing a reliable, efficient and cost effective service. State and local governments are better situated to specify the service to be run, to monitor performance, and to control operating costs.

The most recent legislation to reauthorize Federal aviation programs, Vision 100 (Public Law 108–176), established an Alternate Essential Air Service Pilot Program and a Community Flexibility Pilot Program. By creating these pilot programs, Congress endorsed the idea that flexibility, needs assessment, and cost-effectiveness have roles to play in connecting communities to the air transportation system. For example, providing for on-demand surface transportation to another airport and promoting air taxi and charters in lieu of higher cost scheduled service were two provisions aimed at achieving rural area access to the Nation's air network more cost-effectively. This adherence to flexibility, needs assessment, and cost-effectiveness should contribute to the long-term assurance of mobility for the full spectrum of America's various transportation user groups.

SUBCOMMITTEE RECESS

Senator BOND. The hearing is recessed.

[Whereupon, at 11:32 a.m., Tuesday, March 15, the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

THURSDAY, APRIL 7, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:30 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Murray, and Dorgan.

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

STATEMENTS OF:

MARK W. EVERSON, COMMISSIONER

J. RUSSELL GEORGE, TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning. The Senate Appropriations Subcommittee on Transportation, Treasury, Judiciary, Housing, Urban Development, and Related Agencies will come to order. I'm going to have to get used to that, Senator Murray. The committee is often called the THUD committee but we will go with the full name for this event.

We welcome Internal Revenue Service Commissioner Mark Everson and J. Russell George, the Treasury Inspector General for Tax Administration to this morning's hearing. I look forward to hearing each of your views on the IRS's fiscal year 2006 budget as well as issues related to the administration and enforcement of our Nation's tax code. With the April 15 tax filing deadline rapidly approaching, you can see everybody smiling about what a wonderful day that will be. As a result, we're especially looking forward to Commissioner Everson's testimony on the current state of the IRS and how the service is responding not only to taxpayers' needs but what has become popularly described as the "tax gap"; namely, what taxes should be paid and what taxes are actually paid.

We also are looking forward to the IG's perspective on the strengths and weaknesses of the IRS's capacity to effectively collect taxes.

As I understand the budget request for 2006, the IRS is making renewed efforts to reduce the tax gap through an increased investment in enforcement funding. I understand and support these efforts. Closing this gap is especially important as the Federal Government seeks to reduce the deficit and reform Social Security. I believe that those of us who pay taxes as we should bear a heavy burden when 15 percent of taxes that are owed are not collected. Consequently, I've appreciated discussions about how we can close that gap so that we can get the taxes that are actually owed and enable the government to lower the deficit that we face.

In particular, the IRS is proposing to close this gap by increasing the Nation's investment in enforcement, proposing an 8 percent increase in enforcement. Moreover, the budget proposes that no less than $6.446 billion must be used exclusively for tax enforcement, which would result in an additional $446.5 million in contingent funding for appropriations. The use of this budget mechanism is justified because the government collects $4 for every $1 spent for enforcement. I'm not convinced of the arithmetic. I am convinced, however, additional enforcement spending will result in additional collections. This is true despite the fact that the strength and weakness of our Nation's Federal income tax system is its reliance on the voluntary compliance of American taxpayers. Most Americans believe in the law and pay their taxes. Nevertheless, there will always be some that fail to comply or engage in outright fraud. This is the IRS's greatest managerial challenge and I believe the IRS should have the resources to meet that challenge.

That's why effective enforcement of the tax laws are so critically important and why I support an increase in the funding for enforcement efforts. Enforcement cannot be lax, ineffective, or uneven; otherwise, more people will be encouraged to commit fraud. We also must ensure enforcement funds are used for enforcement and not other priorities. I'm disappointed that the subcommittee does not get adequate credit under the convoluted budget scoring principles for the savings achieved through enforcement, especially since OMB has proposed the underfunding of so many other parts of our bill. If we could get credit for the additional collections coming from enforcement, we would be able to meet many of our threshold needs. However, the overall budget has been cut by 2 percent with many functions in our budget requiring cost-of-living increases which are not addressed. Housing, for example, does not get 2 percent less expensive. As a result, this budget puts us in a very difficult position, a theme that we will be reiterating in our discussions with all of the other agencies that come before us.

The primary mission of the IRS is to ensure the full and fair compliance of all taxpayers to meet their tax obligations. This is the underlying purpose of the IRS's budget. However, I'm concerned about the proposed 1 percent decrease in taxpayer service funding. The IRS needs to balance customer service with its compliance and enforcement efforts. As a result, the IRS must provide high quality and in-depth customer service to assist taxpayers, especially low-income taxpayers. I believe that most people who fail to comply with the code do so unintentionally because of its difficulty and complexity. Active and timely guidance from the service is imperative to ensure taxpayer compliance.

Nevertheless, I remain concerned about the proposed reduction in customer service, especially since the IRS has improved its customer service and guidance over the past 2 years. I'm especially impressed over the improvement through internet, telephone, and in-person assistance. E-file options have become especially important, helping to reduce the burden of filing tax returns both for the government and the taxpayer.

Unfortunately, the biggest hurdle facing taxpayers and the IRS and all of us is the Federal Tax Code, its regulations and other guidance, which constitute more than 54,000 pages. It is too complex, too confusing, and too costly. On a daily basis, I hear complaints from small tax practitioners and businesses that the code has become unmanageable and confusing, resulting in excessive cost and administrative burdens that far exceed reasonable tax compliance. I believe it was Walt Kelly's "Pogo" who said those famous words, "We have met the enemy and he is us". This is our responsibility and, unfortunately, even with all the wisdom in the Appropriations Committee, we don't write the tax code. Nevertheless, I firmly support a comprehensive reform of the tax code based on simplicity and reasonableness. This alone would result in substantially reduced tax fraud by making the process simpler and the system far fairer for all taxpayers.

Finally, I direct concerns to an area of particular importance to me: the ongoing efforts of the IRS to modernize the IRS computer system known as Business System Modernization or BSM. The ultimate success of this system is critical to collections. Historically, the IRS has long been dependent upon antiquated computer systems to perform basic tax administration activities. As a result, Congress created a special business systems account to fund the replacement of these outdated systems. Nevertheless, the cost for BSM is fast approaching $2 billion. The key feature of the modernization program and the customer account data engine, with acronym being CADE, is hampered by development problems and cost overruns while remaining inadequate and ineffective. For example, the report on Custodial Accounting Project, CAP, showed that it was significantly behind schedule and over budget. This system was designed to correct longstanding weaknesses in the IRS financial management systems, which account for approximately $2 trillion in tax collections annually. Additionally, TIGTA found the IRS and CAP contractor did not adequately manage system requirements. In another example, TIGTA reported that the security audit system used to record the online activity of IRS employees through audit trails was accepted by IRS even though the required functions the IRS paid for were not operating. The bottom line is that scheduling and cost estimation have been a big problem. Almost every system is behind schedule and over cost and is delivering less functionality than originally planned.

Commissioner, your budget request is $199 million for BSM. I'm not convinced this system works adequately, but ultimately the IT system is the heart of the entire collection and compliance system. BSM must be fixed and must be made workable to establish clearer requirements and benchmarks for its progress. As I understand it, the system was supposed to be completed in 10 years. I don't believe anyone believes this schedule is now achievable as schedule delays and cost over-runs continue to rule—this is not the exception in this ongoing effort: schedule slippages and cost over-runs have been epidemic and, in fact, I believe the IRS is running late and is over-budget on all seven core projects related to BSM. I'm concerned BSM is becoming the 21st century version of the TSM program which was the IRS's prior modernization effort that was abandoned after 6 years and $4 billion. TSM was a total loss. The current BSM effort began in 1998 and has already cost $2 billion. This program, like TSM before it, raises more questions than answers.

PREPARED STATEMENT

Commissioner, I support your efforts in enforcement and closing the tax gap. I applaud your efforts but an effective BSM is critical. I'm looking forward to working with you and the IRS on these efforts. I also applaud your commitment on addressing the funding, schedule, and requirement needs of the BSM. I thank you for coming to testify today and I look forward to your testimony and the testimony of Mr. George on the many challenges confronting the IRS in the 21st century. It's now my pleasure to turn to my ranking member, Senator Murray.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, Housing and Urban Development and Related Agencies will come to order. We welcome Internal Revenue Service Commissioner Mark Everson and J. Russell George, the Treasury Inspector General for Tax Administration, to this morning's hearing. I look forward to hearing each of your views on the IRS's fiscal year 2006 budget as well as issues related to the administration and enforcement of our Nation's tax code.

With the April 15 tax filing season deadline rapidly approaching, we are especially looking forward to Commissioner Everson's testimony on the current state of the IRS and how the Service is responding not only to taxpayers' needs but what has become popularly described as the "Tax Gap"; namely, what taxes should be paid and what taxes are actually paid. We also are looking forward to the IG's perspective on the strengths and weakness of the IRS's capacity to effectively collect taxes.

As I understand the budget request for fiscal year 2006, the IRS is making renewed efforts to reduce the tax gap through an increased investment in enforcement funding. I understand and support these efforts. Closing this gap is especially important as the Federal Government seeks to reduce the deficit and reform social security.

In particular, the IRS is proposing to close this gap by increasing the Nation's investment in enforcement by proposing an 8 percent increase in enforcement. Moreover, the budget proposes that no less than $6.446 billion be used exclusively for tax enforcement which would result in an additional $446.5 billion in contingent funding for appropriations. The use of this budget mechanism is justified because the government collects $4 for every $1 dollar spent for enforcement. While I am not convinced of the arithmetic, I am convinced that additional enforcement spending will result in additional collections to a point. This is true despite the fact that the strength and weakness of our Nation's Federal income tax system is its reliance on the voluntary compliance of American taxpayers. Most Americans believe in the law and pay their taxes. Nevertheless, there will always be some that fail to comply or engage in outright fraud. This is the IRS's greatest managerial challenge and the IRS should have the resources.

That is why effective enforcement of our tax laws is so critically important, and why I support an increase in the funding of enforcement efforts. Enforcement cannot be lax, ineffective, or uneven; otherwise more people will be encouraged to commit fraud. We must ensure enforcement funds are used for enforcement and not other priorities. I am disappointed that the subcommittee does not get adequate credit and savings for its investment in enforcement, especially since the administration has proposed underfunding of so many other parts of our bill.

The primary mission of the IRS is to ensure the full and fair compliance of all U.S. taxpayers with their tax obligations. These efforts cannot through enforcement and compliance solely. Consequently, I am very troubled by the proposed 1 percent decrease in Taxpayer Service funding. The IRS needs to balance customer service with its compliance and enforcement efforts.

As a result, the IRS must provide high quality and in-depth customer service to assist taxpayers, especially low-income taxpayers. I believe that most people who fail to comply with the code do so unintentionally because of its difficulty and complexity. Accurate and timely guidance from the Service is imperative to ensuring taxpayer compliance.

Nevertheless, while I remain concerned about the proposed reductions in customer service, the IRS has improved its customer service and guidance over the past few years. I especially am impressed over improvements through the internet, telephone and in-person assistance. E-file options have become especially important, helping to reduce the burden of filing tax returns for both the government and the taxpayer.

Unfortunately, the biggest hurdle facing taxpayers and the IRS is the Federal tax code, its regulations and other guidance, which has morphed to more than 54,000 pages—this is too complex, confusing, and costly. On an almost daily basis, I hear complaints from small tax practitioners and businesses that the Code has become unmanageable and confusing, resulting in excessive cost and administrative burdens that far exceed reasonable tax compliance. I firmly support a comprehensive reform of the tax code that is founded in simplicity and reasonableness. This alone would result in substantially reduced tax fraud by making the process simpler and the system far fairer for all taxpayers.

Finally, I'd like to direct my concerns to an area of particular importance to me: the ongoing efforts of the IRS to modernize the IRS computer systems, known as Business Systems Modernization (BSM). The ultimate success of this system is critical to collections.

Historically, the IRS has been long dependent upon antiquated computer systems to perform basic tax administration activities. As a result, Congress created a special business systems modernization account to fund the replacement of these outdated systems. Nevertheless, the cost for the BSM program is fast approaching $2 billion. The key feature of the modernization program, Customer Account Data Engine (CADE), is hampered by delays in development and cost overruns while remaining inadequate and ineffective.

For example, TIGTA's report on the Custodial Accounting Project (CAP) showed that it was significantly behind schedule and over budget. This system was designed to correct longstanding weaknesses in the IRS financial management systems systems, which account for approximately $2 trillion in tax collections annually. Additionally, TIGTA found the IRS and the CAP contractor did not adequately manage system requirements. In another example, TIGTA reported that the system (Security Audit and Analysis System) used to record the online activity of IRS employees through audit trails which was accepted by IRS even though the required functions IRS paid for were not operating.

The bottom line is that scheduling and cost estimation have been a very big problem for IRS. Almost every system is behind schedule, over cost, and is delivering less functionality than originally planned.

Mr. Commissioner, your budget request seeks $199 million for BSM. I am not convinced this system works, but ultimately the IT system is the heart of the entire collection and compliance system. BSM must be fixed. IRS needs to establish clear requirements and benchmarks for progress. As I understand it, this system was supposed to be completed in 10 years. I do not believe that anyone believes this schedule is now achievable and schedule delays and cost overruns continue to be the rule—not the exception—to this ongoing effort. These schedule slippages and cost-overruns have been epidemic. In fact, I believe the IRS is running late and is over budget on all seven core projects related to BSM.

I am very concerned that BSM is becoming the 21st century version of the Tax Systems Modernization (TSM) program, which was the IRS's prior modernization effort that was abandoned after consuming 6 years and $4 billion in Federal tax dollars. That effort was a complete loss.

The current BSM effort began in 1998 and has already cost almost $2 billion. This program, like TSM before it, raises more questions than answers.

Commissioner Everson, I support your efforts in enforcement and closing the tax gap. I applaud your efforts. However, an effective BSM is critical to these efforts. I am looking forward to working with you on these efforts. However, I also am looking to your commitment on addressing the funding, schedule and requirement needs of the BSM.

I thank you again coming to testify before the subcommittee this morning. I look forward to your testimony and the testimony of Mr. George on the many challenges confronting the IRS in the 21st century.

I now turn to my Ranking Member, Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Thank you very much. Mr. Chairman, I want to welcome back IRS Commissioner Everson and I want to welcome Russell George who is our new Treasury Inspector General for Tax Administration testifying before this subcommittee for the first time. In 8 days, millions of Americans who play by the rules will go to the post office to file their tax returns. These honest taxpayers should be appalled by the IRS's findings released last week that reveal that the agency will fail to collect between a quarter and a third of a trillion dollars it's owed this year because of tax cheats. That figure is the equivalent of the amount we spent on the entire Department of Defense a couple of years ago. It represents roughly $1 out of every $5 that is owed by American taxpayers.

According to the IRS, the majority of these unpaid taxes take the form of unreported income by businesses, partnerships, estates, and so-called S corporations. Thankfully, the IRS now recognizes they need to get serious with tax cheats. The agency is asking for almost an 8 percent increase for tax law enforcement and a budget that is extremely frugal when it comes to other areas of domestic spending.

While some Senators have expressed concern that boosting IRS's enforcement budget could cost the agency to return to its troubled past when IRS agents used excessive force to harass taxpayers, I want to believe the agency has learned from its past mistakes and would use this funding boost to go after the real criminals. But what troubles me about this proposed IRS budget is the lack of balance between the desire to boost enforcement and the need to fund critical services to taxpayers. A detailed review of the budget request for the IRS shows that buried within the overall funding increase for the agency is almost a quarter billion dollars in anticipated cuts in current activities. Most disappointing is that the majority of those cuts come in the form of cuts in direct taxpayer services. Proposals to achieve these cuts include closing as many as one out of every four taxpayer assistance centers in the United States. The IRS wants to eliminate phone filing, a tool currently used by more than 5 million individuals and business every year. Other proposed cuts in taxpayer services include shortening phone service hours, discontinuing tax law assistance through the internet, limiting distribution of some outreach publications and face-to-face contacts with practitioners, and eliminating phone-routing sites and staffing.

In last year's hearing, the commissioner shared with us his motto that "service plus enforcement equals compliance". That motto is also prominently featured in his testimony this year. However, I fear a review of the budget request might indicate the motto should more appropriately be "only enforcement yields compliance so let's cut services to pay for it". I believe that service to taxpayers is still a critical mission of the IRS and I know I'm not alone in believing this. While a recent IRS Oversight Board Taxpayer Attitude Survey found that 62 percent of taxpayers thought the IRS should get more money for enforcement, 64 percent of taxpayers said the IRS should get more money to assist taxpayers on the phone and in person. But it's precisely those types of services that the IRS wants to cut.

PREPARED STATEMENT

Now, while she's not appearing before us today, I have reviewed the submitted testimony of the Taxpayer Advocate, Nina Olson. The Office of the Taxpayer Advocate was created by Congress so there would be staffed professionals with access to the commissioner to constantly look out for the interests of individual taxpayers as the IRS develops his processes and procedures. The Advocate is also charged with assisting taxpayers in resolving problems with the IRS and communicating the interests of taxpayers directly to Congress. According to Ms. Olson, closing taxpayer assistance centers at this time will irrevocably harm taxpayers. She points out that the IRS has not offered alternatives to the face-to-face interaction of these centers. It seems the only face-to-face alternative left is for affected taxpayers to drive much farther to another center. Especially because the IRS is moving so quickly on these new proposals, I would like to use a portion of today's hearing to discuss in detail precisely what the impact will be on individual taxpayers resulting from IRS-proposed cuts, as called for in the administration's budget. The tax code is complicated enough without our cutting back on the level of assistance our citizens have come to expect as they seek to file the taxes accurately and on time. Thank you very much, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF SENATOR PATTY MURRAY

Thank you, Mr. Chairman.

I want to welcome back IRS Commissioner Everson. I also want to welcome Russell George, our new Treasury Inspector General for Tax Administration, who is testifying before us for the first time.

In 8 days, millions of Americans who play by the rules will go to the post office to file their tax returns. These honest taxpayers should be appalled by the IRS's findings, released last week, that reveal that the agency will fail to collect between a quarter and a third of a trillion dollars it is owed this year because of tax cheats.

That figure is the equivalent of the amount we spent on the entire Department of Defense a couple of years ago. It represents roughly $1 out of every $5 that is owed by American taxpayers.

According to the IRS, the majority of these unpaid taxes take the form of unreported income by businesses, partnerships, estates, and so-called "S-corporations."

Thankfully, the IRS now recognizes that they need to get serious with tax cheats. The agency is asking for almost an 8 percent increase for tax law enforcement in a budget that is extremely frugal when it comes to other areas of domestic spending.

While some Senators have expressed concern that boosting IRS's enforcement budget could cause the agency to return to its troubled past, when IRS agents used excessive efforts to harass taxpayers, I want to believe that the agency has learned from its past mistakes and would use this funding boost to go after the real criminals.

What troubles me about this proposed IRS budget is the lack of balance between the desire to boost enforcement and the need to fund critical services to taxpayers. A detailed review of the budget request for the IRS reveals that buried within the overall funding increase for the agency is almost a quarter billion dollars in anticipated cuts in current activities.

Most disappointing is that the majority of those cuts come in the form of cuts in direct taxpayer services. Proposals to achieve these cuts include closing as many as one out of every four Taxpayer Assistance Centers in the United States.

The IRS wants to eliminate phone filing, a tool currently used by more than 5 million individuals and businesses every year. Other proposed cuts in taxpayer services include:

—shortening phone service hours;

—discontinuing tax law assistance through the Internet;

—limiting distribution of some outreach publications and face-to-face contact with practitioners; and,

—eliminating phone-routing sites and staffing.

In last year's hearing, the Commissioner shared with us his motto that, "Service Plus Enforcement Equals Compliance." That motto is also prominently featured in his testimony this year. However, I fear a review of the IRS's budget request might indicate that the motto should more appropriately be: "Only Enforcement Yields Compliance—So Let's Cut Services to Pay For It."

I believe that service to taxpayers is still a critical mission of the IRS—and I know I am not alone in believing this. While a recent IRS Oversight Board Taxpayer Attitude Survey found that 62 percent of taxpayers thought that the IRS should get more money for enforcement, 64 percent of taxpayers said that the IRS should get more money to assist taxpayers on the phone and in person.

But it is precisely those types of services that the IRS wants to cut.

Now, while she is not appearing before us today, I have reviewed the submitted testimony of the Taxpayer Advocate, Nina Olson. The Office of the Taxpayer Advocate was created by Congress so that there would be staffed professionals with access to the Commissioner to constantly look out for the interests of individual taxpayers as the IRS develops its processes and procedures.

The Advocate is also charged with assisting taxpayers in resolving problems with the IRS and communicating the interest of taxpayers directly to Congress.

According to Ms. Olson, "closing Taxpayer Assistance Centers at this time will irrevocably harm taxpayers." She points out that the IRS has not offered alternatives to the face-to-face interaction of these centers. It seems the only face-to-face alternative left is for affected taxpayers to drive much farther to another center.

Especially because the IRS is moving so quickly on these new proposals, I would like to use a portion of today's hearing to discuss in detail precisely what the impact will be on individual taxpayers resulting from IRS-proposed cuts, as called for in the administration's budget.

The tax code is complicated enough without our cutting back on the level of assistance our citizens have come to expect as they seek to file their taxes accurately and on time.

Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Murray. Senator Dorgan, do you have a brief opening statement?

STATEMENT OF SENATOR BYRON L. DORGAN

Senator DORGAN. Mr. Chairman, first of all, thank you for holding this hearing. I think recent announcements about the size of the tax gap should cause all of us great concern. It's something I want to visit with the IRS officials about. Also, the issues of taxpayer assistance, I assume my colleague was just discussing that as I walked in. Let me defer and hear from the commissioner and then I will ask some questions.

Senator BOND. Thank you very much, Senator Dorgan, and Commissioner Everson, we're making your full statement part of the record and I believe you have provided a summary. We invite you to give that now. Thank you.

STATEMENT OF MARK W. EVERSON

Mr. EVERSON. Chairman Bond, Ranking Member Murray, Senator Dorgan, I'm happy to be here. I appreciate the opportunity to testify on the President's request.

The President's 2006 request for the IRS is crafted to continue the necessary rebuilding of our enforcement capabilities, and it maintains a stable commitment to our important IT modernization program. Enforcement and modernization were categorized earlier this year by the GAO as high risk areas of government-wide importance. The 2006 budget request calls for a modest amount of belt-tightening in taxpayer services. The cut to services of 1 percent is consistent with the requests for domestic discretionary programs other than those associated with homeland security. In a report issued last year, the GAO stated, "Taxpayer services are much improved, raising a question about the appropriate balance to strike between investing in further service improvements and enforcement. At the same time, the use of IRS's walk-in assistance sites is declining. The improvements in telephone service, increased web site use, and the availability of volunteer sites raise a question about whether the IRS should continue to operate as many walk-in sites. Reconsidering the level and types of services is an option—but not a recommendation—to be considered by IRS management and the Congress."

[The information follows:]

GAO'S COMMENTS ON WALK-IN ASSISTANCE

". . . the use of IRS's walk-in assistance sites is declining. The improvements in telephone service, increased Web site use, and the availability of volunteer sites raise a question about whether IRS should continue to operate as many walk-in sites. Reconsidering the level and types of service is an option—but not a recommendation—to be considered by IRS management and the Congress."—Statement of James R. White, Director, Tax Issues.

PRESIDENT'S BUDGET REQUEST

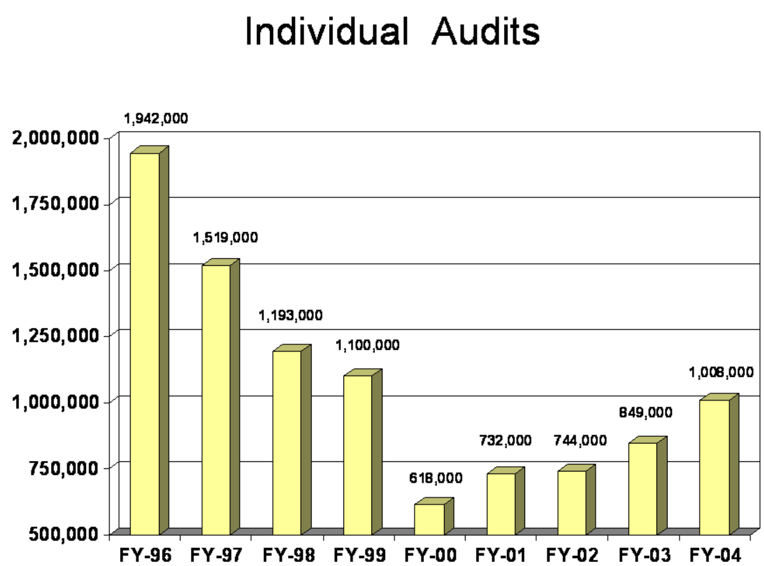
The President's request for the IRS adopts just this approach. I am comfortable with this request and support it wholeheartedly. I want to stress to you, Senator Murray, that I believe that we will provide good services. If enacted at the requested level without constraining language, we will continue to do our job on the service front.

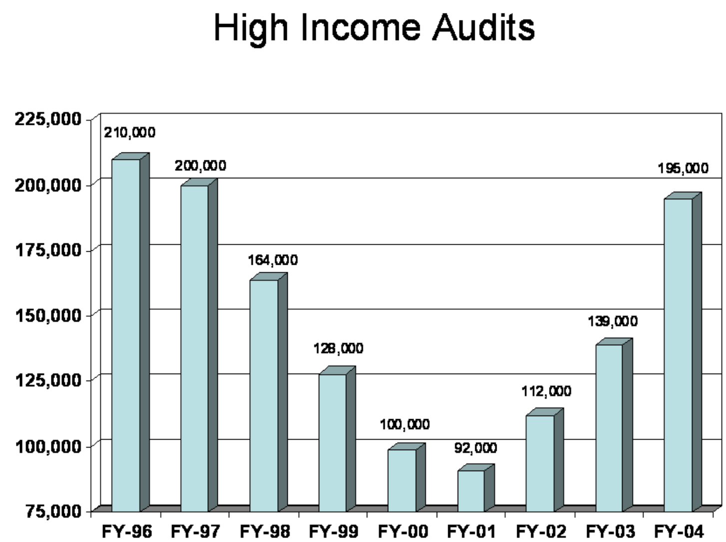
The budget will hold Business System Modernization funding steady at substantially the same level as 2005. In terms of modernizing our big computer systems at the IRS, after years of cost overruns and missed delivery dates, we've finally turned the corner. In the past 9 months, two important systems have come on-line. We have a new financial system to help better manage the agency, and more importantly, this filing season the IRS has already processed over 1 million 1040EZ tax returns using the first new processing system in 40 years. The 2006 budget continues investment in three critical areas: further work on return processing, collections, and electronic filing.

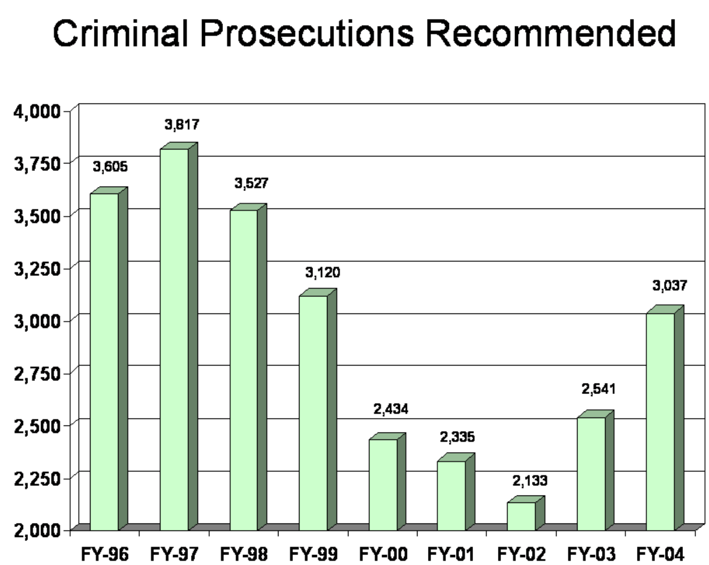
ENFORCEMENT FUNDING

Let me turn to the need for more enforcement funding.

As you mentioned, 2 weeks ago we announced that the gross tax gap—that's the difference between what taxpayers should pay and what they actually pay on a timely basis—exceeds $300 billion per year. Average Americans pay their taxes honestly and accurately and have every right to be confident that when they do so, neighbors and competitors are doing the same. We've taken some important steps to bolster this confidence.







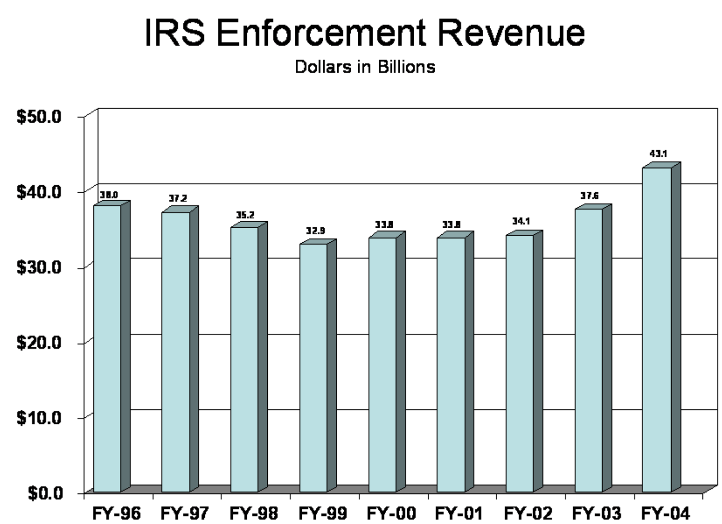
AUDIT RATES

We have ramped up our audits of individuals. You can see they've gone from 618,000, 4 years ago to over 1 million last year, and they will go up again in 2005. We've done this particularly for high-income individuals. You can see they've doubled from $192,000, pardon me, $92,000 to $195,000 over the same period, and they're going to go up again in a double-digit increase for 2005.

We are doing more with corporations and we're doing more with criminal investigations. This next chart shows the referrals we've made to the Justice Department, which have come up significantly in the last several years. We recently announced collections of over $3.2 billion in the settlement initiative for Son of Boss, a particularly abusive shelter.

The 2006 budget calls for nearly 8 percent increase for enforcement. This will enable us to expand our efforts over strategic compliance by corporations, individual taxpayers, and other contributors to the tax gap; ensure that attorneys, accountants, and other tax practitioners adhere to professional standards and follow the law; detect and deter domestic and off-shore based tax and financial criminal activity; and, deter abuse within tax-exempt and governmental entities and misuse of such entities by third parties for tax evasion or other unintended purposes. It's a very important subject that was the subject of an inquiry by the Finance Committee just 2 days ago.

These investments will pay for themselves several times over. The IRS yields more than $4 in direct revenue from its enforcement efforts for the money invested in its total budget, including our service and outreach activities. That's to say, the $43 billion in enforcement revenue compares to the $10.2 billion we are appropriated. The $10.2 billion includes everything we do, not just the enforcement, but the processing and the outreach, all those activities.

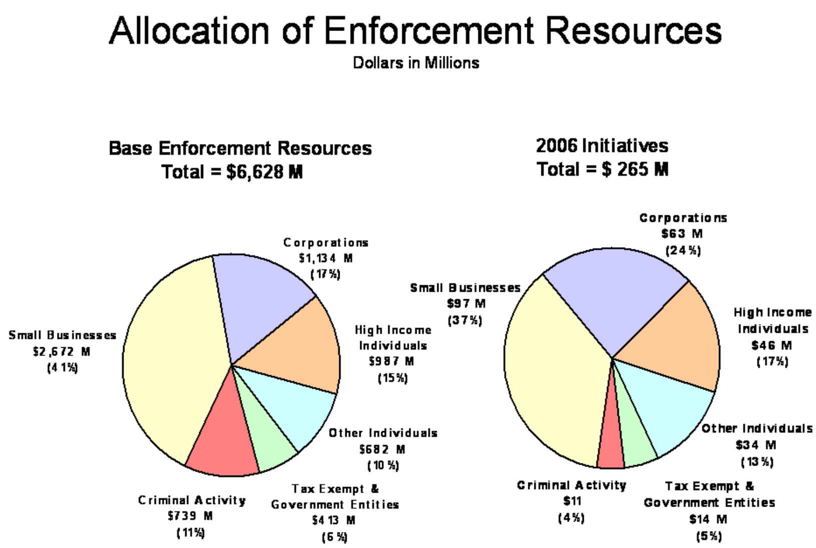


ENFORCEMENT REVENUE

Now, last year, the $43 billion, that represented a 15 percent increase from the year before, so you can see that is coming up. That is a result of all the other things you saw. I want to emphasize that these figures exclude the positive impact on compliance that occurs when someone learns in a casual conversation that their neighbor has been audited and then thinks twice about fudging his or her own return. So this is just the direct return.

Let me make one additional point that the chairman has touched upon about enforcement.

The President's budget calls for the Congress to adjust its 302(a) allocation to the Appropriations Committee up to $446 million, once the base level of $6.4 billion for IRS enforcement is fully funded and restricted for use only on IRS enforcement. The $446 million consists of $265 million for new enforcement initiatives and $182 million for maintaining current enforcement levels.



BUDGET RESOLUTION

The Senate Budget Resolution contains language which would allow this proposal to proceed. The House Resolution does not. I urge you to see the Senate position maintained during the conference. This proposal will allow the IRS to devote resources where needed: in enforcement. Thank you.

[The statement follows:]

PREPARED STATEMENT OF MARK W. EVERSON

INTRODUCTION

Chairman Bond, Ranking Member Murray, and members of the subcommittee, thank you for the opportunity to testify today on the fiscal year 2006 budget request for the Internal Revenue Service.

Our working equation at the IRS is service plus enforcement equals compliance. The better we serve the taxpayer, and the better we enforce the law, the more likely the taxpayer will pay the taxes he or she owes.

This is not an issue of service OR enforcement, but service AND enforcement. As you know, IRS service lagged in the 1990's. In response, we took important and necessary steps to upgrade service—we significantly improved the answering of taxpayer telephone inquiries and electronic filing to name just a couple areas.

Unfortunately, improvement in service coincided with a drop in enforcement of the tax law. After 1996, the number of IRS revenue agents, officers, and criminal investigators dropped by over 25 percent.

TAX GAP

We currently have a serious tax gap—the difference between what taxpayers are supposed to pay and what is actually paid—in this country. The results of the National Research Program indicate the Nation's tax gap increased slightly to between $312 billion and $353 billion in tax year 2001. This compares to the old tax gap estimate for 2001 of $311 billion based on earlier studies. By our best estimates, we lose almost $300 billion each year due to non-filing, underreporting, and underpayment, although this number reflects the fact that we do eventually recover about $55 billion of the gross tax gap.

We launched the National Research Program (NRP) in 2001. We designed the NRP to measure individual taxpayer reporting compliance for tax year 2001. Over the course of the next 3 years, we randomly selected about 46,000 returns for review and examination. We largely completed these audits by the fall of 2004. To gather statistically valid data, the return selection process for the NRP included an oversampling of high income returns. This enables IRS researchers to draw valid conclusions about important sub-categories of taxpayers.

For instance, slightly more than 6 percent of individual taxpayers filed Schedule C as sole proprietors in 2001. These taxpayers reflect a wide range of economic activity. To draw valid conclusions on Schedule C filers, the NRP examined about 21,000 individuals who filed a Schedule C, slightly less than 46 percent of the total sample.

The current data from the NRP are preliminary, so the results are shown as ranges. As refinements are made to the tax gap analysis, some of these estimates may change. It is unlikely, but possible, that the final estimates of the tax gap will fall outside of the established range.

The tax gap figure does not include taxes that should have been paid on income from the illegal sector of the economy.

For Tax Year 2001, all taxpayers paid $1.77 trillion on time, a figure that represents from 83.4 percent to 85 percent of the total amount due. The 2001 tax gap, the difference between taxes owed and taxes paid on time is from $312 billion to $353 billion for all types of taxes.

Overall, the noncompliance rate is from 15 percent to 16.6 percent of the true tax liability. The old estimate, derived from compliance data for Tax Year 1988 and earlier, was 14.9 percent.

Late payments and other IRS enforcement and compliance efforts, including taxpayer audits and collection activities (payment arrangements, liens, levies and other legal actions) recover some of the Tax Gap. For Tax Year 2001, we expect eventually to collect an additional $55 billion of the tax gap, reducing the net amount of the tax gap to between $257 billion and $298 billion.

Among the areas where taxpayer compliance appears to have worsened are:

—Reporting of net income from flow-through entities, such as partnerships and S corporations;

—Reporting of proprietor income and expenses, such as gross receipts, bad debts and vehicle expenses; and,

—Reporting of various types of deductions.

Among the areas where compliance seems to have improved is the reporting of farm income.

Overall, compliance is highest where there is information reporting and/or withholding. For example, most wages, salaries and tip compensation are reported by employers to the IRS through Form W–2. Preliminary findings from the NRP indicate that less than 1.5 percent of this type of income is misreported on individual returns.

IRS researchers anticipate identifying other specific areas of deterioration and improvement in the coming months as they complete the detailed analysis of the study's data.

Today I will give you an update on what we've accomplished over the past year, speaking in particular about enforcement, the area where our challenges remain the greatest. We must restore the balance between service and enforcement, but that will not come at the expense of taxpayer service. In recent years, we have begun to attack the decline in enforcement by revitalizing our investigations, audits and prosecutions against those who do not pay their taxes. The President's fiscal year 2006 budget—if approved by Congress—will help with our efforts to boost enforcement while maintaining our levels of service. This budget includes $265 million for initiatives aimed at enhancing the enforcement of tax laws.

Before I talk specifically about our fiscal year 2006 budget request, let me first talk about our progress in service. By service, we mean helping people understand their tax obligations and making it easier for them to participate in the tax system.

Electronic filing continues to grow. Last year Americans filed over 61 million electronic returns. This year we expect that over half of all individual returns will be e-filed. Thus, it appears that individuals who file on paper will soon be in the minority. We take every opportunity we can to proclaim the benefits of electronic filing, including a reduction in processing errors and cost savings for taxpayers and the IRS. E-filing is fast, convenient and gets your refund to you in half the time of paper returns.

Use of our website, IRS.gov, is also up sharply. During the filing season, it is one of the busiest websites in the world. We average more than 1 million visits a day. Just to give you a frame of reference: one major search engine reported that in a recent week we were surpassed only by Paris Hilton, Clay Aiken, Pamela Anderson, Britney Spears, and a poker game. During the past year, we have also rolled out important new on-line services to tax professionals to help them better serve their clients.

In terms of modernizing our big computer systems at the IRS, we've finally turned the corner. Since March 2004, two important systems have started operating. First, we have a new financial system to help better manage the agency. And secondly, and more importantly, for the first time in 40 years, the IRS is processing tax returns on a new computer system. We started with 1040EZ returns and have processed over 1 million as of April 4. This is a big step forward in our effort to modernize our antiquated computer systems.

CONTINUING SERVICE AND INCREASING ENFORCEMENT

We are quite aware of the need to operate efficiently, consolidate operations and drive down costs wherever we can. In today's fiscal environment, we recognize that resources are tight. Nevertheless, we are determined to do all we can to improve service and modernize the IRS. In the last several years, we have begun to arrest the decline in enforcement and stabilize IRS enforcement staffing; now 73 percent of taxpayers completely agree that it is every American's duty to pay their fair share of taxes, up from 68 percent in 2003. A 2004 IRS Oversight Board commissioned NOP World study revealed 79 percent of taxpayers believe it is very important for the IRS to enforce compliance from high-income individuals and 85 percent believe it is very important for the IRS to enforce compliance from corporations. But in order to continue to reverse the downward trend of compliance, we must continue to use our resources wisely.

We are working aggressively to improve productivity and achieve cost savings, which we will apply to other priority areas, such as enforcement. The fiscal year 2006 budget reduction initiatives focus mainly on targeted reductions in assistance, outreach, and processing program areas. Reductions will also be achieved through improved efficiencies and re-engineering of business processes in key program areas in accounts management, submission processing, media and publications, field assistance, and outreach and education. Approximately 65 percent of these reductions will occur in assistance, 20 percent in outreach and 15 percent in processing. We will minimize the impact on taxpayers by providing alternative means to obtain service, wherever possible. Our budget estimates all these taxpayer service reengineering initiatives will yield $134 million in savings we can reinvest in other program areas. The reductions represent a balanced approach in program delivery and service to taxpayers to enable them to meet their tax obligations.

We estimate savings of $75 million to $95 million from additional efficiencies in our field assistance, accounts management and toll-free telephone operations. We will achieve these savings, in part, because of our recent consolidation our Customer Accounts Service organizations and revamping our business processes. For example, due to the steady decline in taxpayers corresponding with us about their accounts, we will need fewer resources to manage these accounts. We are also adjusting the hours of our toll-free telephone operations from 15 to 12 hours daily, Monday through Friday in the local times zones, beginning in 2005. We expect minimal impact to our level of service for taxpayers who call us. Another portion of these savings will come from reducing the number of walk-in sites. In recent years, the number of taxpayers walking into a Taxpayer Assistance Center (TAC) site for assistance has decreased from a high of nearly 10 million contacts in fiscal year 2000 to about 7.7 million contacts in fiscal year 2004. This trend reflects the increased availability and quality of services that do not require travel or waiting in line. Examples include improved access to IRS telephone service, the increasing availability of volunteer assistance, and the many services now available through IRS.gov, such as "Free File" and "Where's My Refund." In addition, the ability to download forms online has also contributed to the decline in the number of customers walking into a TAC. We have also continued to improve our telephone service for taxpayers who call the IRS with questions. The use of other alternatives, such as volunteer return assistance at Volunteer Income Tax Assistance (VITA) sites and Tax Counseling for the Elderly (TCE) sites, has steadily increased while the number of TAC contacts decreased. In fiscal year 1999, for example, VITA sites filed almost 584,000 returns, and TCE sites filed 446,000 returns. In the next 5 years, the numbers of returns filed through these sites increased 88 percent, reaching 976,000 VITA returns and 958,000 TCE returns in fiscal year 2004.

Because of these other options, fewer taxpayers need to travel to an IRS office to get the services they need. There are currently about 400 TAC sites across the country which are serviced by approximately 2,300 TAC employees. We believe that adjusting the TAC sites to more closely align to this decreased walk-in volume will yield staffing and building cost savings of $45 million to $55 million of the $75 million to $95 million in savings, and allow us the flexibility to improve efficiencies and concentrate more on front-line enforcement.

We have developed a criteria model that measures the impact on taxpayers across the country. The criteria include: location, employee cost, facilities cost, workload, and demographic measurements. In anticipation of the closing of approximately 70 TACs and their employees, we have requested authority to offer early-outs and buyouts to all eligible IRS TAC personnel. We expect to have further announcements in the near future.

In addition to reducing the number of TAC sites, we will save $20 million to $31 million in outreach programs though reductions in printing and postage and additional efficiencies in our outreach organizations. For example, we will save more money in printing and postage as taxpayers shift to e-filing, and as we eliminate redundant services and publications.

We will save another $17 million to $23 million by retiring Telefile, implementing program enhancements in the processing of employment tax returns, and re-engineering processes in Submission Processing. We will redirect taxpayers who previously used Telefile to e-file alternatives, such as Free File, that are available through IRS.gov so we maintain an acceptable level of service.

Though we are re-engineering how we provide service, we will continually strive to improve service to taxpayers. Having stated this, I must address the fundamental issue of enforcement.

While the President's Budget Request to Congress would increase IRS enforcement activities by 7.8 percent, given the current budgetary constraints, we responsibly proposed to reduce spending in other areas throughout the Service. We are confronted with difficult choices.

Average Americans pay their taxes honestly and accurately, and have every right to be confident that when they do so, their neighbors and competitors are doing the same. Let me provide an overview of the steps we have taken over the past year to bolster this confidence, turning briefly to each of our four service-wide enforcement priorities.

Our first enforcement priority is to discourage and deter non-compliance, with emphasis on corrosive activity by corporations, high-income individuals, and other contributors to the tax gap.

—In 2004, audits of high-income taxpayers jumped 40 percent from the year before. We audited almost 200,000 high-income individuals last year—double the number from 2000.

—Overall, audits for individuals exceeded the 1 million mark last year, up from 618,000 4 years earlier.

—In 2004, the number of audits of the largest businesses—those with assets of $10 million or more—finally increased after years of decline.

The centerpiece of our enforcement strategy is combating abusive tax shelters, both for corporations and high-income individuals. I will touch upon two important initiatives of the past 12 months.

We have continued our program of settlement offers for those who entered into abusive transactions in the past but would like to get their problems behind them. Last May, we made a settlement offer regarding the Son of Boss tax shelter, a particularly abusive transaction used by wealthy individuals to eliminate taxes on large gains, often in the tens of millions of dollars. In this program, for the first time, the IRS required a total concession by the taxpayer of artificial losses claimed. I am pleased with the response to the offer. So far, $3.2 billion in taxes, interest and penalties have been collected from the 1,165 taxpayers who are participating in the settlement initiative. The typical taxpayer payment was almost $1 million, with 18 taxpayers paying more than $20 million each and one paying over $100 million. Processing of individual settlements continues.

Based on disclosures we have received from promoter investigations and from investor lists from Justice Department litigation, we have determined that just over 1,800 people participated in Son of Boss. When the project concludes in the coming months, we expect the collected figure should top $3.5 billion.

In February 2005, we announced a second important settlement initiative—this one involving executive stock options. This abusive tax transaction involved the transfer of stock options or restricted stock to family-controlled entities. These deals were done for the personal benefit of executives, sometimes at the expense of public shareholders. This shelter was not just a matter of tax avoidance but, in some instances, raises basic questions about corporate governance. Again, the settlement offer is a tough one: full payment of the taxes plus a penalty.

A noteworthy point about the stock option settlement offer is that our actions in this matter were closely coordinated with the Securities and Exchange Commission and the Public Company Accounting Oversight Board.

Our settlement initiatives and increased audits have sent a signal to taxpayers: the playing field is no longer as lopsided as it once was. Non-compliant taxpayers might have to pay the entire tax, interest, and a stiff penalty. A taxpayer might have to wrestle with questions like “how much am I going to have to pay the lawyers and expert witnesses to litigate this thing?” Moreover, going to court is a public matter. Damage to one’s reputation is a potential factor. Many wealthy individuals, otherwise seen as community leaders, may not want to be identified as paying less than their fair share in taxes.

Another example of cooperation in the battle against abusive shelters is in the international arena. A year ago, I announced the formation of what has come to be known as the Joint International Tax Shelter Information Centre. Since last Labor Day, we have had an operational task force of personnel from Australia, Canada, the United Kingdom, and the United States working together on-site here in Washington. We are exchanging information about specific abusive transactions. Results to date are promising. Thus far, we have uncovered a number of transactions which, but for the Centre, we would have unraveled only over a number of years, if ever. It makes sense that we continue to work with other countries because, in this increasingly global world, we are up against what is, in essence, a reinforcing commercial network of largely stateless accounting firms, law firms, investment banks, and brokerage houses.

The government stepped up its use of civil injunctions in 2001 to prohibit promoters from selling illegal tax schemes on the Internet, at seminars or through other means. Currently the courts have issued injunctions against 99 abusive scheme promoters—81 permanent injunctions and 18 preliminary injunctions. They have issued injunctions against 17 abusive return preparers—all permanent injunctions. And an additional 49 suits have been filed by Justice seeking injunction action—28 against scheme promoters and 21 against return preparers. Injunctions issued have involved schemes such as:

—Using abusive trusts to shift assets out of a taxpayer’s name while retaining control;

—Misusing “corporation sole” laws to establish phony religious organizations;

—Using frivolous “Section 861” arguments to evade employment taxes;

—Claiming personal housing and living expenses as business expenses;

—Filing tax returns reporting “zero income”; and,

—Misusing the Disabled Access Credit.

The IRS has another 1,000 investigations ongoing for possible referral to the Department of Justice; and individual examinations are being conducted on thousands of scheme participants. Most of the investigations and examinations are being conducted by the IRS Small Business/Self-Employed (SB/SE) Division.

Our second enforcement priority is to assure that attorneys, accountants, and other tax practitioners adhere to professional standards and follow the law.

Our system of tax administration depends upon the integrity of practitioners. Altogether, there are approximately 1.2 million tax practitioners. The vast majority of practitioners are conscientious and honest, but even honest tax professionals suffered from the sad and steep erosion of ethics in recent years by being subjected to untoward competitive pressures. The tax shelter industry had a corrupting influence on our legal and accounting professions.

We have done quite a bit since March 2004 to restore faith in the work of tax professionals. We have strengthened regulations governing the standards of tax practice to discourage the manufacturing of bogus legal opinions on the validity of tax shelters. The IRS standards set forth rules governing what does and does not qualify as an independent opinion about a tax shelter.

Last year, the government won a series of court opinions on privilege. The cases established that promoters who develop and market generic tax shelters can no longer protect the identity of their clients by hiding behind a false wall of privilege.

Abusive tax shelters often flourished because penalties were too small. Some blue chip tax professionals actually weighed potential fees from promoting shelters, but not following the law, against the risk of IRS detection and the size of our penalties. Clearly, the penalties were too low. They were no more than a speed bump on a single-minded road to professional riches.

But these speed bumps have become speed traps. Last fall, Congress enacted the American Jobs Creation Act. The legislation both created new penalties and increased existing penalties for those who make false statements or fail to properly disclose information on tax shelters. Under the new law, the IRS can now impose monetary penalties not just on tax professionals who violate standards, but also on their employers, firms, or other entities if those parties knew, or should have known, of the misconduct.

Our third enforcement objective is to detect and deter domestic and off-shore based criminal tax activity and related financial criminal activity.

Last year, the IRS referred more than 3,000 cases to the Justice Department for possible criminal prosecution, nearly a 20 percent jump over the previous year. We continue our active role in the President's Corporate Fraud Task Force. We are going after promoters of tax shelters—both civilly and, where warranted, criminally. This tactic is a departure from the past. Previously, during a criminal investigation, all civil activity came to a halt. The result was that our business units were reluctant to refer matters for criminal investigation lest they lose their traditional turf. But, we are now moving forward on parallel tracks with the Department of Justice. We have a number of important criminal investigations. The enforcement model is changing.

Our fourth enforcement priority is to discourage and deter noncompliance within tax-exempt and government entities, and misuse of such entities by third parties for tax avoidance purposes.

Consider, for example, certain credit counseling agencies. Increasingly, it appears that some credit counseling organizations have moved from their original purposes, that is, to counsel and educate troubled debtors, to inappropriately enrolling debtors in proprietary debt-management plans and credit-repair schemes for a fee. These activities may be disadvantageous to the debtors and are not consistent with the requirements for tax exemption. Further, a number of these organizations appear to be rewarding their insiders by negotiating service contracts with for-profit entities owned by related parties. Many newer organizations appear to have been created as a result of promoter activity.

Some shelter promoters join with tax-exempt organizations to create abusive shelters. The organization receives a large fee from the taxpayer who is taking advantage of its tax-free status. That is an unintended abuse of the tax exemption that our Nation bestows upon charities.

It is heartening to see leading members of the nonprofit community taking steps to address abuses. I particularly want to salute the Independent Sector—which recently delivered a constructive report to the Senate Finance Committee. The report states that "government should ensure effective enforcement of the law" and calls for tougher rules for charities and foundations. The report calls for stronger action by the IRS to hold accountable charities that do not supply accurate and timely public information. I encourage the accounting, legal, and business communities to be as enthusiastic about confronting abuses and the erosion of professional ethics as the nonprofit community. An interesting point to note is that the report supports mandatory electronic filing of all tax returns for nonprofits.

The threat to the integrity of our Nation's charities is real and growing. At the IRS, we take it very seriously. We are augmenting our resources in the nonprofit area. By the end of September, we will have increased the number of our personnel who audit tax-exempt organizations by over 30 percent from 2 years earlier. If we do not act expeditiously, there is a risk that Americans will lose faith in our Nation's charitable organizations. If that happens, Americans will stop giving and those in need will suffer.

As we move forward with these priorities, we will leverage our success to achieve greater results within our fiscal year 2006 budget request.

BUDGET RESTRUCTURE

To facilitate full alignment and integration of the Service's goals and measures with its resources, we are proposing to restructure our budget beginning in fiscal year 2006. These changes will facilitate a more accurate assessment of the overall value of IRS programs, simplify the full costing of programs, and allow the IRS to demonstrate incremental increases in an initiative's effectiveness based on the level of funding received.

In addition, this new budget structure will enable us to manage activities more effectively. The normal processing of tax returns generally proceeds from pre-filing activities to filing activities, and finally to compliance activities, should they prove necessary. Although these activities are interrelated, we currently distribute their resources among three appropriations, with unevenly distributed support costs. This system makes it difficult to manage, track, and report the full cost of a given Taxpayer Service or Enforcement program.

This new budget structure will enable us to prepare a true performance-based budget by providing the capability to integrate operational and support costs into one appropriation, thereby allowing us to cost budget activities and programs fully for the first time. The new structure will also facilitate the full incorporation of performance measures into the budget, as the measures could be tied to funds in one appropriation rather than a series of program activities dispersed across multiple appropriations. The proposed new budget structure will allow stakeholders to assess more accurately the overall value of IRS programs, and make program reviews, such as the Office of Management and Budget's Program Assessment Rating Tool (PART), more effective, thus providing greater accountability and results-oriented management focus.

The proposed budget structure combines the three major appropriations accounts—Processing, Assistance and Management (PAM); Tax Law Enforcement (TLE); and Information Systems (ISY)—into one appropriation called Tax Administration and Operations (TAO).

The Taxpayer Service and Enforcement programs of the TAO appropriation are divided among eight critical program areas. These budget activities focus on Assistance, Outreach, Processing, Examination, Collection, Investigations, Regulatory Compliance, and Research. Full funding for each activity will be reflected in the budget, along with key performance measures. As we continue to move toward the development and implementation of this new structure, we will refine these program areas and the associated resource distributions to provide more accurate costing.

Let me now provide more details on the budget request for the IRS.

PRESIDENT'S FISCAL YEAR 2006 BUDGET SEEKS INCREASE IN ENFORCEMENT

The President's fiscal year 2006 budget requests $10.7 billion for the IRS, a 4.3 percent increase over the fiscal year 2005 enacted level. This request represents a 1 percent decrease in Taxpayer Service and a 2 percent decrease in Business Systems Modernization (BSM), but an 8 percent increase in enforcement.

This budget includes $265 million for initiatives aimed at enhancing the enforcement of tax laws. This request is above the increases to fund the pay raise and other cost adjustments ($182 million), for a total of $446 million for new enforcement investments and cost increases. It is important the Congress fully fund these cost increases and new enforcement investments. The President's budget proposal to fund them as contingent appropriations reflects the importance of this investment to the administration.

To ensure full funding of the new enforcement investments, the budget proposes to employ a budget enforcement mechanism that allows for an adjustment by the Budget Committees to the section 302(a) allocation to the Appropriations Committees found in the concurrent resolution on the budget. In addition, the administration will also seek to establish statutory spending limits, as defined by section 251 of the Balanced Budget and Emergency Deficit Control Act of 1985, and to adjust them for this purpose. To ensure full funding of the cost increases, either of these adjustments would only be permissible if the Congress funds the base level for IRS enforcement at $6.4 million and restricts the use of the funds to the specified purpose. The maximum allowable adjustment to the 302(a) allocation and/or the statutory spending limit would be $446 million for 2006, bringing the total enforcement level in the IRS to $6.9 million.

We will use the additional funds for enforcement in several key ways to combat the tax gap. Combating tax non-compliance is a top priority for us. Americans deserve to feel confident that when they pay their taxes, their neighbors and competitors are doing the same. These investments will yield substantial results.

The IRS yields more than $4 in direct revenue from its enforcement efforts for every $1 invested in its total budget. In fiscal year 2004, we brought in a record $43.1 billion in enforcement revenue—an increase of $5.5 billion from the year before, or 15 percent. Beyond the direct revenues generated by increasing audits, collection, and criminal investigations, our enforcement efforts have a deterrent effect on those who might be tempted to skirt their tax obligations.

The nearly 8 percent increase for enforcement activities in the administration's 2006 IRS budget request will increase audits of corporations and high-income individuals as well as expand collection and criminal investigation efforts.

DETAILED BUDGET SUMMARY

Our fiscal year 2006 request of $10.7 billion includes a transfer from the Justice Department of $53.913 million and 329 FTE for our portion of the Interagency Crime and Drug Enforcement (ICDE) appropriation, $277.6 million for a 2.3 percent pay raise and non-labor inflationary costs, and $264.6 million for initiatives aimed at enhancing our enforcement efforts. This request also includes a $22 million rent reduction to result from consolidation of space, and the $134.1 million reduction to taxpayer service activities that we will responsibly leverage through productivity improvements and program reengineering, as previously discussed. We will take a balanced approach to these targeted reductions.

In addition to the taxpayer service reengineering initiatives, we also expect to continue to realize savings, which we reinvest to other key areas, through the following other reengineering initiatives:

—*Savings from Increased Individual Master File (IMF) E-Filing (Reduction: −$7,700,000 and −190 FTE; Reinvestment: +$7,600,000 and +12 FTE).*—This savings is based on processing efficiencies from the projected decrease in IMF paper returns and processing costs for electronically filed IMF returns in Submission Processing Centers. These savings will be reinvested to enable us to continue our consolidation of IMF returns processing into fewer Submissions Processing sites.

—*Consolidation of Case Processing Activities to Maximize Resources Devoted to Front-Line Operations (Reduction: −$66,654,000 and −649 FTE; Reinvestment: +$66,654,000 and +585 FTE).*—Staffing for conducting case processing activities that support our examination, collection and lien-processing programs will be consolidated from nearly 100 sites and centralized among four campuses (Philadelphia, Cincinnati, Ogden and Memphis).

—*Consolidation of Insolvency Activities to Maximize Resources Devoted to Front-Line Operations (Reduction: −$14,928,000 and −134 FTE; Reinvestment: +$14,928,000 and +156 FTE).*—Staff conducting insolvency operations to protect the government's interest in bankruptcy proceedings will be consolidated from numerous sites and centralized at the Philadelphia campus.

—*Detection and Deterrence of Corrosive Corporate Non-Compliance (Reduction: −$6,711,000 and −52 FTE; Reinvestment: +$6,711,000 and +52 FTE).*—By using improved issue-management and risk-assessment strategies for examining corporations, the IRS expects to realize productivity improvements. These savings will be reinvested to fund front-line enforcement activities.

Finally, the fiscal year 2006 request includes several program increases, totaling $264.6 million:

—*Attack Corrosive Non-Compliance Activity Driving the Tax Gap (+$149,700,000 and +920 FTE).*—This initiative increases coverage of the growing number of high-risk compliance problems and addresses the largest portion of the tax gap—underreporting of tax. It proposes a funding increase across all major domestic and international compliance programs to leverage new workload-selection systems and case-building approaches from continuing reengineering efforts.

—*Detect and Deter Corrosive Corporate Non-Compliance (+$51,800,000 and +236 FTE).*—This initiative addresses complex, high-risk issues in abusive tax avoidance transactions, promoter activities, corporate fraud, and aggressive domestic and off-shore transactions, resulting in increased corporate and high-income return closures and audit coverage. This initiative also includes critical post-filing support provided by outside experts to expedite the resolution of issues at the field examination level, reducing taxpayer burden, and increasing the credibility of the Service's positions on the most complex and potentially highest compliance impact issues sent to court.

—*Increase Individual Taxpayer Compliance (+$37,900,000 and +417 FTE)*.—This initiative addresses the tax gap through: the identification and implementation of actions needed to address non-compliance with filing requirements; increased Automated Underreporter resources to address the reporting compliance tax gap; increased audit coverage; and expanded collection work in Taxpayer Assistance Centers.

—*Combat Abusive Transactions by Entities with Special Tax Status (+$14,460,000 and +77 FTE)*.—This initiative focuses on the most egregious cases of non-compliance and identifies compliance risks sooner, reducing burden on compliant customers and enabling the development of new interventions to curtail the growth of abusive transactions.

—*Curtailing Fraudulent Refund Crimes (+$10,772,000 and +22 FTE)*.—This initiative is aimed at attacking the increased questionable refunds and return preparer fraud identified through expanded operations of the Fraud Detection Centers located on IRS campuses. Fraudulent refund schemes are one of the most serious threats to voluntary compliance and an IRS investigative priority.

The fiscal year 2006 request of $10.7 billion funds the IRS's three appropriations: Tax Administration and Operations (TAO) for operations, service and enforcement; Business Systems Modernization (BSM) for modernization; and, the Health Insurance Tax Credit (HITCA) for administering a refundable tax credit for qualified individuals. I will describe each in turn.

TAX ADMINISTRATION AND OPERATIONS (TAO)

For fiscal year 2006, we request funding of $10,460,051,000, an increase of 4.6 percent over the fiscal year 2005 appropriation of $9,998,164,640 for programs previously funded from the PAM, TLE, and ISY appropriations.

The TAO appropriation provides resources for the IRS's service and enforcement programs. The IRS is responsible for ensuring that each taxpayer receives prompt and professional service. To that end, the IRS's assistance, outreach, and processing activities funded in the TAO appropriation are dedicated to providing assistance to taxpayers in all forms—electronic interaction, published guidance, paper correspondence, telephone contact, and face-to-face communication—so that taxpayers may fulfill their tax obligations timely and accurately. It also includes the resources the IRS requires to handle the processing and disposition of tax returns, refunds, and other filing materials.

We are also responsible for the fair enforcement of the Nation's tax laws. Each year, a small percentage of taxpayers file erroneous returns or, for reasons both innocent and less benign, fail to file a return at all. The IRS conducts enforcement activities using a variety of methods, including correspondence audits, matching reporting documents (such as Forms W–2) to information on taxpayer returns, in-person audits, criminal investigations of those suspected of violating tax laws, and participation in joint governmental task forces. The IRS's examination, collection, investigations, regulatory compliance, and research activities funded in the TAO appropriation provide the resources required for equitable enforcement of the tax code and the investigation and prosecution of individuals and organizations that circumvent tax laws.

BUSINESS SYSTEMS MODERNIZATION (BSM)

The IRS tax administration system, which collects $2 trillion in revenues annually, is critically dependent on a collection of 40-year-old, obsolete computer systems. Recognizing the long-term commitment needed to solve the problem of modernizing these antiquated systems, Congress and the administration created a special business systems modernization account. They designed the BSM program to bring the IRS's business systems to a level equivalent with best practices in the private and public sectors while managing the risks inherent in a program that is unquestionably one of the largest, most visible, and most sensitive modernization programs ever undertaken.

In 2004, the modernization budget was $387 million. Based on the challenges the modernization program was facing, we realized the program needed to be smaller in 2005 so we requested a lesser budget of $285 million. In the end, Congress appropriated $203 million. One of the ways we are accommodating these changes is by substantially lowering the costs of the core infrastructure as well as the architecture, integration, and management parts of the BSM program in 2005. These two areas are the programmatic elements of the program, and cost $160 million in fiscal year 2004. We certainly cannot justify that level of continued investment for a program that is roughly $200 million. Therefore, we are dramatically reducing those core services to $107 million in fiscal year 2005 and we anticipate making additional reduction in fiscal year 2006. For fiscal year 2006, we request funding of $199 million for all BSM activities, substantially the same funding as the fiscal year 2005 appropriated level.

Our most successful year ever for the modernization program was 2004; we measured our success by the number of projects we delivered, the schedule and cost targets we hit, and the substantial improvements we made in program management.

We delivered the first release of the Customer Account Data Engine (CADE) project in July 2004, allowing the IRS to process an initial set of the simplest tax returns on a new computer system for the first time in 40 years. We launched IRS's new Integrated Financial System (IFS), and declared it the IRS's financial accounting system of record. IFS will provide the capability for improved timeliness and accuracy of the financial reports and information available to IRS management and key stakeholders, facilitating continued clean financial audit opinions of the IRS. We deployed a full suite of e-Services products, providing tax professionals and businesses with new Web-based tools that dramatically improve their interface with the IRS. Additionally, we released Modernized e-File, whereby corporations and tax-exempt organizations can file their annual income tax and information returns electronically.

We have also made significant improvements in our cost estimating and scheduling. In the Fall and Winter of 2003, we re-baselined the cost estimates and delivery schedules for each of the BSM program projects. Since then, we have shown a marked improvement in significantly reducing our variances between cost estimates and actual delivery costs from 33 percent in 2002 to 4 percent in 2004.

In terms of improving program management, we identified four key areas that we had to address to enhance the performance of the modernization program:

—Resizing our modernization efforts to better align with our management and skill capacity;
—Engaging IRS business units to drive the modernization projects with a business focus;
—Improving contractor performance on cost, schedule, and functionality; and
—Hiring outside executives to achieve a better balance between large project management and tax administration experience.

We have made significant progress in addressing each of these major challenges.

First, the IRS will concentrate on a few key projects and will develop a track record of improved management and successful delivery of modernization projects.

Second, the IRS assigned a business unit leader to each project with responsibility for leading the related BSM Governance Committee, and sharing accountability for delivering the modernization project as stated in their annual performance commitments.

Third, we are making real progress in improving the accountability of the PRIME contractor. I meet monthly with the Chief Operating Officer of the Computer Sciences Corporation (CSC) to reinforce the accountability of the contractor to the IRS. Additionally, we have made major progress in restructuring BSM project contracts with the PRIME that shift an appropriate amount of financial risk to the contractor and tie costs to performance. These steps have resulted in improved contractor performance, as demonstrated in the deliverables in 2004 and the general adherence to costs and schedules.

Fourth, we have made great progress in hiring experienced executives and seasoned managers from outside the agency who have expertise in running large-scale information technology programs and projects. A little over a year ago the mix of leadership at the top of the BSM program consisted of one outside expert and six internal IRS executives. Today, that mix will soon be five outside experienced outside experts and three internal IRS executives. This mix is a much better balance of the project management and technology talent and tax administration experience needed to successfully run the BSM program.

While we were very successful in 2004, we have a lot of work ahead of us. It is critical that we continue this level of performance in 2005 and beyond.

Our focus for fiscal year 2005 is on maintaining substantial modernization work for three key tax administration systems that will provide additional benefits to taxpayers and IRS employees, specifically:

—The Customer Account Data Engine (CADE) project;

—Modernized e-File; and
—Filing and Payment Compliance (F&PC).

CADE

CADE replaces the IRS's antiquated system called the Master File which is the Service's repository of taxpayer information. With CADE being the core fundamental component of the modernized systems, it is the IRS's highest priority technology project.

We cannot over-emphasize the importance of CADE. The current Master Files have served the IRS for more than 40 years. However, they were developed in a different era and rely on an obsolete programming language and a flat-file system that still requires batch updates. These systems are very expensive to maintain; development of new applications costs the IRS two to three times what it would cost if they were already retired. Yet the IRS must update the Master Files every year to take into account tax law changes. As importantly, the vast majority of the workforce who are familiar with these old systems will be retiring over the next few years and we cannot hire individuals with these obsolete skills. Until the Master Files are replaced, the IRS can not offer service approaching what a typical financial services firm offers today (such as full account views for employees and real-time account updates and settlement).

The returns we are processing in CADE are the most basic of 1040EZ forms and have a narrow range of taxpayer information, but it marks the first time since the 1960's that the IRS has processed individual tax returns in a new way. The success of CADE proves that we can deliver technology that will process tax returns on a 24-hour cycle, breaking the 40-year-old standard of processing on a weekly cycle. As of March 25, 2005, CADE had processed 965,000 returns and generated nearly $318 million in refunds to taxpayers. This achievement is significant. CADE will have processed over 1 million 1040EZ tax returns by the time of this hearing and for the 2005 filing season that figure should reach over 1.3 million returns.

The CADE system is scheduled to be phased in over several years, processing increasingly more complex tax returns. When fully operational, CADE will be a modern database that will house tax information for more than 200 million individual and business tax returns. It will provide a variety of benefits to taxpayers, such as faster refunds (by over 50 percent) along with daily postings of transactions and updating accounts, which (with other technology elements) will significantly improve customer service and enforcement. With CADE, we will have the flexibility necessary to respond quickly to our complex tax law and tax reform changes.

One of the most significant changes that we introduced in 2004 was the segmentation of CADE releases into two annual deliveries—one in July and one in January. The July delivery will involve higher risk, more complex functionality, and the January delivery will include filing season changes combined with additional changes as capacity permits. For the July release, returns will be available from the previous 6 months which will enable us to test the higher risk, complex changes with high volumes, and then go live with reduced volumes, which will mitigate the operational risks.

MODERNIZED E-FILE

Modernized e-File will provide a single point Federal/State filing option for Forms 1120, 1120S (corporations) and 990 (tax-exempt organizations) returns in many States via a Web Services interface. Our work on Modernized e-File will be comprised of Release 3.1, which includes additional Forms 1120, 7004 (Application for Automatic Extension of Time to file Corporation Income Tax Return) and 990, and tax law changes for filing season 2004. Release 3.1 deployed initial operating capabilities on schedule on January 10, 2005. Release 3.2 will provide an interface with State tax information retrieval systems and a redesign of the signature matching process for Form 8453 (U.S. Individual Tax Declaration for Electronic Filing).

FILING AND PAYMENT COMPLIANCE/PRIVATE COLLECTION AGENCIES

In 2004, Congress passed the American Jobs Creation Act, allowing the IRS to use Private Collection Agencies (PCAs). The legislation authorized the IRS to augment our collection efforts by allowing us to use PCAs to pursue what has been deemed as uncollectible tax liabilities; these agencies will not have enforcement authority and will only contact delinquent taxpayers to arrange voluntary, full-payment installment agreements. We will use the Filing and Payment Compliance (F&PC) system to analyze tax collection cases and divide the complex cases requiring direct IRS involvement from the simple "balance due" cases that can be handled by PCAs. The use of PCAs is to supplement—not supplant—current IRS personnel.

Quite frankly, this activity is geared for an inventory that the IRS currently can not chase with existing resources.

PCAs will benefit the IRS in three major ways:

—PCAs will help reduce the significant and growing amount of tax liabilities deemed uncollectible.

—PCAs will help maintain taxpayer confidence in our tax system.

—PCAs will allow the IRS to focus on more difficult cases and issues.

We expect to issue a Request for Procurement (RFP) in the next several weeks. We plan to award contract in June 2005, to begin an initial limited release of the uncollected tax inventory in January 2006. We provided all interested parties notification via the IRS.gov/Business Opportunity webpage and electronic letters.

Safeguarding taxpayer rights is paramount. The same IRS standards for customer service and protection of taxpayer rights will be strictly enforced. PCAs will be prohibited from threatening or intimidating taxpayers or implying that enforcement action will be taken against them. Specific safeguards to protect the taxpayer include:

—Fair Debt Collection Practices Act protections;

—Protections against unauthorized disclosures;

—Assistance from the National Taxpayer Advocate; and,

—Protections with respect to third party contacts, installment agreements and communications.

The IRS expects to place cases with PCAs using the following criteria:

—The taxpayer does not dispute the liability;

—The liability is reportable on the Form 1040 series of returns;

—The balance due is greater than $100; and,

—The case does not involve a restriction on collection or otherwise indicate that discretion or enforcement action may be required to resolve the liability.

The delivery of the CADE project was a major milestone, but we still have a long way to go and a lot of work ahead of us as we introduce technology changes and expand into processing more complex tax returns at greater volumes. To that end, we recognize that a project of this complexity must continually look at new technologies that can support the level of development and implementation productivity needed for a project of this scale.

We certainly hope, and expect, that we will build on the successes of 2004, and we will continue to mature the modernization program by gaining a solid reputation for on-time deliveries with high productivity.

HEALTH INSURANCE TAX CREDIT ADMINISTRATION (HITCA)

In August 2002, the President signed Public Law 107–210, the Trade Act of 2002, which, among other things, provides a refundable tax credit for the cost of health insurance for certain individuals who receive a trade readjustment allowance or a benefit from the Pension Benefit Guaranty Corporation (PBGC). The Health Insurance Tax Credit Administration (HITCA) Appropriation funds the costs to administer a refundable tax credit for health insurance to qualified individuals. The tax credit is equal to 65 percent of the health insurance premium paid by eligible persons for themselves and qualifying family members. For fiscal year 2006 we request funding of $20,210,000, a decrease of 41.5 percent below the fiscal year 2005 appropriation of $34,562,272. Costs for the HITCA program have declined since implementation due to our active program oversight and management, as well as several cost-cutting initiatives we began to implement in March 2004. We developed a comprehensive action plan outlining cost-reduction initiatives and are following it to achieve these significant savings.

PROGRAM PERFORMANCE

The IRS expects to achieve the following levels of performance after attaining full performance of the requested fiscal year 2006 initiatives:

—Increase in field examinations for high-income individuals with complex returns; significant increase in collection processed; and closing of over 40 percent more delinquent balance-due accounts in fiscal year 2008 than in fiscal year 2004.

—Nearly double the audit coverage for individuals with income between $250,000 and $1 million, from 1.5 percent in fiscal year 2004 to 2.8 percent in fiscal year 2008.

—Auditing 15 percent more individuals earning above $1 million, from 3.4 percent projected for fiscal year 2004 to 3.9 percent in fiscal year 2008.

—Significantly more collection cases processed, closing 50 percent more delinquent accounts in fiscal year 2008 than fiscal year 2004.

—Double the audit coverage for mid-size corporations, from 7.6 percent in fiscal year 2004 to 16 percent in fiscal year 2008.
—Increased efforts to deter abusive tax shelters among corporations.

LEGISLATIVE PROPOSALS

The President's fiscal year 2006 request includes several proposals that will assist me in managing the agency more efficiently and effectively. These proposals, if enacted, will allow us to focus more resources on high-income, high-risk areas, automate several routine transactions, use electronic data to reduce costly manual transactions, consolidate resources related to judicial and counsel review, and broaden administrative authorities and accesses to support further electronic administration and tax reform. We are seeking to:
—Make Section 1203 of the IRS Restructuring and Reform Act of 1998 more effective and fair;
—Curb the use of frivolous submissions and filings made to impede or delay tax administration;
—Allow for the termination of installment agreements for failure to file returns and for failure to make tax deposits;
—Consolidate judicial review of collection due process cases in the United States Tax Court;
—Eliminate the monetary threshold for counsel review of offers in compromise;
—Allow the Financial Management Service to retain transaction fees otherwise paid from IRS appropriations from levied amounts to recover delinquent taxes;
—Extend the due date for electronically filed returns to provide additional incentive for taxpayers to e-file and expand the authority to require electronic filing by businesses and exempt organizations; and,
—Allow IRS to access information in the National Directory of New Hires for tax administration purposes.

CONCLUSION

The IRS has lagged behind, for reasons that are understandable, in tax enforcement. But that is changing. We will continue to improve service and respect taxpayer rights. But we will also enforce the law. We won't relax until taxpayers who are unwilling to pay their fair share see that that is not a worthwhile course to follow.

Mr. Chairman, the great majority of Americans honestly and accurately pay their taxes. Average Americans deserve to feel confident that, when they pay their taxes, their neighbors and competitors are doing the same.

The President's budget request will help us enforce the tax law more fairly and efficiently. I am most grateful for your support of increased enforcement, and I look forward to working with you on this important budget request.

Thank you very much. I am happy to take your questions.

Senator BOND. Thank you very much, Commissioner. Now we turn to Mr. George.

Now, again, as I said, your full statement will be submitted as a part of the record and we invite you to give a summary.

STATEMENT OF J. RUSSELL GEORGE

Mr. GEORGE. Thank you, Mr. Chairman. Chairman Bond, Ranking Member Murray, Senator Dorgan. Thank you for the opportunity to testify this morning. As you consider the fiscal year 2006 appropriation for the Internal Revenue Service, while I've held the position of Treasury Inspector General for Tax Administration for a little over 3 months, many of the issues I will discuss today are issues that I worked on over a decade ago. I served as a staff director and chief counsel of the House subcommittee with oversight responsibilities of the management and financial accounting practices of Federal agencies including the Internal Revenue Service. Unfortunately, many of the very same challenges facing the IRS not only persist 10 years later but in some cases have actually worsened. The office of the Treasury Inspector General for Tax Administration or, TIGTA, has identified 10 significant challenges facing the Internal Revenue Service.

They are: modernizing IRS systems, ensuring tax law compliance, reducing tax law complexity, preventing erroneous and improper payments, providing quality customer service, protecting taxpayers and taxpayer rights, securing IRS employees, facilities, and information systems, integrating performance and financial management, managing human capital, and finally processing returns and implementing tax law changes during the tax filing season.

My written statement addresses each of these challenges. Given the time constraints I will limit my comments to three of these issues, those being modernizing IRS systems, providing quality customer service, and ensuring tax law compliance.

The first issue, modernizing IRS computer systems, that's been a persistent challenge for many years. Unfortunately, it will likely remain a challenge for the foreseeable future. In 1986 the IRS initiated the tax systems modernization program to replace its antiquated computer systems. After spending over 10 years and approximately $3 billion on tax systems modernization the program was scrapped and a new effort was begun. The new effort is called Business Systems Modernization. It is estimated that this modernization effort will last up to 15 years and cost over $8 billion. While the program is progressing the modernization effort is behind schedule, it is over budget and it's still delivering less functionality than originally planned. TIGTA, the government accountability office, and the IRS oversight board have all expressed concerns about the ability of the IRS to effectively manage its portfolio or modernization projects. To succeed the IRS must demonstrate that it can handle the overall management of the modernization effort.

A second challenge facing the IRS is one that affects many taxpayers this time of year, receiving quality customer service. As the commissioner noted in his testimony the IRS has made progress in customer service, however, I am concerned that the IRS may take a step backwards on customer service if it follows through with the proposal to close many taxpayer assistance centers. The taxpayer assistance centers are walk-in sites where taxpayers can receive answers to both account questions and tax law questions as well as receive assistance preparing their tax returns. The IRS is considering closing nearly 20 percent of the approximately 400 taxpayer assistance centers nationwide. As part of an ongoing audit we at TIGTA are reviewing the methodology used by the IRS to determine which taxpayer assistance centers to close. At this point I am skeptical that the IRS has adequate data to assess the impact that closing these centers will have on customer service. I'm also concerned that the IRS has insufficient data to draw conclusions on the likelihood that taxpayers who used these centers in the past will be able to use other methods of seeking help, such as the Internet or telephone. I strongly recommend that the IRS further research these issues before closing selected taxpayer assisted centers.

Finally, on the topic of improving tax law compliance the IRS continues to and will always face challenges in ensuring that taxes are paid of time. According to IRS estimates the tax gap, which again is defined as the difference between what taxpayers are supposed to pay and what is actually paid is as noted approximately between $312 and $353 billion each year. To improve tax compliance the IRS must begin to use private contractors to collect taxes in the next year. While the use of private collection agencies could result in significant recoveries of unpaid taxes the potential for abuse exists. My office has developed a three-phase strategy to monitor this initiative. We will be vigilant in ensuring the IRS effectively uses its new authority to use private debt collectors while also ensuring that taxpayers due rights and privacy rights are protected.

PREPARED STATEMENT

Mr. Chairman, members of the subcommittee, I hope this brief discussion of three of the major challenges facing the IRS aids you as you consider its fiscal year 2006 appropriation. Thank you for allowing me to share my views. I look forward to taking whatever questions you might have at the appropriate time.

[The statement follows:]

PREPARED STATEMENT OF J. RUSSELL GEORGE

INTRODUCTION

Chairman Bond, Ranking Member Murray, and members of the subcommittee, I thank you for the opportunity to testify as you consider the fiscal year 2006 appropriations for the Internal Revenue Service. As the relatively new Treasury Inspector General for Tax Administration—having been on the job for 16 weeks—my observations are based on the body of work my organization has developed through audits and investigations of the IRS. I will focus on the major challenges facing the IRS to assist you in your consideration of the IRS's fiscal year 2006 budget.

Though I have been the Treasury Inspector General for Tax Administration (TIGTA) for only a few short months, my first experience conducting oversight of the Internal Revenue Service (IRS) dates back a number of years. In 1995, one of the initial charges I received as staff director of the House Subcommittee on Government Management, Information and Technology was to examine inefficiency at the IRS. Under then Chairman Stephen Horn's leadership, we reviewed several issues such as the IRS's tax systems modernization program, as well as ways to improve Federal debt collection practices. A decade later, I am disappointed to report that some of the same concerns Chairman Horn reviewed 10 years ago continue at the IRS today.

While the IRS faces longstanding challenges, it deserves credit for making marked progress in an area that will always be a challenge: providing quality customer service to the American taxpayer. Commissioner Everson's guiding principle for the IRS is Service + Enforcement=Compliance. Over the past few years, TIGTA audits have shown the accuracy of information provided by the IRS to taxpayers with tax law questions has generally improved, the average time spent by taxpayers waiting for IRS assistance on the phone or in person has declined, and the general professionalism with which taxpayers were treated by the IRS has increased. Since most interactions between the IRS and taxpayers involve these types of customer services, it is encouraging to see that the IRS's focus on customer service has made headway.

CHALLENGES FACING THE IRS

Despite such progress in customer service, improvements need to be made in this and other areas where significant challenges face the IRS in accomplishing its mission. The Treasury Inspector General for Tax Administration (TIGTA) has identified the following management and performance challenges that confront the IRS:

—Modernizing IRS Systems;
—Ensuring Tax Law Compliance;
—Reducing Tax Law Complexity;
—Preventing Erroneous and Improper Payments;

—Providing Quality Customer Service;
—Protecting Taxpayers and Taxpayer Rights;
—Securing IRS Employees, Facilities, and Information Systems;
—Integrating Performance and Financial Management;
—Managing Human Capital; and,
—Processing Returns and Implementing Tax Law Changes during the Tax Filing Season.[1]

Each of these areas presents its own unique challenges, which will be addressed individually in the remaining portion of my testimony.

MODERNIZING IRS SYSTEMS

Modernizing the IRS's computer systems has been a persistent challenge for many years, and will likely remain a challenge for the foreseeable future. As I noted above, back in 1995, under Chairman Stephen Horn's leadership, the House Subcommittee on Government Management, Information and Technology began reviewing what was then referred to as tax systems modernization.

The IRS initiated the tax systems modernization program in 1986. The purpose of the tax systems modernization program was to replace the antiquated computer systems that the IRS still relies on today to conduct tax administration. The tax systems modernization program intended to create a tax processing environment that was virtually paper-free, an environment where taxpayer information would be readily available to IRS employees to update taxpayer accounts and respond to taxpayer questions.[2] The program, however, was plagued by management and technical weaknesses.[3] After spending over $3 billion on tax systems modernization,[4] the program was scrapped and a new effort was begun under a fresh moniker, Business Systems Modernization (BSM) program.

This latest effort to modernize the IRS's systems, the BSM program, began in fiscal year 1999. The purpose of the BSM program is to modernize the IRS's technology and related business processes. According to the IRS, this effort will involve integrating thousands of hardware and software components. Through March 2005, the IRS has received appropriations of approximately $1.8 billion to support the BSM program, and the fiscal year 2006 budget requests an additional $199 million. It is estimated that the BSM program will last up to 15 years and cost over $8 billion.[5]

Succeeding in the modernization effort is critical—not only because of the amount of time and money at stake—but also to improve the level of service provided to taxpayers. To accomplish the modernization effort, the IRS hired the Computer Sciences Corporation (CSC) as the PRIME[6] to design, develop, and integrate the modernized computer systems.

The joint effort between the IRS and CSC has shown progress. In July 2004, the IRS released the first part of the Customer Account Data Engine (CADE) project. The CADE is the foundation for managing taxpayer accounts in the modernization plan. The CADE will replace the IRS's existing Master File.[7] Once fully operational, the capabilities of the CADE will far surpass those of the Master File.[8]

The first release of the CADE allowed the IRS to process some of the simplest tax returns, Form 1040EZ, using a new database of taxpayer accounts. The IRS has also deployed projects that provide value to taxpayers, such as "Where's My Re-

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[1] The filing season refers to the period from January through mid-April when most individual income tax returns are filed.

[2] See General Accounting Office Report GAO/AIMD/GGD–98–54, Tax Systems Modernization: Blueprint Is a Good Start But Not Yet Sufficiently Complete to Build or Acquire Systems (Feb. 1998).

[3] See General Accounting Office Report GAO/T–GGD–97–79, IRS Management: Improvement Needed in High-Risk Areas (Apr. 14, 1997).

[4] See General Accounting Office Report T–GGD–97–52, Modernization of Processes and Systems Necessary to Resolve Problems (Mar. 4, 1997).

[5] The Internal Revenue Service Has Appropriate Processes to Accept Modernization Software From Developers (Reference Number 2005–20–028, February 2005).

[6] The PRIME stands for Prime Systems Integration Services Contractor.

[7] The Master File is the IRS database for storing taxpayer account information on individuals, businesses, employee retirement plans, and exempt organizations.

[8] The CADE will include applications for daily posting, settlement, maintenance, refund processing, and issue detection for taxpayer account and return data. In conjunction with other applications, the CADE will allow employees to post transactions and update taxpayer account and return data on-line from their desks. Updates will be immediately available to any IRS employee who accesses the data and will provide a complete, timely, and accurate account of the taxpayer's information. In contrast, the current Master File processing system can take up to 2 weeks to update taxpayer accounts, and IRS employees may need to access several computer systems to gather all relevant information related to a taxpayer's account.

fund?," the web-based application that allows taxpayers to check the status of their refunds. In addition, the IRS and its contractors have built the infrastructure needed to support these projects and have developed an enterprise architecture to guide the Business Systems Modernization (BSM) program.

Although progress is being made, the modernization program is behind schedule, over budget, and is delivering less functionality than originally planned. TIGTA, GAO and the IRS Oversight Board have expressed concerns over the IRS's ability to effectively manage its portfolio of BSM projects. Both TIGTA and GAO have recommended that the IRS slow the pace of the BSM program due to some of the risks that have surfaced. Specifically, the imbalance between the number and pace of the BSM projects and available management capabilities has added significant cost, schedule, and performance risks that have continued to escalate.

In addition, TIGTA has identified four primary challenges that the IRS must overcome for modernization to be successful: (1) The IRS must implement planned improvements in key management processes and commit necessary resources to succeed; (2) The IRS must manage the increasing complexity and risks of the modernization program; (3) The IRS must maintain continuity of strategic direction with experienced leadership; and, (4) The IRS must ensure that CSC's performance and accountability are effectively managed.

Without these four challenges being addressed, modernization will not succeed.[9] In addition, IRS is reassessing its relationship with the PRIME contractor. For the past 6 years, the PRIME contractor has performed the role of system integrator and program manager for the BSM effort. In the new operating model, the IRS assumes responsibility for overall program management. The IRS must demonstrate that it can effectively manage the BSM program before its chances for success improve.

ENSURING TAX LAW COMPLIANCE

The IRS continues to face challenges in ensuring that taxes owed are paid on time. The importance of this issue cannot be overstated. The Nation's ability to provide for the general welfare and protect its citizens is based on the ability to raise revenue through taxes. Yet, the tax gap, which the IRS defines as the difference between what taxpayers are supposed to pay and what is actually paid, is at staggering levels.[10] On March 29, 2005, the IRS released updated estimates of the tax gap. For tax year 2001, the IRS estimated the annual gross tax gap[11] to be between $312 billion and $353 billion.[12]

For some time, the IRS, the Congress, and other stakeholders have been concerned about the slow erosion of voluntary tax compliance. IRS tax compliance programs must ensure that noncompliant taxpayers who do not meet their tax obligations are identified and penalized. The undermining of voluntary compliance begins when honest taxpayers believe that others are not paying their fair share.[13]

To improve tax compliance, the IRS must fully exercise its authority under the law. The American Jobs Creation Act of 2004 enables the IRS to use private contractors to collect unpaid taxes. While the use of private collection agencies could result in significant recoveries of unpaid taxes, the potential for abuse exists. TIGTA has developed a three phase audit strategy to monitor this initiative. In the first phase, TIGTA will review the IRS's planning and initial implementation of the program. In the second phase, TIGTA will review the initiative after full implementation, which may not occur until fiscal year 2007. In the third phase, TIGTA will review the effectiveness of the program. The goal of this audit strategy is to ensure

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[9] Annual Assessment of the Business Systems Modernization Program (Reference Number 2004–20–107, dated June 2004).

[10] See written statement of Commissioner of Internal Revenue Mark Everson before the Committee on Finance United States Senate Hearing on "Bridging the Tax Gap," (July 21, 2004).

[11] The amount of tax that is imposed for a given tax year, but is not paid voluntarily and timely.

[12] It is worth noting that the recently released tax gap figures noted above did not update key segments of the tax gap that are at least 15 years old, such as nonfiled tax returns and underreported corporate income tax for large corporations.

[13] The IRS fiscal year 2006 budget requests a significant increase in enforcement funds. As the IRS attempts to increase enforcement, it is worth considering the results of a 2003 GAO report. GAO found that the IRS's frontline enforcement employees understood—but feared—section 1203 of the Internal Revenue Service Restructuring and Reform Act of 1998. Section 1203 outlines conditions for firing IRS employees for committing any of 10 acts of misconduct. These enforcement employees also reported that, because of section 1203, their work takes longer and the likelihood of their taking an enforcement action, such as recommending a seizure has decreased. See General Accounting Office Report GAO–03–394, IRS and TIGTA Should Evaluate Their Processing of Employee Misconduct under Section 1203 (February 2003).

that the IRS effectively uses its new authority to use private debt collectors, while also ensuring that taxpayers' due process and privacy rights are protected.

Congress has provided other statutory tools to the IRS to increase tax compliance. The IRS has the legal authority to charge a monetary penalty, called the Failure to Pay (FTP) tax penalty, against taxpayers who fail to pay their taxes on time.[14] The law also requires the IRS to charge interest on FTP tax penalties.[15] A recent TIGTA report found that the IRS computer system would assess the FTP tax penalty on taxpayers' accounts, but would not officially charge these assessments to accounts. By not assessing these penalties periodically, the IRS has foregone the interest associated with them. If the IRS had assessed all penalty accruals at least quarterly, TIGTA estimates that for calendar year 2002 alone, over $817 million in interest on accrued penalties would be due to the IRS.[16] This is one example of how the IRS could better use the tools at its disposal.

In addition to more fully exercising authority provided by Congress, the IRS must obtain timely and reliable data on the tax gap to improve tax compliance. To collect such data, the IRS launched the National Research Program, a study of individual taxpayer reporting compliance for tax year 2001. The National Research Program is intended to produce timely and reliable data that will allow the IRS to better target its limited enforcement resources on taxpayers who are not complying with the tax law instead of law-abiding individuals.

While timely and reliable data will help the IRS quantify noncompliant segments of the population, different approaches are also needed to determine how to most effectively address noncompliance. The Taxpayer Advocate's 2004 Annual Report to Congress depicts some of the complexities involved in structuring an enforcement program to address the tax gap. The Taxpayer Advocate also describes the efforts the IRS still needs to make to analyze the effectiveness of various compliance techniques.[17] Similarly, in two recent audit reports, TIGTA identified examination programs that the IRS implemented nationwide before obtaining results on their possible effectiveness or before implementing an effective strategy to measure the results of the program.[18]

Accurate measures of the effectiveness of actions taken to reduce the tax gap are critical to the IRS for strategic direction, budgeting, and staff allocation. The Department of the Treasury also needs such measures for the purpose of creating tax policy. Additionally, the Congress could use this information to develop legislation that improves the efficacy of the tax system.

In addition to gathering better compliance data, TIGTA, other oversight groups, and interested stakeholders have made a number of recommendations to close the tax gap. These recommendations include: reducing the complexity of the tax code; instituting withholding on non-employee compensation; improving compliance with estimated tax payments; using document matching to verify business income; addressing escalating levels of late filed returns; increasing resources in the IRS enforcement functions; and addressing delays in systems modernization. While reducing the complexity of the tax code lies outside the authority of the IRS, the remaining recommendations are within the IRS's discretion and should be acted upon to further tax compliance.

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[14] 26 U.S.C. § 6651 (2004).

[15] 26 U.S.C. § 6601(e)(2)(A) (2004).

[16] This report also found that the IRS's current practice results in inconsistent treatment of taxpayers. Some taxpayers in hardship situations, such as victims of natural disasters or military personnel serving in combat zones, have accounts that are administered by the IRS manually rather than by computer. IRS personnel periodically calculate and manually assess penalties on these accounts. Because the manually computer FTP penalties are periodically assessed, interest is charged to these taxpayer accounts but not charged to taxpayer accounts administered by computer. Procedures Regarding the Failure to Pay Tax Penalty Result in Inconsistent Treatment of Taxpayers and Hundreds of Millions of Dollars in Lost Revenue (Reference Number 2005–30–052, dated March 2005).

[17] National Taxpayer Advocate 2004 Annual Report to Congress (Dec. 31, 2004).

[18] In TIGTA's judgment, the IRS implemented the High-Income Taxpayer Strategy, designed to target individuals with the financial resources to use sophisticated methods of tax avoidance, without a method and specific baselines to measure the strategy's success. In addition, the IRS introduced the Limited Issue Focused Examination (LIFE) process to reduce the length of examinations of large and mid-sized businesses. While the LIFE process has merit, the IRS implemented it nationwide before obtaining results on its possible effectiveness. The High Income Taxpayer Strategy Was Effectively Implemented, Although Its Success Still Needs to Be Determined (Reference Number 2005–30–012, dated November 2004) and The Limited Issue Focused Examination Process Has Merit, but Its Use and Productivity Are Concerns (Reference Number 2005–30–029, dated February 2005).

REDUCING TAX LAW COMPLEXITY

The scope and complexity of the United States Tax Code make it virtually certain that taxpayers will face procedural, technical, and bureaucratic obstacles before meeting their tax obligations. The IRS has consistently sought to ease the process for all taxpayers, but each tax season brings new challenges, and old problems sometimes resist solution.

According to the Taxpayer Advocate's 2004 Annual Report to Congress, the most serious problem facing taxpayers and the IRS is the complexity of the Internal Revenue Code.[19] The Joint Committee on Taxation conducted a study in 2001 that demonstrates the vastness of the tax code. The study found that, in 2001, the tax code consisted of nearly 1.4 million words. There were 693 sections of the code applicable to individuals, 1,501 sections applicable to businesses, and 445 sections applicable to tax exempt organizations, employee plans, and governments.[20]

The complexity of the code hampers the ability of the IRS to administer the Nation's tax system and confuses most taxpayers. The IRS has attempted to provide assistance to taxpayers with questions about the tax code through toll-free telephone lines, Taxpayer Assistance Centers (TACs), kiosks, and the IRS internet web site. TIGTA has performed numerous audits of the accuracy of IRS responses to taxpayer questions submitted via these methods and found that even some IRS employees cannot apply the tax code correctly.

Our most recent audit of the accuracy of responses provided to tax law questions received via the toll-free telephone lines during the 2004 Filing Season found that 62 percent of the answers given were correct.[21] The IRS conducted its own tests and found an accuracy rate of 79 percent. Both of these figures were well below the IRS's accuracy goal of 85 percent for this service. Tax law complexity contributes to the IRS's challenges in reaching these accuracy goals, as well as to taxpayer frustration with attempting to decipher the tax code.

Besides adding to the burden on the taxpayer and the IRS, tax law complexity also may inadvertently contribute to the tax gap. Complexity has given rise to the latest generation of abusive tax avoidance transactions, with taxpayers attempting to take advantage of the tax code's length and complexity by devising intricate schemes to illegally shelter income from taxation. Administering such a complex tax code makes the job of pursuing these abusive tax avoidance schemes challenging and costly to the IRS. For example, in 2004, the hours revenue agents spent per return on examinations increased by 23 percent for individual tax returns and 19 percent for corporate tax returns compared to 2003 figures.[22]

As part of its goal to improve service to taxpayers, the IRS includes simplifying the tax process as an objective in its new Strategic Plan. Simplification could incorporate a range of actions from developing legislative recommendations to clarifying tax instructions or forms. Changing tax laws, however, can be a lengthy process since the IRS only administers the tax code that is passed by the Congress. Thus, the IRS must work extensively with these stakeholders, as well as the Department of the Treasury, to identify and develop legislative recommendations that would reduce tax law complexity and taxpayer burden.

PREVENTING ERRONEOUS AND IMPROPER PAYMENTS

One of the goals of The President's Management Agenda is to reduce erroneous payments.[23] Further, the Improper Payments Information Act of 2002[24] greatly expanded the administration's efforts to identify and reduce erroneous and improper payments in government programs and activities. While the administration has pushed to prevent erroneous and improper payments, stewardship over public funds remains a major challenge for IRS management.

Improper and erroneous payments include inadvertent errors, payments for unsupported or inadequately supported claims, payments for services not rendered, payments to ineligible beneficiaries, and payments resulting from outright fraud and abuse by program participants or Federal employees. For the IRS, improper and

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[19] National Taxpayer Advocate 2004 Annual Report to Congress (Dec. 31, 2004).

[20] Study of the Overall State of the Federal Tax System and Recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1986, Staff of the Joint Committee on Taxation, JCS–3–01 (Apr. 2001).

[21] Additional Effort Answering Tax Law Questions Would Improve Customer Service (Reference Number 2004–40–150, dated August 2004).

[22] TIGTA analysis of IRS Data Book information.

[23] The President's Management Agenda, announced in the summer of 2001, is the President's aggressive strategy for improving the management of the Federal Government. It focuses on five areas of management weakness across the Government where improvements should be made.

[24] Public Law No. 107–300, 116 Stat. 2350.

erroneous payments generally involve improperly paid refunds, tax return filing fraud, or overpayments to vendors or contractors.

Some tax credits, such as the Earned Income Tax Credit (EITC), provide opportunities for taxpayer abuse. The EITC is a refundable credit available to taxpayers who do not exceed a certain amount of income per year. The EITC was intended to provide significant benefits to the working poor, but some taxpayers have abused the credit, which has resulted in a significant loss of revenue to the Federal Government. An IRS compliance study of tax year 1999 returns estimated between $8.5 billion and $9.9 billion (27 to 32 percent) of the $31 billion in EITC claimed for tax year 1999 should not have been paid.[25] A TIGTA review of EITC claimed for tax year 2002 estimated that the IRS allowed over $16 million in potentially erroneous credits because the claimed qualifying "child" was significantly older than the primary taxpayer.

In addition to erroneous payments of credits, contract expenditures represent a significant outlay of IRS funds and are also susceptible to mistakes or abuse. The IRS approved payment of nearly a billion dollars for the Business Systems Modernization contract. Initially, neither the IRS nor the contractor could provide proper supporting documentation for approximately $9.5 million (approximately 54 percent of the $17.6 million sampled) in direct charges.[26] The contractor subsequently provided additional documentation, and TIGTA was able to verify all but approximately $52,200. Nevertheless, to assure that its billings are adequately justified and to facilitate timely independent reviews, the IRS should strengthen its invoice review process by routinely requesting and reviewing a sample of supporting documents.

PROVIDING QUALITY CUSTOMER SERVICE

Providing quality customer service to the taxpayer is not only a primary goal of the IRS, but it is also one of its major management challenges. The Commissioner has frequently stated that service combined with enforcement will result in compliance. Quality taxpayer service includes helping the taxpaying public understand their tax obligations while making it easier to participate in the tax system.

Since the passage of the IRS Restructuring and Reform Act of 1998 (RRA 98),[27] the IRS's focus on customer service has led to many improvements. Taxpayer satisfaction rates with the IRS have increased since the Act's passage, growing almost 2 percent in 2004 alone.[28] Every year, the IRS helps millions of taxpayers understand their tax obligations by answering questions on its toll-free telephone lines or in person at local offices, making information available on its Web site, and responding to correspondence.

The IRS internet site, www.IRS.gov, is an excellent source for forms, publications, and other guidance. Taxpayers visited the site over 139 million times last year.[29] The site also received an award for being the Nation's most reliable government internet site.[30] Electronic filing of tax returns continues to grow, and the ability to check the status of tax refunds online has been a successful IRS project that is helpful to taxpayers.[31]

As for the toll-free telephone system, access by taxpayers to the IRS via telephone has improved. Callers were able to connect with the IRS more easily and received better, quicker service. Surveys of callers during the 2004 filing season showed that the vast majority of taxpayers were satisfied with the services they received.[32] While the IRS exceeded its goals in professionalism and timeliness, the accuracy of answers provided to taxpayers on tax law questions slipped in 1 year from 73 percent to 62 percent. TIGTA attributed this decrease to IRS employees not always using the required Probe and Response Guide to obtain sufficient information from taxpayers or the employees were not correctly interpreting the tax law.

The IRS has obviously made strides in customer service over the past 7 years. TIGTA is concerned, however, that the IRS may disrupt the balance between cus-

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[25] IRS report, Compliance Estimates for Earned Income Tax Credit on 1999 Returns (dated February 2002).

[26] Improvements Are Needed in the Invoice Review Process for the Business Systems Modernization Contract (Reference Number 2004–10–117, dated June 2004).

[27] Public Law No. 105–206, 112 Stat. 683 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

[28] Special Report on IRS Fiscal 2006 Budget, IRS Oversight Board, March 15, 2005.

[29] IRS.gov Cited As Most Reliable Government Web Site, IR–2004–131, October 25, 2004.

[30] Id.

[31] Free File Tops Last Year's Total, IR–2005–36, March 23, 2005.

[32] Taxpayers Experienced Improved Access to Toll-Free Telephone Services During the 2004 Filing Season (Reference Number 2004–30–144, dated August 2004).

tomer service and enforcement by closing many of its Taxpayer Assistance Centers. The TACs are walk-in sites where taxpayers can receive answers to both account and tax law questions, as well as receive assistance preparing their returns. Over the past few years, customer service at Taxpayer Assistance Centers has shown improvement.[33] Yet, the IRS is considering closing nearly a quarter of its approximately 400 TACs nationwide. TIGTA is skeptical that the IRS has adequate data to assess the impact that closing TACs will have on customer service.

From the information provided by the IRS to TIGTA, the IRS is using the following criteria to select TACs to close: location, labor cost, facility cost, workload, and demographics. The last criterion, demographics, falls short of capturing the information needed to make a well-informed decision. To compile information on the demographics of a particular TAC location, the IRS is collecting data, by zip code, on population size, income level, age, unemployment, and percent of population who e-file. TIGTA believes this information is insufficient to draw conclusions on the capability and likelihood that taxpayers who have used these centers in the past will be willing to use alternative methods of seeking help, such as the internet or telephone. I strongly recommend that the IRS further research these issues before closing TACs.

PROTECTING TAXPAYERS AND TAXPAYER RIGHTS

Congress realized the importance of protecting taxpayers and taxpayer rights when it passed RRA 98. This legislation required the IRS to devote significant attention and resources to protecting taxpayer rights. The RRA 98 and other legislation require TIGTA to review IRS compliance with taxpayer rights provisions. Our most recent audit results on some of these taxpayer rights provisions are:

—*Notice of Levy*.—TIGTA reports have recognized that the IRS has implemented tighter controls over the issuance of systemically generated levies, and TIGTA testing of these controls indicated that they continue to function effectively. However, revenue officers who issue levies manually still are not always properly notifying taxpayers of their appeal rights.[34]

—*Restrictions on the Use of Enforcement Statistics to Evaluate Employees*.—The IRS is complying with the law. A sample review of employee performance and related supervisory documentation revealed no instances of tax enforcement results, production quotas, or goals being used to evaluate employee performance.[35]

—*Notice of Lien*.—The IRS did not completely comply with the law. For example, the IRS did not always timely mail lien notices. In other cases, the IRS could not provide proof of mailing. In addition, the IRS did not always follow its guidelines for notifying taxpayer representatives and for maintaining certified mail listings.[36]

—*Seizures.*—The IRS did not always comply with legal provisions and internal procedures when conducting seizures. The TIGTA review did not identify any instances where taxpayers were adversely affected, but not following legal and internal guidelines could result in abuses of taxpayer rights.[37]

—*Illegal Tax Protestor Designations*.—The IRS is prohibited by law from designating taxpayers as "illegal tax protestors" but may refer to taxpayers as "nonfilers." TIGTA has reviewed the Master File for illegal tax protestor designations. We found that the IRS has not reintroduced such designations on the Master File, taxpayer accounts that were formerly coded as illegal tax protestor accounts have not been assigned similar designations, and current IRS publications do not refer to illegal tax protestors. However, a few illegal tax protestor references still exist in manuals, job aids, computer systems, and isolated case files.[38]

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[33] Customer Service at the Taxpayer Assistance Centers Is Improving but Is Still Not Meeting Expectations (Reference Number 2005–40–021, dated December 2004).

[34] Additional Efforts Are Needed to Ensure Taxpayer Rights Are Protected When Manual Levies Are Issued (Reference Number 2004–30–094, dated April 2004).

[35] Fiscal year 2004 Statutory Audit of Compliance With Legal Guidelines Restricting the Use of Records of Tax Enforcement Results (Reference Number 2004–40–066, dated March 2004).

[36] Fiscal year 2004 Statutory Review of Compliance With Lien Due Process Procedures (Reference Number 2004–30–086, dated April 2004).

[37] Legal and Internal Guidelines Were Not Always Followed When Conducting Seizures of Taxpayers' Property (Reference Number 2004–30–149, dated August 2004).

[38] Fiscal year 2004 Statutory Audit of Compliance With Legal Guidelines Prohibiting the Use of Illegal Tax Protester and Similar Designations (Reference Number 2004–40–109, dated June 2004).

—*Denials of Requests for Information*.—The IRS improperly withheld information from requesters in 4.4 percent of the Freedom of Information Act [39] and Privacy Act of 1974 [40] requests, and 14.6 percent of the 26 U.S.C. § 6103 requests reviewed.[41]

—*Collection Due Process*.—IRS Appeals Officers and Settlement Officers substantially complied with the requirements of the law when conducting collection due process hearings. However, the Settlement Officers did not always address all the issues raised by the taxpayers.[42]

Neither TIGTA nor the IRS could evaluate the IRS's compliance with three RRA 98 provisions since IRS information systems do not track specific cases. These three provisions relate to: restrictions on directly contacting taxpayers instead of authorized representatives, taxpayer complaints, and separated or divorced joint filer requests.

SECURING IRS EMPLOYEES, FACILITIES, AND INFORMATION SYSTEMS

As the Nation's primary revenue collector and an integral part of the Nation's critical infrastructure, the IRS is a prime target for anti-government protestors, international terrorists, and other extremists. Millions of taxpayers entrust the IRS with sensitive financial and personal data, which are stored and processed by IRS computer systems. The risks that sensitive data or computer systems could be compromised and that computer operations could be disrupted have increased over the last few years due to the external threats noted above and the increased connectivity of computer systems. In addition, IRS systems and data are vulnerable to unhappy taxpayers and disgruntled employees, as well as natural disasters. Although many steps have been taken to limit risks, IRS systems and taxpayer information remain susceptible to threats that could impact the confidentiality, integrity, and availability of data and information systems.

For the past 4 years, TIGTA assessments have concluded that the security infrastructure and the applications that guard sensitive data are weak because of inadequate accountability and security awareness, as well as insufficient training for key security employees. The IRS has focused on technical solutions to this issue, but the primary causes are managerial and operational factors. For example, in 2004, TIGTA found that while security roles and responsibilities have been defined, we continue to identify significant security weaknesses throughout the IRS that can be attributed to employees not fulfilling their responsibilities.[43] This results in the IRS failing to establish an organizational culture that strongly emphasizes the security and privacy of taxpayer data. In addition, some disaster recovery plans require additional development, testing, or personnel training to ensure that the IRS can quickly recover in the event of a disaster.

TIGTA has also identified security weaknesses in a number of IRS systems. For example, the IRS envisions the Security Audit and Analysis System (SAAS) as the audit trail collection and reporting system for the IRS's modernized applications. To date, no modernization applications are employing the SAAS for this purpose. This failure to employ the SAAS for audit trail collection and reporting results in at least two weaknesses. First, the IRS could deploy modernization applications without proper audit trail controls in place. Second, the IRS may spend additional resources to employ an application-specific audit trail that is not consistent with the IRS's architecture and would, in essence, represent a double investment in audit trail controls. Furthermore, the SAAS was accepted by the IRS despite the fact that it did not meet performance requirements.[44]

The IRS has taken several positive steps toward improving security in the IRS. In October 2003, the IRS combined key security activities into a single organization to promote better performance and consistent customer focus. Adequate security policies and procedures have been established and, in most cases, the IRS has the

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[39] 5 U.S.C. § 552.

[40] 5 U.S.C. § 552a.

[41] Improvements Are Needed to Ensure Compliance With the Freedom of Information Act (Reference Number 2004–40–064, dated March 2004).

[42] Appeals Complied With the Provisions of the Law for the Collection Due Process (Reference Number 2004–40–067, dated March 2004).

[43] Computer Security Roles and Responsibilities and Training Should Remain Part of the Computer Security Material Weakness (Reference Number 2004–20–155, dated September 2004).

[44] For example, the SAAS users cannot query the audit trail information to generate reports. In addition, the functionality and software performance problems of the SAAS prevent the IRS business units from using it to identify questionable activities on modernized applications. See The Audit Trail System for Detecting Improper Activities on Modernized Systems Is Not Functioning, (Reference Number 2004–20–135, dated August 2004).

necessary hardware and software to provide adequate system security. While the IRS has become a leader in government under this management structure, it must emphasize the importance of security to its employees.

For the IRS to make the largest strides in improving computer security at a relatively low cost, managers and employees must be aware of the security risks inherent in their positions and consider security implications in their day-to-day activities. Thus, IRS business unit managers should be held accountable for the security of their systems and key security employees should be adequately trained to carry out their responsibilities. It is also vital that the IRS continues to refine its plans and capabilities to manage emergency situations in a manner that protects employees and allows restoration of business operations in a timely manner. In addition, aggressive network control, monitoring, and incident response capabilities are necessary to prevent incursions into IRS systems from external and internal sources.

INTEGRATING PERFORMANCE AND FINANCIAL MANAGEMENT

The President's Management Agenda aims to place a greater focus on performance by formally integrating it with budget decisions. In addition, without accurate and timely financial information, it is not possible to accomplish the President's agenda to secure the best performance and highest measure of accountability for the American people. The IRS has made some progress; however, integrating performance and financial management remains a major challenge.

The IRS has achieved mixed success in establishing long-term goals to integrate performance and financial management. During the fiscal year 2005 budget formulation process, the IRS took the important step of aligning performance and resources requested. The IRS also modified its budget and performance plans to include more customer-focused and "end result" measures. However, TIGTA believes the IRS must continue to integrate performance into its decision-making and resource allocation processes to completely achieve an integrated performance budget.

The IRS also continues to analyze the critical data needed to develop long-term enforcement outcome measures. For example, the IRS released the first results from its National Research Program and they provide fresh data on taxpayer voluntary compliance levels—the first in more than a decade. Such data is essential to establishing enforcement measures and effectively allocating resources to related activities. The IRS, however, needs to develop a more strategic approach to the entire tax administration system. Such an effort would better identify the characteristics of an effective and efficient tax administration system, help pinpoint desired outcomes, and create a road map for the next decade that would complement the IRS's strategic, budget, and annual performance plans.

The IRS's financial statements and related activities also continue to be of concern to IRS stakeholders. The GAO audits the IRS's financial statements annually. The audit determines whether the IRS: (1) prepared reliable financial statements; (2) maintained effective internal controls; and, (3) complied with selected provisions of significant laws and regulations, including compliance of its financial systems with the Federal Financial Management Improvement Act of 1996 (FFMIA).[45]

In audits of the IRS's financial statements, the GAO has concluded that the records were fairly presented in all material respects.[46] The GAO, however, identified some continuing serious deficiencies in the IRS's financial systems, including control weaknesses and system deficiencies affecting financial reporting, unpaid tax assessments, tax revenue and refunds, and computer security. However, the IRS again had to rely extensively on resource-intensive compensating processes to prepare its financial statements. Without a financial management system that can produce timely, accurate, and useful information needed for day-to-day decisions, the IRS's financial stewardship responsibilities continue to be one of the largest challenges facing IRS management.

MANAGING HUMAN CAPITAL

Like much of the Federal Government, managing the extensive human capital resources at the IRS remains a serious concern. Workforce issues, ranging from recruiting to training and retaining employees, have challenged Federal agencies for years. The GAO, the Office of Management and Budget, and the Office of Personnel Management have all made the strategic management of human capital a top priority. Specifically for the IRS, recent reorganization and modernization efforts, such

[45] Public Law No. 104–208, 110 Stat. 3009.

[46] Financial Audit: IRS's fiscal years 2003 and 2002 Financial Statement (GAO–04–126, dated November 2003).

as the focus on e-filing, have made many jobs dealing with processing paper tax returns redundant.

The Large and Mid-Size Business Division reported in its fiscal year 2006 strategic assessment that it will continue to lose substantial experience in the Revenue Agent position through attrition. Similarly, in the Small Business/Self-Employed Division, the human capital crisis continues to intensify as employees in key occupations increasingly become eligible for retirement, are lost through attrition, or migrate to other areas. Stagnant funding allocations have impacted the ability to attract new hires and retain existing employees. Thus, potential losses in critical occupational groups (e.g., Revenue Agents, Revenue Officers, Tax Compliance Officers), coupled with concerns regarding grade and competency gaps, further emphasize the need to strategically manage human capital.

The Tax-Exempt/Government Entities Division is already understaffed to handle the current volume of customer calls. The Division's toll-free service is still maturing and acquiring new customers; however, without additional staffing or system enhancements, the level of service will deteriorate. This issue requires immediate attention because the Division relies on quality toll-free customer service to help ensure voluntary compliance among its customers, since it has very limited resources for more traditional compliance activities like examinations.

In contrast, the Wage and Investment Division has reported that it has made significant progress in the human capital area. Examples include increased employee use of electronic learning and training by demand, and improved technical assessments for identifying skill levels and training needs of employees. In addition, the Division effectively planned and realigned its workforce as the result of reduced workload demands and technological improvements. Even so, more work needs to be completed to attract and retain high-quality employees, to increase productivity and quality, and to provide equal employment opportunities for all.

The Criminal Investigation function has also moved forward in this area. The function is implementing a computer-based knowledge management program, which can immediately identify current subject matter experts. Skill transfer programs will be implemented to provide continuity of technical subject matter expertise, and continuing education programs will provide updated training on emerging issues, strategies, and operational priority subjects.

The President's fiscal year 2006 budget may offer some relief in staffing shortages; however, the overall training and acclimation process will take some time. The IRS must devote significant attention to managing human capital to overcome the challenges noted above.

PROCESSING RETURNS AND IMPLEMENTING TAX LAW CHANGES DURING THE TAX FILING SEASON

Each filing season tests the ability of the IRS to implement tax law changes made by the Congress during the year. It is during the filing season that most individuals file their income tax returns and call the IRS if they have questions about specific tax laws or filing procedures. Correctly implementing tax law changes is a continuing challenge because the IRS must identify the tax law changes; revise the various tax forms, instructions, and publications; and reprogram the computer system used in processing returns.

This year's filing season includes significant tax law changes created by the American Jobs Creation Act of 2004.[47] One significant tax law change for the 2005 filing season that many taxpayers are familiar with is the ability to deduct sales tax instead of State and local income tax. Changes to the tax law can have a major effect on how the IRS conducts its activities, how many resources are required, and how much progress can be made on strategic goals. Generally, the Congress makes changes to the tax law each year, so some level of change is a normal part of the IRS environment. However, certain kinds of changes can significantly impact the IRS in terms of the quality and effectiveness of service and in how taxpayers perceive the IRS.

To date, we have seen no significant problems during the 2005 filing season. During the 2004 filing season, most of the 123.1 million individual income tax returns received through May 28, 2004 (including over 60 million received electronically, an increase of nearly 16 percent from 2003) were timely and accurately processed. TIGTA determined that the IRS correctly implemented the key tax law changes that affected 2003 returns. However, TIGTA has previously identified tax law changes that have not yet been effectively implemented and could result in loss of taxpayer entitlements and erroneous tax reductions. For example, TIGTA identified taxpayers

[47] Public Law No. 108–357, 118 Stat. 1418 (2004).

that are continuing to receive erroneous deductions for student loan interest, taxpayers with potentially unclaimed Additional Child Tax Credits, and taxpayers that were allowed questionable "dual benefits" for the tuition and fees deduction and the education credit.[48] These tax law changes must be effectively implemented to fairly apply the law to all taxpayers.

I hope this discussion of the major challenges facing the IRS aids you in your consideration of the IRS's appropriation for fiscal year 2006. Mr. Chairman and members of the committee, thank you for allowing me to share my views. I would be pleased to answer any questions you might have at this time.

Senator BOND. Thank you very much, Mr. George. We will try to go 5 minutes each for questioning so all of us have an opportunity to go. Now, we will go as long as we can stand up to it. So let me begin.

Mr. EVERSON. As long as you can stand up to it.

Senator BOND. I haven't lost too many witnesses at the witness table but there have been one or two occasions. I doubt if this will be the case today, but looking at BSM and the customer account data engine, CADE, which is essential for the BSM, we are concerned that IRS has re-baselined the program and has a moving set of requirements which obscures oversight and allows success to be measured in terms of garbage in rather than revenue coming out.

But let me ask two questions to begin. BSM, the biggest challenge you have, is fast approaching $2 billion, with CADE as a key feature. I would like to know, No. 1, how much will it cost to include all 120 million individual taxpayers? Moreover, since CADE currently only allows for the processing of the easiest returns of taxpayers using the EZ form, how many filers will be processed during the 2004 tax season by CADE?

BUSINESS SYSTEMS MODERNIZATION

Mr. EVERSON. Let me back up and talk about the whole program for a moment, if I may? I agree with your characterization. As I stated, the whole program has been too costly and delayed, and didn't get us the functionality we needed. When I came in 2 years ago I immediately commissioned a set of reviews. The set of reviews were consistent, the four different reviews, and the conclusions that were reached were that No. 1, we were too ambitious. We had been encouraged by the oversight board and others to move very quickly. And we spent hundreds or millions of dollars; the funding stream on this was $400 or $500 million a year at one point. We felt we needed to resize the portfolio. We had inadequate business unit involvement, meaning customers, people that were going to use these things in the process. We changed that as well. We had uneven performance by the contractor. Now, it would be easy to blame everything on the contractor, but I don't think that was appropriate. The final thing is we had very little in the way of outside experts coming in and helping us, in terms of our staff. We've addressed each of those issues and I think that we have, as I said, turned a corner. We've reset dates and we met those dates last year in both CADE and in the financial system that we put on line.

[48] The 2004 Filing Season Was Completed Timely and Accurately, but Some Tax Law Changes Have Not Been Effectively Implemented (Reference Number 2005–40–016, dated Dec. 2004).

So we brought down the funding level from about $400 million to this $200 million and we straight-lined it in fiscal year 2006, even though I think we could have made a case to increase it further this year. We want to proceed carefully and what we're doing now, Mr. Chairman, is limiting our ongoing work to just three areas so that we can stay on it. We're going to continue to work on this master file, the processing that includes the EZ's, and right now I think we're going to get 1.3 million or 1.5 million out of the total filing season for 2004. I can't tell you because we're not looking at how quickly this will ramp up over the years, what the remainder of the CADE program will be. We will get that number to you as soon we've done some additional work on it. The second piece we're working on right now, as I indicated, is the collections. There's several hundred billion dollars of monies that haven't come in to the government. We need to update our systems so that we can work better, including the pieces done by the private collection agencies. That is the thrust of our modernization effort.

And the last is electronic filing. We have mandated electronic filing for corporations. This change will speed up our audits. It cuts 1½ years out of the audit process, which now goes 5 years. It's way too long for us to detect what's going on in these corporations. We're working on those three areas, very limited, and I think we will meet our deadlines and our cost targets as we go forward because our record in the last year has been good.

Senator BOND. Thank you, Commissioner. I would like to turn to Mr. George. How can the BSM be successful, within what time frame and at what cost? What is the TIGTA assessment?

Mr. GEORGE. That's a very difficult question to answer, Mr. Chairman. When you look at CADE and then look at the fact that it's over $130 billion, $130 million over budget, and 30 months behind schedule already, and then of course when you look at the TSM, the Tax Systems Modernization effort that occurred 10 years ago, it really doesn't give one a lot of encouragement that something as massive as BSM will be any much more successful unless a complete understanding as to what went wrong with TSM is had. I don't question that the current commissioner is examining the problems and has examined the problems of tax system modernization, but it involves not only the major prime contractor, Computer Science Corp, but many subcontractors. And we are in the process, Senator, of conducting audits on some of those sub-contractors and we'll share that information with this committee once those ordered audits are complete.

Senator BOND. We appreciate your continuing to share this information with us. This hearing is just the beginning of our inquiries and we look forward to having that information.

Let me ask one quick question to the Commissioner. Since the IRS is only getting 11 of the 15 items promised with the next CADE delivery in July, can you tell me how much the government will be refunded for the four dropped items?

CUSTOMER ACCOUNT DATA ENGINE

Mr. EVERSON. I'm not sure to which items you are specifically referring. I will certainly take a look at that and provide the information for the record. We've had ongoing discussions and negotiations with the contractors and reached some pretty tough deals over the last year, where we've changed the way we're dealing with them and the relationship is subject to renegotiation. I want you to know my commitment here. I meet monthly with the President and chief operating officer of CSC and I've done that for a year and a half now, and their performance has improved significantly. We are continuing to hold their feet to the fire to make sure we get everything, every nickel's worth that the government pays.

Senator BOND. Thank you very much, Mr. Commissioner. Senator Murray.

Senator MURRAY. Thank you, Mr. Everson. I appreciate your testimony and as I talked about in my opening statement the IRS is talking about significant cuts to taxpayer services in order to pay for enforcement. You're proposing closing taxpayer assistance centers, reducing telephone service, eliminating phone-routing sites, discontinuing TeleFile, and reducing communications with practitioners. Last year, you published a comprehensive reorganization plan but those reductions are nowhere to be found in that plan. Why are you now suddenly proposing cuts when they were never a part of your recent reorganization plan?

IRS STRATEGIC PLAN AND TAXPAYER SERVICE

Mr. EVERSON. Do you mean you're citing a strategic plan? I'm not sure what you mean by the reorganization plan.

Senator MURRAY. The strategic plan that was published last year.

Mr. EVERSON. We have set out a strategic plan and it has three objectives, which are to continue to maintain and improve taxpayer services, to significantly enhance enforcement, and to modernize the IRS. And I think that plan has guided all of our internal work and our budget discussions. Now, the IRS is not protected from overall fiscal realities so we have been asked to do our share and we are going to do our share to tighten our belt where we can. What we've done is gone through a very detailed process, and my two deputies are leading a lot of discussions to tighten up where we can. We're making a lot of increases in productivity and efficiency. You mentioned reducing phone services as an example. We've taken a look at the phones. Right now we provide 15 hours of access. We're going to bring that down to 12 hours. That is comparable to what Social Security and Blue Cross/Blue Shield do. Ninety-three percent of the calls that come in fall within those 12 hours. We believe that we can save money through less overtime pay, but not reduce services there.

TAXPAYER SERVICE CENTERS

Closing the tax centers, I understand that that will cause some disruption of services. It is relatively higher cost services and our decisions here are based upon just as GAO said, an increase in things like the VITA volunteer centers. There are 14,000 VITA sites around the country. There will necessarily be a shifting of work to these sites. We see other changes. For instance, the calls coming into our telephone system now are down 6 or 7 percent this year. That reflects movement activity over to the Internet, where contacts have doubled.

Senator MURRAY. But there are always people who don't have access to the Internet.

Mr. EVERSON. Absolutely, Senator. You look at tele-file as an example where in terms of individuals, that usage has been going down 10 or 15 percent a year. I've asked our people to come up with what were the tough choices, instead of bleeding away and cutting everything over a period of years by 5 percent or something. To take a look at what we do and then make the hard choices to not do 110 different things, to strip off some of those so that we can do well what we ought to do. There are some tough choices here. I agree with you.

Senator MURRAY. But your budget says you want to improve taxpayer service by, "make it easier for people to participate in the tax system", and when you close centers that puts undue hardship on a number of people who are already living in more remote locations to travel further. So that is at odds with your statement, but let me ask you, how do you plan to measure the adverse impacts of these proposals on taxpayers?

TAXPAYER SERVICE CHANGES

Mr. EVERSON. What we have done is gone through a process that looks at five different considerations. We ended up developing two models and we've taken input from a variety of people, including an advisory committee, an IRS advisory committee, and I——

Senator MURRAY. It's a little hard to read.

Mr. EVERSON. I think you have copies of this. It's my understanding, anyway. If you don't, I'll give you mine.

Application of Criteria for Closing TAC Sites

Option I	Option II
67 TACs closed in 27 states/DC	105 TACS closed in 38 states/DC
Greater weight on employee and facilities costs	Greater weight on workload, demographics and geography
Affects more large offices in urban areas	Affects more small, medium offices in rural areas

Selecting TAC's begins with agreeing to the criteria that make up the model—stakeholders helped to determine the components

Model Criteria and Components

Sub-Model	Criterion	Sub-Model Components
1	**Geographic**	‣ Traffic volumes (Filing and Non-Filing Season) ‣ Distance to next nearest TAC ‣ Distance to nearest VITA center ‣ Distance to nearest library, post office, or kiosk
2	**Employee Cost**	‣ Number of managers, secretaries, IARs, TRRs, CSRs, and others ‣ Number of employees at the TAC ‣ Number of full-time, seasonal, and part-time employees ‣ Total direct labor hours ‣ Total overhead hours ‣ Average salary ‣ Average benefits ‣ Retirement eligibility
3	**Facilities Cost**	‣ Space usage ‣ Furniture cost ‣ Square footage cost ‣ Total rent/leasing cost ‣ Length of rent/leasing contract ‣ MITS cost
4	**Workload**	‣ Tax Law, Forms and Pubs., Return Preparation, Accounts workloads ‣ Modernization efforts applied ‣ Abandoned TACs
5	**Demographic**	‣ Population size by zip code ‣ Income level by zip code ‣ Poverty level by zip code ‣ Percentage older than 65 by zip code ‣ Population of Household income <$35,000 ‣ Number of Returns filed by zip code ‣ Number of EITC Returns filed by zip code ‣ Percentage breakout by EEO demographic categories ‣ Percent of E-file by zip code ‣ Percent Unemployed by zip code ‣ Average Education Level by zip code ‣ Percent of Households with Computers

Approximately 13,000 data points in the model criteria

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We've looked across our system. We have 408 of these taxpayer assistance centers and have compared them using some three dozen factors that we have loaded into the models we've run. There are over 13,000 different data points, is my understanding. We're looking at geography. As you say, how far is it to the next TAC? How far is it to the next volunteer center? We'd look at the cost. Obviously, a part of this is trying to drive down cost and hold the funding to a reasonable cost. It includes employee cost, it includes a facilities cost. We've looked at workload, obviously. Some TACs that are in more rural states have one or two people as opposed to in larger cities. And we've looked at demographics, changes in the country. We had a team of 12 people that's been doing this work for the last several months and we've ended up developing two models. This was after an initial conversation we had with the taxpayer advocate who has said, make sure you're looking at things that affect taxpayer access and that gets more to this question of workload. And initially a model that we had had something like 37 TACs being closed. They were all in big locations, big cities, and high cost operations, but what we've now done is refine this to two different models. One of them ends up with 67 TACs closed in 27 States across the country. And that gives a slightly greater weight to employee facilities costs. The other ends up with 105 closed and that gives more weight to issues like workload and demographics. And the difference is, in some States you obviously end up with a deeper impact like in Washington or North Dakota or any place in going to the second model. Our inclinations are to go to option No. 1. We've been reviewing these options with others and we haven't reached any final decisions. We're still refining this.

Senator MURRAY. Well, let me ask Mr. George, because in your formal testimony you expressed concern to us that the IRS may disrupt a balance between customer service and enforcement by closing some of these centers. Then you question whether the IRS has sufficient data to conclude the taxpayers that use these centers would be willing and able to use alternative methods to gain tax preparation assistance from the IRS. So given all of these uncertainties you've just seen do you believe the cost savings closing these centers will yield is worth the sacrifice that will be endured by taxpayers?

Mr. GEORGE. Senator, we have no evidence that it will or won't just because the data is not there. But the one thing that I would note that is striking in terms of what is missing from the components of the criteria that the commissioner noted is the behavior of those who use the taxpayer assistance centers. As was noted we truly do not know what options they will or will not pursue of this and I do not believe that the Internal Revenue Service has considered that as a factor when it's considered.

Senator MURRAY. Are you concerned that it's not a fair way to evaluate the system?

Mr. GEORGE. I think it is not a complete way in which to do it.

Senator MURRAY. Can you tell me exactly what you think needs to be added to it?

Mr. GEORGE. I think a very comprehensive survey of the users of the taxpayer assistance centers using a methodology which is reasonable given the large numbers that are affected by this, something of that sort, Senator.

LEGISLATIVE LANGUAGE

Mr. EVERSON. If I could prolong this for just a second. I want the committee to understand what the stakes really are here. I mentioned in the opening statement the impact if we're constrained from taking this action. We've gone through a very deliberate, careful process to try to squeeze down into the President's service mark. If you tell us not to do this and you use the President's mark for service as the ceiling, you will be doing things like forcing us into further cuts on services for telephones, stopping basic transcription of information like K1 data which we use for high income audits. We will be reducing support to our VITA programs because we have already gone through a whole series of belt tightening exercises over recent years. So I do caution you. Obviously, we will do whatever is said here but unless you——

EFFECT OF SERVICE REDUCTIONS

Senator MURRAY. Are you telling us costs savings for option No. 1 or option No. 2?

Mr. EVERSON. They both cost about $52 or $54 million, I can't remember which is which, but they're comparable for the two options.

Senator MURRAY. For what time period?

Mr. EVERSON. That is what comes out next year.

Senator MURRAY. But we don't know whether that will mean reduced number of taxes paid because people don't get the correct assistance.

Mr. EVERSON. I think that if we were to attempt to quantify that, it would be an excruciatingly long and detailed process because I've not seen any research that ties that kind of service changes directly to taxes paid give that answer. You would have to wait years to get that answer.

Senator MURRAY. That may well be but if people do their taxes accurately the first time around it does save us money in not having to go back and forth with them.

Mr. EVERSON. I agree with that. I agree with what the chairman said that if we simplify all this we would get a lot better answers. Now we're working in other areas, like the VITA sites, where TIGTA and others have said the quality of their return preparation isn't what it ought to be. We're trying to increase that service so those are the kinds of considerations we have getting at just what you're talking about.

Senator MURRAY. I'm out of time.

Senator BOND. Thank you very much, Senator Murray. Senator Dorgan.

Senator DORGAN. Mr. Chairman, thank you very much. I thank you and the ranking member. At one point, I was a chairman and then ranking member of the subcommittee that funded the IRS. I've always been very supportive of the IRS. I'm a former Tax Administrator but I'll tell you over the years you almost run out of patience on this. This year we're told modernization, a program for which we have literally shoveled money out of this Congress, is behind schedule, over budget, and probably will produce a product less valuable than anticipated. You know at some point this is not the type of science that requires sending a person to the moon. Modernizing the computer system of the Internal Revenue Service ought to be able to be done. It is really disappointing to hear these reports and we do it every year. It's not just on your watch. Behind schedule, over budget, less valuable than we expect.

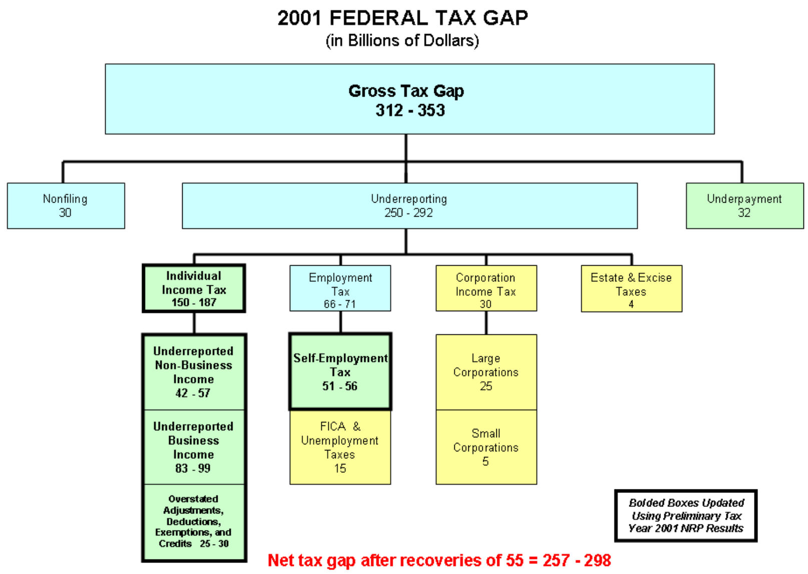
With respect to the tax gap I just wanted to make a couple of comments and ask you, Mr. Commissioner, to respond. The tax gap continues to grow. I think we need to increase enforcement in order to respond to that but we can't increase enforcement at the cost of closing taxpayer assistance centers in my judgment. For 2 years I put money in your budget for the Inspector General to go have people anonymously visit taxpayer assistance centers every 2 months and tell us about the quality of the taxpayer assistance. One of the reasons I did that is because a large percent of the time the IRS employees themselves were giving inaccurate information and couldn't complete the tax returns properly. The results were still pretty miserable, frankly. The Inspector General now has reported about 44 anonymous visits to IRS Volunteer Income Tax Assistance centers and here's what they found. These are the centers that you would increase I think if you close some taxpayer assisted centers. From February to April last year Inspector General employees conducted 44 anonymous visits to VITA sites. Thirty-five tax returns were prepared. None of them were prepared correctly. Of the 35, if 28 of those returns had been filed the IRS would have incorrectly refunded $26,000. If the remaining 7 returns had been filed, the taxpayers would have failed to receive $4,500 in refunds. For 9 of the 44 visits, tax returns were not prepared at all because the VITA sites weren't open, had been relocated or too many people were in line. But the fact is that of the 35 people who actually got help, none of them got correct help. All of them, 100 percent, incorrect. And so I mean to close taxpayer assisted centers themselves—that themselves have a pretty miserable record. Relying on VITA sites, I think is the wrong thing.

Let me just say one other thing. I think big multinational corporations are having a field day with the Internal Revenue Service on the issue of transfer pricing. They're now doing business all across the world so you have related companies in this country and abroad. They are buying and selling to each other in order to move profits out of this country so that they can't be taxed. They inflate prices, or deflated prices as it were, and let me give you some examples. Tweezers, $4,800 each purchased from your own subsidiary. That is an inflated price. Safety pins, $29 each. Deflated prices, tractor tires for $7. Pianos for $50. Missile launchers for $52. There are two professors, Doctors Simon Pak and John Zdanowicz at Penn State and Florida International University, respectively, who are doing some research, that I helped fund through an earmark to determine about how much tax revenue we may be losing due to abnormal pricing. The IRS is using the arms-length method to deal with their pricing abuses. It's like trying to take two plates of spaghetti and fuse the ends together. It is impossible and the corporations are having a field day. In my judgment, there's massive tax avoidance and nobody seems to do much about it. And there are some obvious answers to it. I don't have time to deal with it here but I wanted to make this final point.

We need more enforcement, better enforcement, smarter enforcement, and we need more taxpayer assistance and taxpayer assistance that is accurate. And if that requires additional funding we need to do that. You can't have a tax system you impose on the shoulders of the American people and say to them you comply even though paid IRS employees can't figure it out when a citizen walks up to get help. So you've got a tough job Mr. Everson. I want to be supportive of you but I'm telling you I'm really discouraged year after year to see modernization apparently failing and to see all of these other things pile up and the tax cap grow much larger. Now, is that a mouthful, and you deserve an opportunity to respond.

COMPLIANCE

Mr. EVERSON. You covered a lot of ground there. Maybe I'll be somewhat selective in what I respond to. Let's go to this chart.



No one has spoken more aggressively or acted more aggressively to go after corporations and high income individuals than I have since coming onto this job 2 years ago. We asked for more money last year. We didn't get it all, and the President's request again gives a great deal of focus, as you can see, to corporations. We're asking for $63 million in new funding, and for high-income individuals compliance we're asking for $46 million. I agree with your assessment. The corporations, it's a relatively small portion of the tax gap. We did not update the corporate tax gap in our work, but I suspect that the gap is understated. We are working aggressively on this. We're doing something like establishing a joint international tax shelter information center here in town with counterparts from Britain, Australia, and Canada. We're sharing information and we're seeing many of the things you're talking about. Corporations, in too many instances, are not just interested in going through a low tax jurisdiction, they want to set up transactions that have two different treatments in two different taxing jurisdictions, and then no taxes paid. So we're working on this very aggressively. We do need that funding to keep giving that problem prominence, and we do that even though, in terms of a tax gap, the larger portion of the tax gap is in individuals and an understatement of income, largely associated with schedule C, their own sort of business activities. We give that prominence because of the sense of fairness that is so important to average Americans. They can't feel that just because you're rich or you're a company you get away with it. So I'm with you a 100 percent on that and so is the President in terms of the allocation of resources.

BUSINESS SYSTEMS MODERNIZATION

BSM. I think there's a risk here that the committee is drawing the wrong impression. I do not disagree at all that this has been a troubled program, and it's tempting to say let's cut that program down to a $100 million or put further controls on it. That would, in my view, be exactly the wrong thing to do. We are just now getting a handle on this. We're just now delivering the systems. I think that the problems that Inspector General stated are absolutely correct, but that was a view from 2 years ago. We've acted and we are turning a corner here and if we act as if nothing has happened then you will choke it off and then we really will be at risk of this system cratering because we won't move forward. These fiscal pressures as you know, Senator, are not going to get any easier. If we don't invest in this technology, you won't get the services. Right now we're at over 50 percent of the returns being filed electronically. That is good news. It helps everybody. If we don't keep going on this—hold me accountable to do it right for sure—but if we don't continue to have a baseline of funding—and this $200 million is a very modest amount compared to where we were at $400 million or $500 million just 2 or 3 years ago—I fear we will really not make it.

Senator DORGAN. Mr. Chairman, could I just observe that if you are always turning a corner you may be going in a circle. The reason I say that and Mr. Everson I want you to succeed and I want to work with you and be helpful to you but for 8 years working on this subcommittee or some derivation of it, I've been told by Commissioners we're turning the corner. At some point it is apparently a track that we're on. So I guess in the final analysis, Mr. George, your work is very important. You tell us exactly what's happening down there. Mr. Everson, we want you to succeed. This is not criticism. It is frustration. So, Mr. Chairman, thank you for allowing me that therapy.

Senator BOND. Senator Dorgan, I hope you feel better.

Senator DORGAN. Much better. Thank you.

Senator BOND. We look forward to hearing your suggestions how we can make sure we're turning the corner in the right direction based on your experience. Senator Murray.

Senator MURRAY. Thank you very much. Mr. Chairman, I have a Veteran's Committee hearing that I want to get to so let me just ask you a quick question on the tax gap. Are there any findings in your report that are going to cause you to change your area of emphasis on enforcement?

COMPLIANCE BUDGET

Mr. EVERSON. I would say that we've looked at this and the results are preliminary, Senator. We're going to be refining them over the course of the year. That is why we've established this range. The statisticians are continuing to go through all of these areas. I have been struck by the fact that our allocation of resources is generally consistent with what we're seeing in the gap. You can see that we're asking for more money. Last year we didn't really touch individuals and small businesses very much compared to the high income and the corporation. This year in the request we're starting to move past those two areas to cover that area more—that is where the big preponderance of the gap is. And so I think what we're doing here is generally consistent. The final point I would make for you to consider is that we've got two buckets of money: criminal activity and the tax-exempt area. They're not as directly tied to the gap. It's very tempting for the committee to just fund the things that get you the very best return, but we have other responsibilities, like maintaining the integrity of tax exemption, that are very important too. So while I think our resource allocation is consistent with the findings, we have to make sure we go beyond just the tax cap.

Senator MURRAY. Okay. Thank you very much. Thank you, Mr. Chairman. I appreciate it.

Senator BOND. Thank you very much, Senator Murray. I believe that we do need to support via some funding but we need clear benchmarks and requirements. We need a plan to lay out a straight path forward, so we know we're getting there. Mr. George, I'm sure, will be all over it to help us to determine that we're on that right path. TIGTA reported that the Security Audit and Analysis System that was developed to audit online activity of IRS employees was accepted by IRS even though its required functions IRS paid for were not operating. How much did it cost? What weaknesses still exist? And what are you doing to make the system work as advertised?

IT SECURITY

Mr. EVERSON. IT security is an issue of paramount concern for us. It is something that we've recognized. After I arrived at the agency, we stripped out our security functions from a variety of pockets in the agency and put together one mission assurance organization. One of my two deputies gives it the appropriate providence. I think that is bearing results. We've never had any penetrations from the outside of the IRS into our systems. TIGTA has correctly pointed out, as have others, that when you're inside the system there's maybe too much latitude, and we do have some problems where things can get compromised from time to time. We're working on that. We need to address it further. I think we're making progress. All I can tell you is that it is the subject of regular conversations at the most senior levels. So we're not going to move off this. We're going to continue to give it the prominence it needs because we don't want the security compromised. We recognize the terrible ramifications of that.

Senator BOND. So you're telling me that we saw this theft of personal information from ChoicePoint by criminals accessing data, posing as legitimate users, but you're telling me that nobody has been able, from the outside, to access the IRS system? It is not vulnerable to similar attack?

Mr. EVERSON. That is correct. Now I don't want to sound overconfident about that. But we have really good people who continue to work on that. People try to penetrate the system, Senator, from around the world everyday, but we've got good firewalls there. And we're going to continue to be vigilant to make sure we're doing absolutely everything we can to prevent that. I think TIGTA would certainly say within the firewalls we've got some more work to do as well.

Senator BOND. I was kind of concerned when TIGTA called 100 IRS managers and employees pretending to be help desk employees, and they were able to convince 35 managers and employees to reveal their account name and change their passwords to one suggested by TIGTA. Doesn't that show the likelihood of defeating security measures? What can be done to make sure that that problem does not recur?

Mr. EVERSON. That's exactly the kind of thing I'm saying internally, within the firewalls, and we're obviously moving forward on a lot of what's in that report, and other measures. I think it is an area of continuing discussion and there's a lot of focus from TIGTA as we move forward on their stuff.

Senator BOND. Mr. George, what's your comments on that?

Mr. GEORGE. Well, Senator first of all to quote former Commissioner Sheldon Cohen, he thinks he is an honest man who has never been given the opportunity to cheat. And in effect that there are opportunities, that additional firewalls were maintained. Yes that would enhance the strength, in terms of outside attempts. But there's no question that internal access by disgruntled employees, it's a great risk to the IRS. And now that the Commissioner has restated his commitment to address that, I am more optimistic that something will and can be done. But it is something that TIGTA certainly will be monitoring, and we'll report back to you on.

Senator BOND. Thank you, Mr. George. Well, the Taxpayer Service Budget, Commissioner, assumes a reduction of $134 million through taxpayer service reengineering. Until this week, however, we had not received details on how the IRS plans to achieve these savings. The Taxpayers Advocate's testimony, as you know, said increasing enforcement and reducing service is based on more of an instinct than solid research. Can you lay out for us, and give us further detail, for the record, if that's appropriate, on how you arrive at these proposed cuts. We've had some discussions——

TAXPAYER SERVICE REENGINEERING

Mr. EVERSON. I'm absolutely happy to do that. We've had a long process of 2 or 3 months of detailed planning and weighing of options. And I think it is a sound proposal and we will provide you those details.

[The information follows:]

TAXPAYER SERVICE FISCAL YEAR 2006 BUDGET REDUCTION INITIATIVES

ASSISTANCE

Closing selected Taxpayer Assistance Centers realigns service with changing trends.—TACs are one of the most expensive methods of customer service. The number of people accessing TACs continues to decline as more taxpayers use the IRS toll-free telephone system to get answers to their questions. Web-site use and e-filing continues to rise. Volunteer tax preparation and other outreach assistance is also increasing. The IRS created a business model based on five neutral criteria to identify the most appropriate TACs to close. Based on internal and external input on the model, taxpayer-centric needs, such as workload, geography, and demographics were given greater weight than labor and facilities costs. The estimated savings are $45 million–$55 million.

Changing the Toll-Free Telephone Hours of Operation.—The hours of toll-free telephone operations will change beginning October 2005 from 15 to 12 hours 8:00 a.m.

to 8:00 p.m., Monday though Friday, in local time zones. Current call volume is low during the late evening and early morning. Ninety-three percent of the calls come in from 8 a.m. to 8 p.m. The change in level of service is minimal. The estimated savings are $10 million–$16 million.

IRS will reduce Electronic Tax Law Assistance (ETLA) service.—The will reduce the level of service in fiscal year 2006. Less than 150,000 tax law inquiries were received in fiscal year 2004. This compares with over 8.6 million tax law inquiries handled via our toll-free lines. The IRS will discontinue providing ETLA in early fiscal year 2006 for customers living in the United States. ETLA will continue for customers located overseas (Taxpayers living abroad and Military Personnel) because this is their only toll-free communication tool. The estimated is still being evaluated but is less than $1 million.

The IRS is closing non-continuing call-sites.—The IRS will consolidate work in its Boston, Chicago, Des Moines, Houston, Omaha, and Wichita telephone call-sites into its larger phone centers for greater efficiency and lower costs. The change will be invisible to customers. Taxpayers won't notice a change; their calls are currently routed and answered nationwide. The IRS has 26 call-sites nationwide—these six non-continuing sites are satellites of the 26 sites. Nationwide the IRS has approximately 15,000 employees providing customer service. Savings from staff realignment have not yet been finalized. Rent savings of up to $1.2 million will be achieved primarily in fiscal year 2007.

Updates in processing of applications for Employer ID numbers submitted through the Internet.—The IRS will complete upgrades to its system for accepting applications through the Internet for employer identification numbers (EINs). The current system for accepting the EIN applications at the front-end of the process is automated. This will improve back-end processing of the applications. By September 2006, 100 percent of the forms submitted through the Internet should be fully automated. The estimated savings are $2 million–$5 million.

Efficiencies in managing customer accounts will result in savings.—The process improvements and productivity gains achieved over the past few years, along with the decline in correspondence from taxpayers who have account or tax law inquiries, have changed the need for the same staff levels. The estimated savings are $15 million–$17 million.

OUTREACH

Greater efficiencies in distributing tax products, increases in e-filing and use of Internet to download tax products will decrease printing and postage costs.—For example: The IRS's forms distribution site will be more efficient and save staff, printing and postage resources as a result of consolidating operations from three sites to one site. Other savings include mailing out fewer tax packages because more taxpayers are filing electronically. The IRS will reduce excess quantities of tax products based on increases in e-filing and internet downloads of tax forms and publications, and by streamlining some tax products. The estimated savings are $5 million–$10 million.

Discontinuing lower value products in outreach programs and reducing some program travel will have little affect on customers.—IRS will discontinue developing some lower value publications and outreach material used to support volunteer tax assistors and outreach partners. For example, the IRS will discontinue some small quantities of end-of-season flyers, brochures and pamphlets used by its field staff, and reduce some operational travel. The estimated savings are up to $1 million.

Realigning and refocusing communications, outreach, and liaison efforts within the Small Business/Self-Employed (SB/SE) Division.—The merger will improve service to small business taxpayers and tax professionals, clarify the individual missions, coordinate programs, and minimize any overlapping responsibilities. Efficiencies gained through the realignment will allow the IRS to redirect staff resources to front line enforcement efforts. The estimated savings are $15 million–$20 million.

PROCESSING

IRS will discontinue TeleFile.—The IRS will end its TeleFile program after August 16, 2005. TeleFile allows taxpayers to file certain forms by telephone: Form 1040EZ, Income Tax Return for Single Filers and Joint Filers with No Dependents; Certain State individual tax returns, Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, and Form 941, Employer's Quarterly Federal Tax Return. Decline in use for most forms (e.g., less than 4 million of the 16 million eligible EZ filers used TeleFile), coupled with increasing costs to maintain the system, and the growth of other electronic filing options led to the decision to end the program. The expected printing and postage savings is $4 million–$5 million.

Improved efficiencies in processing tax returns.—The IRS will have additional savings due to improved efficiencies in its Service Center campus processing operations, through re-engineering of its processes, and because more taxpayers are e-filing or using computer software to prepare their tax returns. For example: The IRS is evaluating its current processing procedures so that it can reduce unnecessary labor costs, especially when the returns are prepared by taxpayers and practitioners using computer software. The IRS will improve its productivity rates in data transcription of data from the forms. The expected savings are $9 million–$12 million.

Enhancements to processing of paper Forms 941 will improve productivity.—The IRS will modify its existing Service Center Recognition/Image Processing System (SCRIPS) to add a new application for processing paper Employer's Quarterly Federal Tax Return, Forms 941. This will result in improved productivity rates and increased accuracy in data capture. Fewer additional seasonal employees will be needed. The estimated savings are $4 million–$6 million.

Senator BOND.—We would also like to have Mr. George's review of it so we can take a look at it.

You've already discussed the criteria that you're considering to close Taxpayer Assistance Centers. And you have not, as I understand it, made a determination which of the, on the blue chart, which methodology you're going to use.

Mr. EVERSON. That's correct. I think we're leaning towards the option No. 1, which has the impact of the smaller number of sites being closed. But we're still assessing that over the next coming weeks.

Senator BOND. All right. The tax gap you mentioned—how did you calculate the $4 received for every dollar of enforcement spending?

RETURN ON INVESTMENT

Mr. EVERSON. The chart that you saw there of enforcement revenues, that's a pretty simple thing. We track the collections, which is the bulk of this money. We've got a small strip, a couple of billion dollars of monies that come in from document matching activities. And then the rest is from our audits. And we follow how much money comes in from each of those actions. And now that is turning back up, that is a comparison. That $43 billion, that's cash in hand. And that compares, as I said, to the total budget that you've given us of $10.2 billion. It's a gross simplification. The $10.2 includes the $6 plus billion for enforcement, but also all the other money for processing returns or answering phones, or the outreach that we do. And I'm simply pointing out to everybody that you get $4:$1 on average. Now you get better than that, obviously, if you look only at enforcement programs.

Senator BOND. If you took the audit function and the enforcement function alone, you might get a higher number?

Mr. EVERSON. You would get a higher number, and what we try to do, Senator is run a balanced program here. We could invest in certain strips of activity that would get you $10:$1 or $20:$1, but then you would be ignoring other areas. And you'd be, maybe, going after more middle class people just on under reporting as opposed to trying to run a balanced system, where you go across that whole tax gap map. If you look at the tax gap map there are a lot of activities in there that you have to get after. And you have to show some enforcement presence across everything.

Senator BOND. Mr. George, do you have any input on those figures?

Mr. GEORGE. We're in the process now, Senator, of evaluating the methodology and the conclusions that you heard the Commissioner state. And so we will issue that report as soon as we can. And we'll give that to you.

Mr. EVERSON. That $43 billion in the methodology has been audited by GAO years ago when that system was set up. So I think the integrity of that number is pretty well established.

Senator BOND. Mr. George, as related by Senator Dorgan, your oversight of the VITA program had some pretty stunning results. Out of 35 VITA returns, they were zero for 35 in accuracy, which doesn't get you into a higher league certainly if you're batting zero. Did you present particularly difficult returns? How did you structure this?

Mr. GEORGE. Senator, there's no question that the complexity of tax law is a factor. And so that then leads to the degree to which VITA volunteers are trained. So we do have some question as to whether or not that is being effectively done. Lastly, volunteers did not in effect follow normal procedures in many instances. Some of the mistakes that were made could have been avoided had they, for example used intake sheets properly and were supervised properly. The problems we found are something that we don't believe are insurmountable. Again, through proper training and through appropriate oversight. We think many of the problems could be avoided in the future.

Senator BOND. Commissioner, what do you propose to do to fix that problem?

VITA PROGRAM

Mr. EVERSON. Let me make a couple comments on this. I think that in response to your question, were these overly complex returns, the answer is yes. And in fact TIGTA is looking at this year, I believe both parties agree—and the Inspector General wouldn't notice because he wasn't here last year—a more representative sampling of the returns. It does not yield, based upon the work that is being done now, a good return or a good rate, but it doesn't yield a zero either. So I think that the change in the methodology of how the returns have been selected shows an improvement. Now we have taken their recommendations and are working on them with one exception. We've done more training; we're working on the software, and the whole series of things. We're making sure people are using the guide. There was some contention around one suggestion, and we backed away from the proposal, that we have IRS observers doing more onsite monitoring. We probably will end up doing this in the next filing season when we satisfy ourselves that it can be handled with the appropriate disclosure discussion with taxpayers before we do it. They had recommended that step. The Taxpayer Advocate felt that it was not an appropriate step. The volunteer organizations themselves, who do the bulk of this work, have told me that they think it is good idea. AARP, which does about half of this work, they told me they were fine with having IRS people there to watch what was going on. So I think we want to do that down the road, having organized it correctly. So we have a lot more to do here. To strengthen this area, I think what they're doing is helpful to us. And they're refining what they do and we're refining what we do. And we've got to do better.

Senator BOND. IRS estimates that 740,000 people have set up offshore financial accounts, concealing taxable income at a loss of $20 to $40 billion a year. When you had a voluntary compliance initiative, only 1,300 of them came forward. How can you shut down this abusive practice? And what realistically can you do about it to go after the other 738,000-some-odd taxpayers who are non-taxpayers?

OFFSHORE VOLUNTARY COMPLIANCE INITIATIVE

Mr. EVERSON. I think that this offshore area is particularly troublesome and difficult. Basically augmenting those resources going back in to the offshore compliance and audit rate, that helps sweep in more of these taxpayers. We do look at returns. We have access to other information; we see how people are spending their money. If we see things that are out of line maybe we can get after this in other ways. But the other thing is we're getting better cooperation from other countries. We've had some issues with getting all of the information we need from credit card providers and others. But we're working through those. It is a big, big continuing challenge, internationalization and sending money offshore. It goes beyond what Senator Dorgan was saying on corporations. It really does go into individuals too. And what we have is a very aggressive program with the Justice Department to get injunctions against promoters if we see schemes that are being sold to people. We attack them and try to leverage our findings from the promoters as well.

Senator BOND. Many of the questions we raised really deal with the complexity of the IRS code. With 54,000 pages of tax law regulation and related advisory material, I think we all agree it is too complex, confusing, and costly. What can be done administratively to simplify it? And does the administration have specific legislative changes to reduce the complexity, to assist taxpayers and assist in enforcement?

TAX COMPLEXITY

Mr. EVERSON. I've testified before the Tax Panel that has been formed, as you know, with your former colleagues Senators Mack and Breaux. And I've said that the simplification is terribly important. Our view is that complexity obscures understanding. People either make inadvertent errors or they throw up their hands and say "Why bother?" at a certain point. On the other hand the complexity provides an opportunity for those who would skirt the tax laws to hide and to avoid detection by the IRS. So I agree with your sentiment 100 percent. I've said to the tax panel that compliance is something that they need to watch for when they come forward with proposals that you will ultimately see. We need to look at compliance. A couple of quick points: no system is immune to compliance issues. So you've got to consider its administerability. Look at a VAT as an example. We were in Britain a few months ago and they've got an 11 or 12 percent compliance problem with the VAT system, so you have to be cognizant of these problems, no matter what system you chose. And the administration is, I think, well aware of that, as is the tax panel as they go through these discussions.

Senator BOND. A final question. Some small business tax preparers are concerned and I wonder whether the IRS has any plans to charge fees for those who can afford them for some of IRS's services, especially where there are competing services provided by the private sector. Is it feasible to consider charging fees where it is obvious that the taxpayers, if not for getting IRS service, would be using private sector tax preparers?

FEES FOR SERVICE

Mr. EVERSON. We have something like 1.2 million tax practitioners out there that we're highly relying on. The IRS doesn't do all the work and it doesn't do all the contacts with the individuals. We rely on professionals, good professionals in lots of small firms to help us guide people through the process. I'm unaware at this time of any new fee proposals along the lines of what you've suggested. And I'll check to see what the status is and let you know. But we think the vitality of small practitioners is very central to what we're doing.

Senator BOND. Mr. George, any closing comments?

Mr. GEORGE. Senator, again thank you for the opportunity. This being my first hearing in my new capacity as IG. There is no question of the vital role that the Internal Revenue Service plays to our Nation's security. And I have known of Mark Everson and have worked with him in his capacity as managing official at OMB.

Mr. EVERSON. That's why he's skeptical.

Mr. GEORGE. Not at all, not at all. So I believe that he is committed to helping ensure that this important organization fulfills its mandate. And I can assure you that I'm committed to assisting in terms of tax administration and ensuring that that organization does what it's supposed to do. And if it engages in activity that's inappropriate, that we bring that to both your attention and to the attention of the Secretary of the Treasury.

Senator BOND. Thank you, Mr. George. Commissioner, any closing comments?

Mr. EVERSON. No. I appreciate your interest. We're in tough territory here; you've got some other needy clients. I ask you to bear in mind that we feel we've constructed a balanced proposal. But that getting this enforcement funding does help the government's top line. And that's obviously of some very real importance in this time of deficits.

ADDITIONAL SUBMITTED STATEMENTS

Senator BOND. Additional prepared statements have been submitted, and they will also be included in the record.

[The statements follow:]

PREPARED STATEMENT OF JAMES R. WHITE, DIRECTOR, STRATEGIC ISSUES, AND DAVID A. POWNER, DIRECTOR, INFORMATION TECHNOLOGY MANAGEMENT ISSUES, GOVERNMENT ACCOUNTABILITY OFFICE

INTERNAL REVENUE SERVICE—ASSESSMENT OF THE FISCAL YEAR 2006 BUDGET REQUEST

GAO HIGHLIGHTS

Highlights of GAO–05–566, a statement for the record for the Subcommittee on Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies, Committee on Appropriations.

WHY GAO DID THIS STUDY

The Internal Revenue Service (IRS) has been shifting its priorities from taxpayer service to enforcement and its management of Business Systems Modernization (BSM) from contractors to IRS staff. Although there are sound reasons for these adjustments, they also involve risks.

With respect to the fiscal year 2006 budget request, GAO assessed (1) how IRS proposes to balance its resources between taxpayer service and enforcement programs and the potential impact on taxpayers, (2) status of IRS's efforts to develop and implement the BSM program, and (3) the progress IRS has made in implementing best practices in developing its Information Technology (IT) operations and maintenance budget.

WHAT GAO RECOMMENDS

In a related statement (GAO–05–416T), GAO recommended that the Commissioner of Internal Revenue supplement the 2006 budget request with more detailed information on how proposed service reductions would impact taxpayers. GAO has recommendations still outstanding related to BSM management controls and IT budget justification.

WHAT GAO FOUND

IRS's fiscal year 2006 budget request of $10.9 billion is an increase of 3.7 percent over last year's enacted levels. This includes an 8 percent increase for enforcement, and a 1 percent and 2 percent decrease for taxpayer service and BSM. However, the potential impact of these changes on taxpayers in either the short- or long-term is unclear, because IRS has not provided details of proposed taxpayer service reductions, and although it is developing long-term goals, they are not yet finalized. Because of the proposed reductions and new and improved taxpayer services in recent years, this is an opportune time to examine the menu of services IRS provides. It may be possible to maintain the overall level of service to taxpayers by offsetting reductions in some areas with new and improved service in other areas such as on IRS's Web site.

Taxpayers and IRS are seeing some payoff from the BSM program, with the deployment of initial phases of several modernized systems in 2004. Nevertheless, the BSM program continues to be high-risk, in part, because projects have incurred significant cost increases and schedule delays and the program faces major challenges in areas such as human capital and requirements management. As a result of budget reductions and other factors, IRS has made major adjustments. It is too early to tell what effect these adjustments will have on the program, but they are not without risk and could potentially impact future budgets. Further, the BSM program is based on strategies developed years ago, which, coupled with the delays and changes brought on by budget reductions, indicates that it is time for IRS to revisit its long-term goals, strategy, and plans for BSM. Because of these challenges, IRS is redefining and refocusing the BSM program.

Likewise, IRS has made progress in implementing best practices that would improve its budget development and support for its IT operations and maintenance request. In particular, the recent release of a modernized financial management system included a cost module. However, at this time, historical data is not yet available for IRS to use this module in formulating its IT operations and maintenance request.

IRS BUDGET SUMMARY FOR KEY ACTIVITIES, FISCAL YEARS 2004–2006

[Dollars in millions]

	Fiscal Year 2004 (Enacted)	Fiscal Year 2005 (Enacted)	Fiscal Year 2006 (Request)	Percent Change (2004–2005)	Percent Change (2005–2006)	Percent Change (2004–2006)
Taxpayer service	$3,710	$3,606	$3,567	−2.8	−1.1	−3.8
Enforcement	6,052	6,392	6,893	5.6	7.8	13.9
BSM	388	203	199	−47.6	−2.0	−48.7

Source.—GAO analysis of IRS data.
Note.—Numbers may not add due to rounding.

Mr. Chairman and members of the subcommittee, we are pleased to present this statement for the record regarding the Internal Revenue Service's (IRS) fiscal year 2006 budget request and in support of your April 7, 2005 hearing on IRS's appropriations.

IRS is in the midst of making significant adjustments to its modernization strategy to better serve taxpayers and ensure their compliance with the Nation's tax laws. It is now 7 years since the passage of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98)[1] and IRS is shifting its priorities from improving taxpayer service to strengthening tax law enforcement efforts. IRS is also adjusting its strategy for managing its Business Systems Modernization (BSM) effort by shifting significant program management responsibilities from contractor to IRS staff. Although there are sound reasons for these adjustments, they also involve risk.

We have reported that IRS has made progress improving taxpayer service since the passage of RRA 98.[2] For example, IRS's telephone assistance is now more accessible and accurate. Further, IRS is more efficient at processing tax returns, in part, because of the growth of electronic filing, and has cut processing staff. IRS has also implemented some modernized information systems and increased its capacity to manage large systems acquisition and development programs. However, progress has not been uniform. We have reported on large and pervasive declines in IRS's tax law enforcement programs after 1998. We have also reported that a number of systems modernization projects were over budget and behind schedule.[3]

As noted, IRS is shifting its priorities to better address these problems. The risk, as IRS shifts its priorities towards enforcement, is that some of the gains in the quality of taxpayer service could be surrendered. There are analogous risks associated with moving more of the management of BSM in-house.

With these risks in mind, our statement for the record discusses IRS's fiscal year 2006 budget request. To address your request to provide this statement, we assessed (1) how IRS proposes to balance its resources between taxpayer service and enforcement programs and the potential impact on taxpayers, (2) the status of IRS's efforts to develop and implement the BSM program, and (3) the progress IRS has made in implementing best practices for developing its information technology (IT) operations and maintenance budget.

Our assessment of the budget request and BSM is based on a comparative analysis of IRS's fiscal year 2002 through 2006 budget requests, funding, expenditures, other documentation, and interviews with IRS officials. For this assessment, we used historical budget and performance data from reports and budget requests used by IRS, Department of Treasury, and Office of Management and Budget (OMB). In past work, we assessed IRS's budget and performance data.[4] Since the data sources and procedures for producing this year's budget data have not significantly changed from prior years, we determined that the data were sufficiently reliable for the purposes of this report although for fiscal years 2005 and 2006 subject to change. Regarding our analysis of IRS's BSM program, we primarily used the agency's BSM expenditure plans to determine the status of the program. To assess the reliability of the cost and schedule information contained in these plans, we interviewed appli-

[1] Public Law No. 105–206 (1998).

[2] See for example, GAO–05–67, Tax Administration: IRS Improved Performance in the 2004 Filing Season, But Better Data on the Quality of Some Services Are Needed (Washington, DC: Nov. 15, 2004).

[3] GAO, Internal Revenue Service: Assessment of Fiscal Year 2005 Budget Request and 2004 Filing Season Performance, GAO–04–560T (Washington, DC: Mar. 30, 2004).

[4] GAO, Tax Administration: IRS Needs to Further Refine Its Tax Filing Season Performance Measures, GAO–03–143 (Washington, DC: Nov. 22, 2002) and GAO, Financial Audit: IRS's Fiscal Years 2004 and 2003 Financial Statements, GAO–05–103 (Washington, DC: Nov. 10, 2004).

cable IRS officials to gain an understanding of the data and discuss our use of that data. In addition, we checked that information in the plans was consistent with information contained in IRS internal briefings. Accordingly, we determined that the data in the plans were sufficiently reliable for purposes of this statement. We performed our work in Washington, DC and Atlanta, Georgia from December 2004 through March 2005, in accordance with generally accepted government auditing standards.

In summary, our assessment shows that:

—IRS's 2006 fiscal year budget request reflects a continuing shift in priorities from improving taxpayer service to strengthening enforcement efforts, but the potential impact of these changes on taxpayers in both the short- and long-term is unclear. IRS is requesting $10.9 billion, an increase of 3.7 percent over fiscal year 2005 enacted levels. This includes an 8 percent increase for enforcement, and a 1 percent and 2 percent decrease for taxpayer service and BSM, respectively. IRS has not finalized the details on where reductions in taxpayer service would occur. In addition, IRS is developing, but currently lacks, long-term goals that can help IRS inform stakeholders, including the Congress, and aid them in assessing performance and making budget decisions. In light of the current budget environment and IRS's improvements in taxpayer service over the last several years, this is an opportune time to reconsider the menu of services it provides. It may be possible to maintain the overall level of assistance to taxpayers by changing the menu of services offered, offsetting reductions in some areas with new and improved service in other areas such as on IRS's Web site.

—IRS has taken important steps forward towards implementing the BSM program by delivering the initial phases of several modernized systems in 2004 and early 2005. Nevertheless, BSM continues to be high risk because, in part, its projects have incurred significant cost increases and schedule delays, and the program continues to face major challenges. As a result of funding reductions and other factors, IRS has made major adjustments to the BSM program, including reducing the management reserve and changing the mix and roles of contractor versus Federal staff used to manage the program. It is too early to tell what effect these adjustments will ultimately have on the BSM program, but they are not without risk, could potentially impact future budget requests, and will delay the implementation of certain functionality that was intended to provide benefit to IRS operations and taxpayers. Finally, the BSM program is based on visions and strategies developed years ago, which, coupled with the already significant delays the program has experienced and the changes brought on by the budget reductions, indicates that it is time for IRS to revisit its long-term goals, strategy, and plans for BSM, including an assessment of when significant future BSM functionality would be delivered. According to the Associate Chief Information Officer (CIO) for BSM, IRS is redefining and refocusing this program.

—IRS has made progress toward implementing investment management best practices that would improve its budget development and support for its IT operations and maintenance funding requests. For example, the recent release of a new accounting system included an activity-based cost module, which IRS considered to be a necessary action to implement these best practices. However, Office of the Chief Financial Officer officials stated that IRS needs 3 years of actual costs to have the historical data necessary to provide a basis for future budget estimates. Accordingly, they expect that IRS will begin using the activity-based cost module in formulating the fiscal year 2008 budget and will have the requisite 3 years of historical data in time to develop the fiscal year 2010 budget.

IRS'S BUDGET REQUEST CONTINUES TO SHIFT PRIORITY FROM TAXPAYER SERVICE TO ENFORCEMENT, BUT THE SHORT- AND LONG-TERM IMPACTS ON TAXPAYERS ARE UNCLEAR

IRS's fiscal year 2006 budget request reflects a continuing shift in priorities by proposing reductions in taxpayer service and increases in enforcement activities. The request does not provide details about how the reductions will impact taxpayers in the short-term. Nor does IRS have long-term goals; thus the contribution of the fiscal year 2006 budget request to achieving IRS's mission in the long-term is unclear. Because of budget constraints and the progress IRS has made improving the quality of taxpayer services, this is an opportune time to reconsider the menu of services IRS offers.

IRS Is Proposing Reductions in Taxpayer Service and BSM and Increases in Enforcement

IRS is requesting $10.9 billion, which includes just over a 1 percent decrease for taxpayer service, a 2 percent decrease for BSM, and nearly an 8 percent increase for enforcement, as shown in table 1.[5] As table 1 further shows, the changes proposed in the 2006 budget request continue a trend from 2004. In comparison to the fiscal year 2004 enacted budget, the 2006 budget request proposes almost 4 percent less for service, almost 49 percent less for BSM, and nearly 14 percent more for enforcement.[6]

TABLE 1.—IRS BUDGET SUMMARY FOR KEY ACTIVITIES, FISCAL YEARS 2004–2006

[Dollars in millions]

	Fiscal Year 2004 (Enacted)	Fiscal Year 2005 (Enacted)	Fiscal Year 2006 (Request)	Percent Change (2004–2005)	Percent Change (2005–2006)	Percent Change (2004–2006)
Taxpayer service	$3,710	$3,606	$3,567	−2.8	−1.1	−3.8
Enforcement	6,052	6,392	6,893	5.6	7.8	13.9
BSM	388	203	199	−47.6	−2.0	−48.7

Source.—GAO analysis of IRS data.
Note.—Numbers may not add due to rounding.

As table 1 also shows, taxpayer service sustained a reduction of $104 million or 2.8 percent between fiscal years 2004 and 2005. According to IRS officials, the majority of this reduction was the result of consolidating paper-processing operations, shifting resources from service to enforcement, and reducing some services. IRS officials said that this reduction is not expected to adversely impact the services they provide to taxpayers but added that the agency cannot continue to absorb reductions in taxpayer service without beginning to compromise some services.

For fiscal years 2005 and 2006, table 2 shows some details of changes in both dollars and full-time equivalents (FTE).[7] Both are shown because funding changes do not translate into proportional changes in FTEs due to cost increases for salaries, rent, and other items. For example, the $39 million or 1.1 percent reduction in taxpayer service translates into a reduction of 1,385 FTEs or 3.6 percent. Similarly, the over $500 million or 7.8 percent increase in enforcement spending translates into an increase of 1,961 FTEs or 3.4 percent.

TABLE 2.—IRS REQUESTED CHANGES IN FUNDING FOR TAXPAYER SERVICE AND ENFORCEMENT, FISCAL YEARS 2005 AND 2006 (REQUESTED)

[Dollars in millions]

Program Activities	Fiscal Year 2005 (Estimated)		Fiscal Year 2006 (Requested)		Change Fiscal Year 2005-Fiscal Year 2006	
	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents
Assistance	$1,829	20,798	$1,806	20,160	−$23	−638
Outreach	$500	2,473	$466	1,905	−$34	−568
Processing	$1,276	15,695	$1,295	15,516	$19	−179
Taxpayer service subtotal	$3,606	38,966	$3,567	37,581	−$39	−1,385
Research	$154	1,119	$158	1,119	$4	0
Examination	$3,478	31,498	$3,712	32,284	$234	786
Collection	$1,826	18,023	$1,991	18,815	$165	792

[5] IRS is proposing a new budget structure beginning in fiscal year 2006. The proposal would integrate support costs and the IT appropriation into taxpayer assistance and operations appropriation with eight program areas involving both taxpayer service and enforcement. See appendix I for information on the new budget structure.

[6] The administration proposes to fully fund enforcement efforts and costs as contingent appropriations. This would be achieved by using one of two budgetary mechanisms that would allow for an adjustment to total discretionary spending for fiscal year 2006 of not more than $446 million for IRS tax enforcement.

[7] According to IRS, an FTE is the equivalent of one person working full time for 1 year without overtime.

TABLE 2.—IRS REQUESTED CHANGES IN FUNDING FOR TAXPAYER SERVICE AND ENFORCEMENT, FISCAL YEARS 2005 AND 2006 (REQUESTED)—Continued

[Dollars in millions]

Program Activities	Fiscal Year 2005 (Estimated)		Fiscal Year 2006 (Requested)		Change Fiscal Year 2005-Fiscal Year 2006	
	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents
Investigation	$682	4,899	$767	5,250	$85	351
Regulatory	$253	1,912	$265	1,944	$12	32
Enforcement subtotal	$6,392	57,451	$6,893	59,412	$500	1,961
Taxpayer service and enforcement total	$9,998	96,417	$10,460	96,993	$462	576

Source.—GAO analysis of IRS data.
Note.—Numbers may not add due to rounding.

The difference between changes in dollars and FTEs could be even larger because of unbudgeted expenses. Unbudgeted expenses have consumed some of IRS's budget increases and internal savings increases over the last few years. Unbudgeted expenses include unfunded portions of annual salary increases, which can be substantial given IRS's large workforce, and other costs such as higher-than-budgeted rent increases. According to IRS officials, these unbudgeted expenses accounted for over $150 million in each of the last 4 years.

An IRS official also told us they anticipate having to cover unbudgeted expenses in 2006. As of March 2005, IRS officials were projecting unbudgeted salary increases of at least $40 million. This projection could change since potential Federal salary increases for 2006 have not been determined.

IRS Is Proposing $39 Million Less for Taxpayer Service, but the Impact on Taxpayers Is Unclear

The budget request provides some detail on how IRS plans to absorb cost increases in the taxpayer service budget. IRS is proposing a gross reduction of over $134 million in taxpayer service from reexamining the budget's base and plans to use more than $95 million of it to cover annual increases such as salaries. This leaves a net reduction of nearly $39 million or 1.1 percent in the taxpayer service budget. The extent to which IRS is able to achieve the gross reductions will impact its ability to use the funds as anticipated.

Decisions on how the $134 million gross reduction would be absorbed were not finalized prior to releasing the budget. According to IRS officials, some of the reductions would result from efficiency gains such as reducing printing and postage costs; however, others would result from reductions in the services provided to taxpayers such as shortening the hours of toll-free telephone service operations. The officials also said most decisions have now been made about general areas for reduction and most changes will not be readily apparent to taxpayers.

Although IRS has made general decisions about the reductions, many of the details have yet to be determined. Therefore, the extent of the impact on taxpayers in the short term is unclear. For example, IRS plans to reduce dependence on field assistance, including walk-in sites, but has not reached a final decision on how to reduce services. Table 3 provides further detail on how IRS is proposing to reduce funding and resources for taxpayer service.

TABLE 3.—IRS REQUESTED CHANGES IN FUNDING AND FULL-TIME EQUIVALENTS FOR TAXPAYER SERVICE, FISCAL YEARS 2005 AND 2006

[Dollars in millions]

Program Activities	Fiscal Year 2005 (Actual)		Fiscal Year 2006 (Requested)		Change Fiscal Year 2005–2006	
	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents
Assistance:						
Electronic	$1,536	17,745	$1,557	17,721	$21	−24
Field	$274	2,796	$230	2,181	−$44	−615

TABLE 3.—IRS REQUESTED CHANGES IN FUNDING AND FULL-TIME EQUIVALENTS FOR TAXPAYER SERVICE, FISCAL YEARS 2005 AND 2006—Continued

[Dollars in millions]

Program Activities	Fiscal Year 2005 (Actual)		Fiscal Year 2006 (Requested)		Change Fiscal Year 2005–2006	
	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents	Dollars	Full-time Equivalents
EITC assistance	$19	258	$19	258	<$1	....
Assistance total	$1,829	20,798	$1,806	20,160	−$23	−638
Outreach:						
Publication & Media	$291	821	$276	520	−$15	−301
Taxpayer Education & Communication	$203	1,592	$184	1,326	−$19	−266
EITC Outreach	$7	60	$7	60	<$1	....
Outreach total	$500	2,473	$466	1,905	−$34	−568
Processing	$1,276	15,695	$1,295	15,516	$19	−179
Taxpayer service total	$3,606	38,966	$3,568	37,581	−$39	−1,385

Source.—GAO analysis of IRS data.
Note.—Numbers may not add due to rounding.

IRS Continues to Request Significant Increases for Enforcement to Build on Recent Hiring Gains

IRS's fiscal year 2006 budget request is the sixth consecutive year the agency has requested additional staffing for enforcement. However, up until last year, IRS was unable to increase enforcement staffing; unbudgeted costs and other priorities consumed the budget increase.

IRS's proposal for fiscal year 2006, if implemented as planned, would return enforcement staffing in these occupations to their highest levels since 1999. Of the more than $500 million increase requested for 2006, about $265 million would fund enforcement initiatives, over $182 million would be used in part for salary increases, and over $55 million is a proposal to transfer funding authority from the Department of Justice's Interagency Crime and Drug Enforcement. The $500 million increase would be supplemented by internal enforcement savings of $88 million. As is the case with taxpayer service savings, the extent to which IRS achieves enforcement savings will affect its ability to fund the new enforcement initiatives.

The $265 million for new enforcement initiatives consist of:

—$149.7 million and 920 FTEs to attack corrosive non-compliance activity driving the tax gap such as abusive trusts and shelters, including offshore credit cards and organized tax resistance;

—$51.8 million and 236 FTEs to detect and deter corrosive corporate non-compliance to attack complex abusive tax avoidance transactions on a global basis and challenge those who promote their use;

—$37.9 million and 417 FTEs to increase individual taxpayer compliance by identifying and implementing actions to address non-compliance with filing requirements; increasing Automated Underreporter resources to address the reporting compliance tax gap; increasing audit coverage; and expanding collection work in walk-in sites;

—$14.5 million and 77 FTEs to combat abusive transactions by entities with special tax status by initiating examinations more promptly, safeguarding compliant customers from unscrupulous promoters, and increasing vigilance to ensure that the assets of tax-exempt organizations are put to their intended tax-preferred purpose and not misdirected to fund terrorism or for private gain; and

—$10.8 million and 22 FTEs to curtail fraudulent refund crimes.

The $88 million in internal savings would be reinvested to perform the following activities:

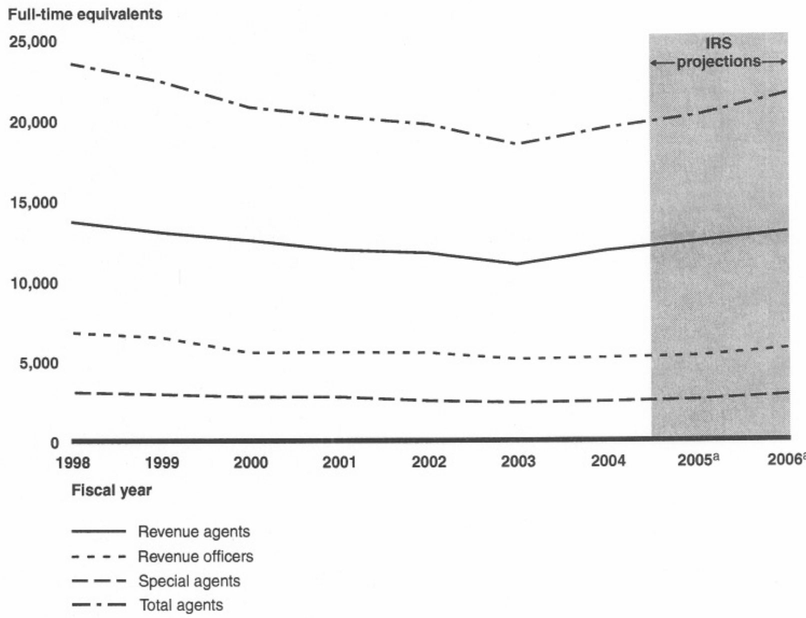
—$66.7 million and 585 FTEs to devote resources to front-line enforcement activities;

—$14.9 million and 156 FTEs to, in part, address bankruptcy-related taxpayer questions; and

—$6.7 million and 52 FTEs to address complex, high-risk issues such as compliance among tax professionals.

In the past, IRS has had trouble achieving enforcement staffing increases because other priorities, including unbudgeted expenses, have absorbed additional funds. IRS achieved some gains in 2004 and expects modest gains in 2005. Figure 1 shows that the number of revenue agents (those who audit complex returns), revenue officers (those who do field collection work), and special agents (those who perform criminal investigations) decreased over 21 percent between 1998 and 2003, but increased almost 6 percent from 2003 to 2004.

Figure 1: Revenue Agents, Revenue Officers, and Special Agents, Fiscal Years 1998-2006



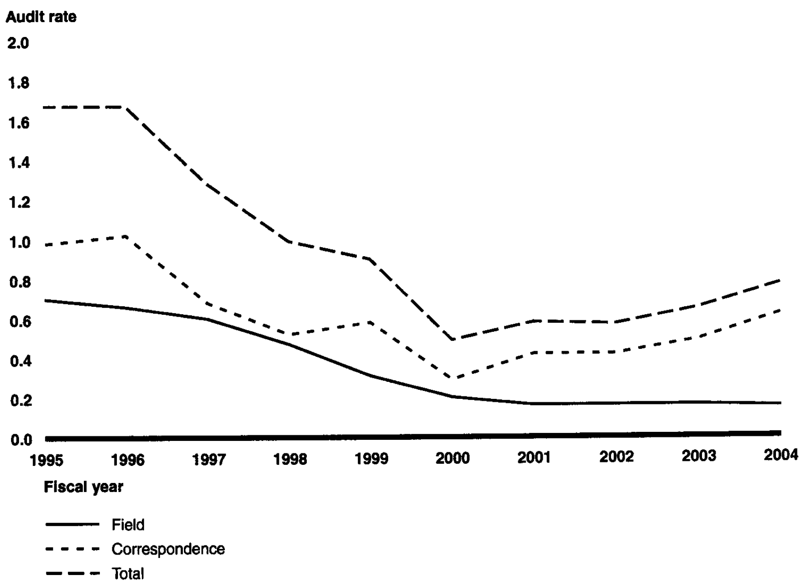
Source: GAO analysis of IRS data.

[a] Fiscal years 2005 and 2006 are IRS projections.

IRS's recent gains in enforcement staffing are encouraging, as tax law enforcement continues to remain an area of high risk for the Federal Government because the resources IRS has dedicated to enforcing the tax laws have declined, while IRS's enforcement workload—measured by the number of taxpayer returns filed—has continually increased.[8] Figure 2 shows the trend in field, correspondence, and total audit rates since 1995. Field audits involve face-to-face audits and correspondence audits are typically less complex involving communication through notices. IRS experienced steep declines in audit rates from 1995 to 1999, but the audit rate—the proportion of tax returns that IRS audits each year—has slowly increased since 2000. The figure shows that the increase in total audit rates of individual filers has been driven mostly by correspondence audits, while more complex field audits, continue to decline.

[8] GAO, High Risk Series: An Update, GAO–05–207 (Washington, DC: January 2005).

Figure 2: Audit Rate of Individual Income Tax Returns, Fiscal Years 1995-2004



Source: GAO analysis of IRS data.

The link between the decline in enforcement staff and the decline in enforcement actions, such as audits, is complicated, and the real impact on taxpayers' rate of voluntary compliance is not known. This leaves open the question of whether the declines in IRS's enforcement programs are eroding taxpayers' incentives to voluntarily comply. IRS's National Research Program (NRP) recently completed a study on compliance by individual tax filers based on tax data provided on 2001 tax returns. The study estimated that the tax gap—the difference between what taxpayers owe and what they pay—is at least $312 billion per year as of 2001 and could be as large as $353 billion. This study is important for several reasons beyond measuring compliance. It is intended to help IRS better target its enforcement actions, such as audits, on non-compliant taxpayers, and minimize audits of compliant taxpayers. It should also help IRS better understand the impact of taxpayer service on compliance.

IRS Is Developing Long-term Goals That Can Be Used to Assess Performance and Make Budget Decisions

IRS is developing but currently lacks long-term goals that can be used to assess performance and make budget decisions.[9] Long-term goals and results measurement are a component of the statutory strategic planning and management framework that the Congress adopted in the Government Performance and Results Act of 1993.[10] As a part of this comprehensive framework, long-term goals that are linked

[9] IRS has one long-term goal set by the Congress in RRA 98 for IRS to have 80 percent of all individual income tax returns filed electronically.

[10] Public Law No. 103–62 (1993). The Government Performance and Results Act of 1993 seeks to improve the management of Federal programs, as well as their effectiveness and efficiency, by requiring executive agencies to prepare multiyear strategic plans, annual performance plans, and annual performance reports. Under the Act, strategic plans are the starting point for setting goals and measuring progress towards them. The Act requires executive agencies to develop strategic plans that include an agency's mission statement, long-term general goals, and the strategies that the agency will use to achieve these goals. The plans should also explain the key external factors that could significantly affect achievement of these goals, and describe how long-term goals will be related to annual performance goals.

to annual performance measures can help guide agencies when considering organizational changes and making resource decisions.

A recent Program Assessment Rating Tool (PART) review conducted by OMB reported that IRS lacks long-term goals.[11] As a result, IRS has been working to identify and establish long-term goals for all aspects of its operations for over a year. IRS officials said these goals will be finalized and provided publicly as an update to the agency's strategic plan before May 2005.

For IRS and its stakeholders, such as the Congress, long-term goals can be used to assess performance and progress towards these goals, and determine whether budget decisions contribute to achieving those goals.

Without long-term goals, the Congress and other stakeholders are hampered in evaluating whether IRS is making satisfactory long-term progress. Further, without such goals, the extent to which IRS's 2006 budget request would help IRS achieve its mission over the long-term is unclear.

This Is an Opportune Time to Review IRS's Menu of Taxpayer Services

For at least two reasons, this is an opportune time to review the menu of taxpayer services that IRS provides. First, IRS's budget for taxpayer services was reduced in 2005 and an additional reduction is proposed for 2006. As already discussed, these reductions have forced IRS to propose scaling back some services. Second, as we have reported, IRS has made significant progress in improving the quality of its taxpayer services. For example, IRS now provides many Internet services that did not exist a few years ago and has noticeably improved the quality of telephone services. This opens up the possibility of maintaining the overall level of taxpayer service but with a different menu of service choices. Cuts in selected services could be offset by the new and improved services.

Generally, as indicated in the budget, the menu of taxpayer services that IRS provides covers assistance, outreach, and processing. Assistance includes answering taxpayer questions via telephone, correspondence, and face-to-face at its walk-in sites. Outreach includes educational programs and the development of partnerships. Processing includes issuing millions of tax refunds.

When considering program reductions, we support a targeted approach rather than across-the-board cuts.[12] A targeted approach helps reduce the risk that effective programs are reduced or eliminated while ineffective or lower priority programs are maintained.

With the above reasons in mind for reconsidering IRS's menu of services, we have compiled a list of options for targeted reductions in taxpayer service. The options on this list are not recommendations but are intended to contribute to a dialogue about the tradeoffs faced when setting IRS's budget. The options presented meet at least one of the following criteria that we generally use to evaluate programs or budget requests.[13] These criteria include that the activity:

—duplicates other efforts that may be more effective and/or efficient;

—historically does not meet performance goals or provide intended results as reported by GAO, the Treasury Inspector General for Tax Administration (TIGTA), IRS, or others;

—experiences a continued decrease in demand;

—lacks adequate oversight, implementation and management plans, or structures and systems to be implemented effectively;

—has been the subject of actual or requested funding increases that cannot be adequately justified; or

—has the potential to make an agency more self-sustaining by charging user fees for services provided.

We recognize that the options listed below involve tradeoffs. In each case, some taxpayers would lose a service they use. However, the savings could be used to help maintain the quality of other services. We also want to give IRS credit for identifying savings, including some on this list. The options include:

—closing walk-in sites. Taxpayer demand for walk-in services has continued to decrease and staff answer a more limited number of tax law questions in person than staff answer via telephone.

[11] The PART was applied during the fiscal year 2004 budget cycle to "programs" selected by OMB. The PART includes general questions in each of four broad topics to which all programs are subjected: (1) program purpose and design; (2) strategic planning; (3) program management; and (4) program results (i.e., whether a program is meeting its long-term and annual goals). OMB also makes an overall assessment on program effectiveness.

[12] GAO, 21st Century Challenges: Reexamining the Base of the Federal Government, GAO–05–325SP (Washington, DC: February 2005).

[13] We selected these criteria from a variety of sources based on generally accepted government auditing standards.

—limiting the type of telephone questions answered by IRS assistors. IRS assistors still answer some refund status questions even though IRS provides automated answers via telephone and its Web site.
—mandating electronic filing for some filers such as paid preparers or businesses. As noted, efficiency gains from electronic filing have enabled IRS to consolidate paper processing operations.
—charging for services. For example, IRS provides paid preparers with information on Federal debts owed by taxpayers seeking refund anticipation loans.

PROGRESS IN BSM IMPLEMENTATION, BUT THE PROGRAM REMAINS HIGH RISK AND BUDGET REDUCTIONS HAVE RESULTED IN SIGNIFICANT ADJUSTMENTS

Although IRS has implemented important elements of the BSM program, much work remains. In particular, the BSM program remains at high risk and has a long history of significant cost overruns and schedule delays. Furthermore, budget reductions have resulted in significant adjustments to the BSM program, although it is too early to determine their ultimate effect.

IRS Has Made Progress in Implementing BSM, but Much Work Remains

IRS has long relied on obsolete automated systems for key operational and financial management functions, and its attempts to modernize these aging computer systems span several decades. IRS's current modernization program, BSM, is a highly complex, multibillion-dollar program that is the agency's latest attempt to modernize its systems. BSM is critical to supporting IRS's taxpayer service and enforcement goals. For example, BSM includes projects to allow taxpayers to file and retrieve information electronically and to provide technology solutions to help reduce the backlog of collections cases. BSM is important for another reason. It allows IRS to provide the reliable and timely financial management information needed to account for the Nation's largest revenue stream and better enable the agency to justify its resource allocation decisions and congressional budgetary requests.

Since our testimony before this subcommittee on last year's budget request, IRS has deployed initial phases of several modernized systems under its BSM program. The following provides examples of the systems and functionality that IRS implemented in 2004 and the beginning of 2005.

—*Modernized e-File (MeF)*.—This project is intended to provide electronic filing for large corporations, small businesses, and tax-exempt organizations. The initial releases of this project were implemented in June and December 2004, and allowed for the electronic filing of forms and schedules for the form 1120 (corporate tax return) and form 990 (tax-exempt organizations' tax return). IRS reported that, during the 2004 filing season, it accepted over 53,000 of these forms and schedules using MeF.
—*e-Services*.—This project created a Web portal and provided other electronic services to promote the goal of conducting most IRS transactions with taxpayers and tax practitioners electronically. IRS implemented e-Services in May 2004. According to IRS, as of late March 2005, over 84,000 users have registered with this Web portal.
—*Customer Account Data Engine (CADE)*.—CADE is intended to replace IRS's antiquated system that contains the agency's repository of taxpayer information and, therefore, is the BSM program's linchpin and highest priority project. In July 2004 and January 2005, IRS implemented the initial releases of CADE, which have been used to process filing year 2004 and 2005 1040EZ returns, respectively, for single taxpayers with refund or even-balance returns. According to IRS, as of March 16, 2005, CADE had processed over 842,000 tax returns so far this filing season.
—*Integrated Financial System (IFS)*.—This system replaces aspects of IRS's core financial systems and is ultimately intended to operate as its new accounting system of record. The first release of this system became fully operational in January 2005.

Although IRS is to be applauded for delivering such important functionality, the BSM program is far from complete. Future deliveries of additional functionality of deployed systems and the implementation of other BSM projects are expected to have a significant impact on IRS's taxpayer services and enforcement capability. For example, IRS has projected that CADE will process about 2 million returns in the 2005 filing season. However, the returns being processed in CADE are the most basic and constitute less than 1 percent of the total tax returns expected to be processed during the current filing season. IRS expects the full implementation of CADE to take several more years. Another BSM project—the Filing and Payment Compliance (F&PC) project—is expected to increase (1) IRS's capacity to treat and resolve the backlog of delinquent taxpayer cases, (2) the closure of collection cases by 10 million annually by 2014, and (3) voluntary taxpayer compliance. As part of this project, IRS plans to implement an initial limited private debt collection capability in January 2006, with full implementation of this aspect of the F&PC project to be delivered by January 2008 and additional functionality to follow in later years.

BSM Program Has History of Cost Increases and Schedule Delays and Is High Risk

The BSM program has a long history of significant cost increases and schedule delays, which, in part, has led us to report this program as high-risk since 1995.[14] Appendix II provides the history of the BSM life-cycle cost and schedule variances. In January 2005 letters to congressional appropriation committees, IRS stated that it had showed a marked improvement in significantly reducing its cost variances. In particular, IRS claimed that it reduced the variance between estimated and actual costs from 33 percent in fiscal year 2002 to 4 percent in fiscal year 2004. However, we do not agree with the methodology used in the analysis supporting this claim. Specifically, (1) the analysis did not reflect actual costs, instead it reflected changes in cost estimates (i.e., budget allocations) for various BSM projects; (2) IRS aggregated all of the changes in the estimates associated with the major activities for some projects, such as CADE, which masked that monies were shifted from future activities to cover increased costs of current activities; and (3) the calculations were based on a percentage of specific fiscal year appropriations, which does not reflect that these are multiyear projects.

In February 2002 we expressed concern over IRS's cost and schedule estimating and made a recommendation for improvement.[15] IRS and its prime systems integration support (PRIME) contractor have taken action to improve their estimating practices, such as developing a cost and schedule estimation guidebook and developing a risk-adjustment model to include an analysis of uncertainty. These actions may ultimately result in more realistic cost and schedule estimates, but our analysis of IRS's expenditure plans[16] over the last few years shows continued increases in estimated project life-cycle costs (see fig. 3).

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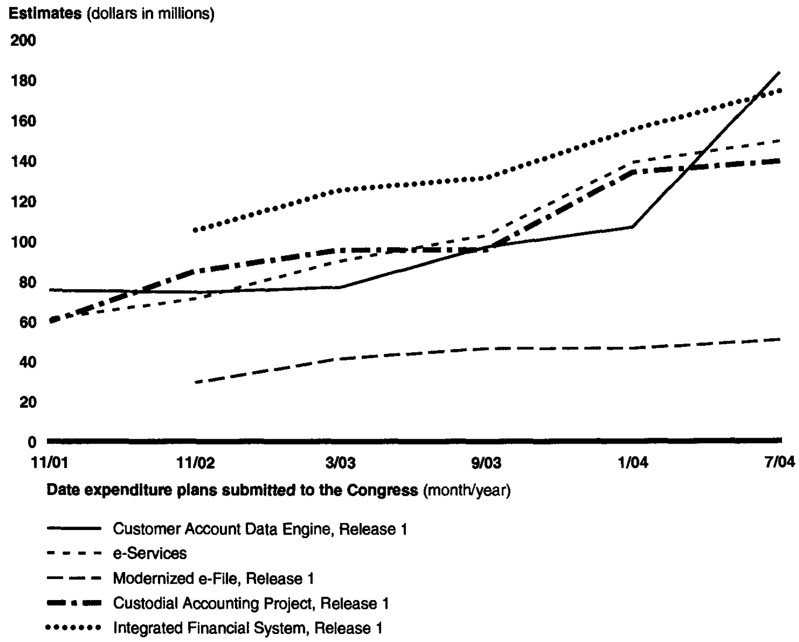
[14] For our latest high-risk report, please see GAO, High-Risk Series: An Update, GAO–05–207 (Washington, DC, January 2005).

[15] GAO, Business Systems Modernization: IRS Needs to Better Balance Management Capacity with Systems Acquisition Workload, GAO–02–356 (Washington, DC: Feb. 28, 2002).

[16] BSM funds are unavailable until the IRS submits to congressional appropriations committees for approval a modernization expenditure plan that (1) meets the OMB capital planning and investment control review requirements; (2) complies with IRS's enterprise architecture; (3) conforms with IRS's enterprise life-cycle methodology; (4) is approved by IRS, the Department of the Treasury, and OMB; (5) is reviewed by GAO; and (6) complies with acquisition rules, requirements, guidelines, and systems acquisition management practices.

Figure 3: Life-cycle Cost Estimates for Key BSM Projects



Source: GAO analysis of IRS data.

The Associate CIO for BSM stated that he believes that IRS's cost and schedule estimating has improved in the past year. In particular, he pointed out that IRS met its cost and schedule goals for the implementation of the latest release of CADE, which allowed the agency to use this system to process certain 1040EZ forms in the 2005 filing season. It is too early to tell whether this signals a fundamental improvement in IRS's ability to accurately forecast project costs and schedules.

The reasons for IRS's cost increases and schedule delays vary. However, we have previously reported that they are due, in part, to weaknesses in management controls and capabilities. We have previously made recommendations to improve BSM management controls, and IRS has implemented or begun to implement these recommendations. For example, in February 2002, we reported that IRS had not yet defined or implemented an IT human capital strategy, and recommended that IRS develop plans for obtaining, developing, and retaining requisite human capital resources.[17] In September 2003, TIGTA reported that IRS had made significant progress in developing a human capital strategy but that it needed further development. In August 2004, the current Associate CIO for BSM identified the completion of a human capital strategy as a high priority. Among the activities that IRS is implementing are prioritizing its BSM staffing needs and developing a recruiting plan. IRS has also identified, and is addressing, other major management challenges in areas such as requirements, contract, and program management. For example, poorly defined requirements have been among the significant weaknesses that have been identified as contributing to project cost overruns and schedule delays. As part of addressing this problem, in March 2005, the IRS BSM office established a requirements management office, although a leader has not yet been hired.

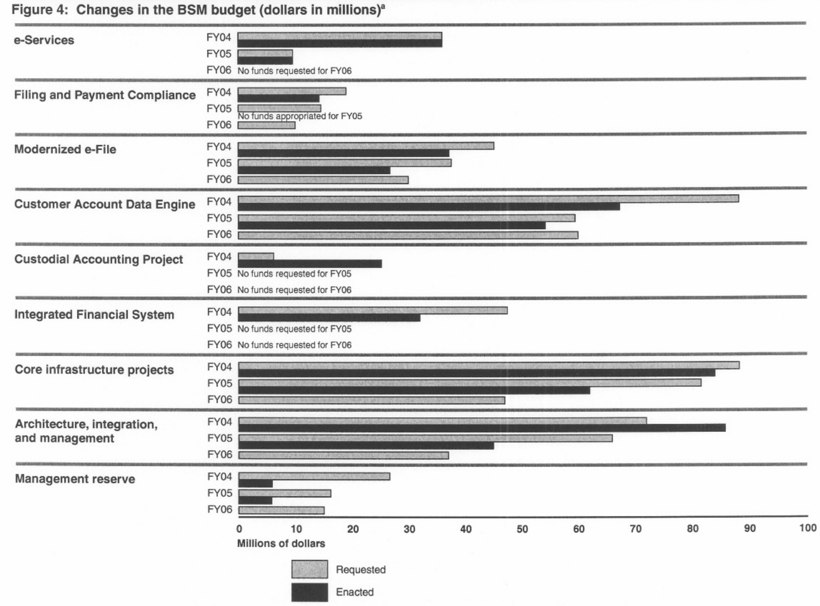
IRS Is Adjusting the BSM Program in Response to Budget Reductions

The BSM program is undergoing significant changes as it adjusts to reductions in its budget. Figure 4 illustrates the BSM program's requested and enacted budg-

[17] GAO–02–356.

ets for fiscal years 2004 through 2006.[18] For fiscal year 2005, IRS received about 29 percent less funding than it requested (from $285 million to $203.4 million). According to the Senate report for the fiscal year 2005 Transportation, Treasury, and General Government appropriations bill, in making its recommendation to reduce BSM funding, the Senate Appropriations Committee was concerned about the program's cost overruns and schedule delays. In addition, the committee emphasized that in providing fewer funds, it wanted IRS to focus on its highest priority projects, particularly CADE.[19] In addition, IRS's fiscal year 2006 budget request reflects an additional reduction of about 2 percent, or about $4.4 million, from the fiscal year 2005 appropriation.

Figure 4: Changes in the BSM budget (dollars in millions)[a]



Source: IRS.

[a] The BSM account authorizes funds to be obligated for 3 years.

It is too early to tell what effect the budget reductions will ultimately have on the BSM program. However, the significant adjustments that IRS is making to the program to address these reductions are not without risk, could potentially impact future budget requests, and will delay the implementation of certain functionality that was intended to provide benefit to IRS operations and the taxpayer. For example:

—*Reductions in Management reserve/project risk adjustments*.—In response to the fiscal year 2005 budget reduction, IRS reduced the amount that it had allotted to program management reserve and project risk adjustments by about 62 percent (from about $49.1 million to about $18.6 million).[20] If BSM projects have future cost overruns that cannot be covered by the depleted reserve, this reduction could result in (1) increased budget requests in future years or (2) delays in planned future activities (e.g., delays in delivering promised functionality) to use those allocated funds to cover the overruns.

—*Shifts of BSM management responsibility from the PRIME contractor to IRS*.—Due to budget reductions and IRS's assessment of the PRIME contractor's performance, IRS decided to shift significant BSM responsibilities for program management, systems engineering, and business integration from the PRIME

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[18] IRS uses the appropriated funds to cover contractor costs related to the BSM program. IRS funds internal costs for managing BSM with another appropriation. These costs are not tracked separately for BSM-related activities.

[19] U.S. Senate, Senate Report 108–342 (2004).

[20] We did not include in our calculations, reductions to specific project risk adjustment amounts that were made for reasons other than the fiscal year 2005 budget reduction.

contractor to IRS staff. For example, IRS staff are assuming responsibility for cost and schedule estimation and measurement, risk management, integration test and deployment, and transition management. There are risks associated with this decision. To successfully accomplish this transfer, IRS must have the management capability to perform this role. Although the BSM program office has been attempting to improve this capability through, for example, implementation of a new governance structure and hiring staff with specific technical and management expertise, IRS has had significant problems in the past managing this and other large development projects, and acknowledges that it has major challenges to overcome in this area.

—*Suspension of the Custodial Accounting Project (CAP)*.—Although the initial release of CAP went into production in September 2004, IRS has decided not to use this system and to stop work on planned improvements due to budget constraints. According to IRS, it made this decision after it evaluated the business benefits and costs to develop and maintain CAP versus the benefits expected to be provided by other projects, such as CADE. Among the functionality that the initial releases of CAP were expected to provide were (1) critical control and reporting capabilities mandated by federal financial management laws; (2) a traceable audit trail to support financial reporting; and (3) a subsidiary ledger to accurately and promptly identify, classify, track, and report custodial revenue transactions and unpaid assessments. With the suspension of CAP, it is now unclear how IRS plans to replace the functionality this system was expected to provide, which was intended to allow the agency to make meaningful progress toward addressing long-standing financial management weaknesses. IRS is currently evaluating alternative approaches to addressing these weaknesses.

—*Reductions in planned functionality*.—According to IRS, the fiscal year 2006 funding reduction will result in delays in planned functionality for some of its BSM projects. For example, IRS no longer plans to include Form 1041 (the income tax return for estates and trusts) in the fourth release of Modernized e-File, which is expected to be implemented in fiscal year 2007.

The BSM program is based on visions and strategies developed in 2000 and 2001. The age of these plans, in conjunction with the significant delays already experienced by the program and the substantive changes brought on by budget reductions, indicate that it is time for IRS to revisit its long-term goals, strategy, and plans for BSM. Such an assessment would include an evaluation of when significant future BSM functionality would be delivered. IRS's Associate CIO for BSM has recognized that it is time to recast the agency's BSM strategy because of changes that have occurred subsequent to the development of the program's initial plans. According to this official, IRS is redefining and refocusing the BSM program, and he expects this effort to be completed by the end of this fiscal year.

ADDITIONAL ACTIONS NEEDED TO IMPROVE BUDGETING FOR IT OPERATIONS AND MAINTENANCE

IRS has requested about $1.62 billion for IT operations and maintenance in fiscal year 2006, within its proposed new Tax Administration and Operations account. Under the prior years' budget structure, these funds were included in a separate account, for which IRS received an appropriation of about $1.59 billion in fiscal year 2005. The $1.62 billion requested in fiscal year 2006 is intended to fund the personnel costs for IT staff (including staff supporting the BSM program) and activities such as IT security, enterprise networks, and the operations and maintenance costs of its current systems. We have previously expressed concern that IRS does not employ best practices in the development of its IT operations and maintenance budget request.[21] Although IRS has made progress in addressing our concern, more work remains.

The Paperwork Reduction Act (PRA) of 1995[22] requires Federal agencies to be accountable for their IT investments and responsible for maximizing the value and managing the risks of their major information systems initiatives. The Clinger-Cohen Act of 1996[23] establishes a more definitive framework for implementing the PRA's requirements for IT investment management. It requires Federal agencies to focus more on the results they have achieved and introduces more rigor and structure into how agencies are to select and manage IT projects. In addition, leading private- and public-sector organizations have taken a project- or system-centric ap-

[21] GAO, Internal Revenue Service: Improving Adequacy of Information Systems Budget Justification, GAO–02–704 (Washington, DC, June 28, 2002).
[22] Public Law No. 104–13 (1995).
[23] Public Law No. 104–106 section 5001 et. seq. (1996).

proach to managing not only new investments but also operations and maintenance of existing systems. As such, these organizations:

—identify operations and maintenance projects and systems for inclusion in budget requests;

—assess these projects or systems on the basis of expected costs, benefits, and risks to the organization;

—analyze these projects as a portfolio of competing funding options; and

—use this information to develop and support budget requests.

This focus on projects, their outcomes, and risks as the basic elements of analysis and decision making is incorporated in the IT investment management approach that is recommended by OMB and GAO. By using these proven investment management approaches for budget formulation, agencies have a systematic method, on the basis of risk and return on investment, to justify what are typically substantial information systems operations and maintenance budget requests.

In our assessment of IRS's fiscal year 2003 budget request, we reported that the agency did not develop its information systems operations and maintenance request in accordance with the investment management approach used by leading organizations. We recommended that IRS prepare its future budget requests in accordance with these best practices.[24] To address our recommendation, IRS agreed to take a variety of actions, which it has made progress in implementing. For example, IRS stated that it planned to develop an activity-based cost model to plan, project, and report costs for business tasks/activities funded by the information systems budget. The recent release of IFS included an activity-based cost module, but IRS does not currently have historical cost data to populate this module. According to officials in the Office of the Chief Financial Officer, IRS is in the process of accumulating these data. These officials stated that IRS needs 3 years of actual costs to have the historical data that would provide a basis for future budget estimates. Accordingly, these officials expected that IRS would begin using the IFS activity-based cost module in formulating the fiscal year 2008 budget request and would have the requisite 3 years' of historical data in time to develop the fiscal year 2010 budget request. In addition, IRS planned to develop a capital planning guide to implement processes for capital planning and investment control, budget formulation and execution, business case development, and project prioritization. IRS has developed a draft guide, which is currently under review by IRS executives, and IRS expects it to become policy on October 1, 2005. Although progress has been made in implementing best practices in the development of the IT operations and maintenance budget, until these actions are completely implemented IRS will not be able to ensure that its request is adequately supported.

CONCLUSIONS

As IRS shifts its priorities to enforcement and faces tight budgets for service, the agency will be challenged to maintain the gains it has made in taxpayer service. In order to avoid a "swinging pendulum," where enforcement gains are achieved at the cost of taxpayer service and vice versa, IRS and the Congress would benefit from a set of agreed-upon long-term goals. Long-term goals would provide a framework for assessing budgetary tradeoffs between taxpayer service and enforcement and whether IRS is making satisfactory progress towards achieving those goals. Similarly, long-term goals could help identify priorities within the taxpayer service and enforcement functions. For example, if the budget for taxpayer service were to be cut and efficiency gains did not offset the cut, long-term goals could help guide decisions about whether to make service cuts across the board or target selected services. To its credit, IRS has been developing a set of long-term goals, so we are not making a recommendation on goals. However, we want to underscore the importance of making the goals public in a timely fashion, as IRS has planned. The Congress would then have an opportunity to review the goals and start using them as a tool for holding IRS accountable for performance.

In addition, the Congress would benefit from more information about the short-term impacts of the 2006 budget request on taxpayers. The 2006 budget request cites a need for reducing the hours of telephone service and scaling back walk-in assistance but provides little additional detail. Without more detail about how taxpayers will be affected, it is difficult to assess whether the 2006 proposed budget would allow IRS to achieve its stated intent of both maintaining a high level of taxpayer service and increasing enforcement.

BSM and related initiatives such as electronic filing hold the promise of delivering further efficiency gains that could offset the need for larger budget increases to fund

[24] GAO–02–704.

taxpayer service and enforcement. Today, taxpayers have seen payoffs from BSM; however, the program is still high risk and budget reductions have caused substantive program changes. IRS has recognized it is time to revisit its long-term BSM strategy and is currently refocusing the program. As we did with long-term goals above, we want to underscore the importance of timely completion of the revision of the BSM strategy.

RECOMMENDATION

In a related statement (GAO–05–416T), GAO recommended that the Commissioner of Internal Revenue supplement the 2006 budget request with more detailed information on how proposed service reductions would impact taxpayers.

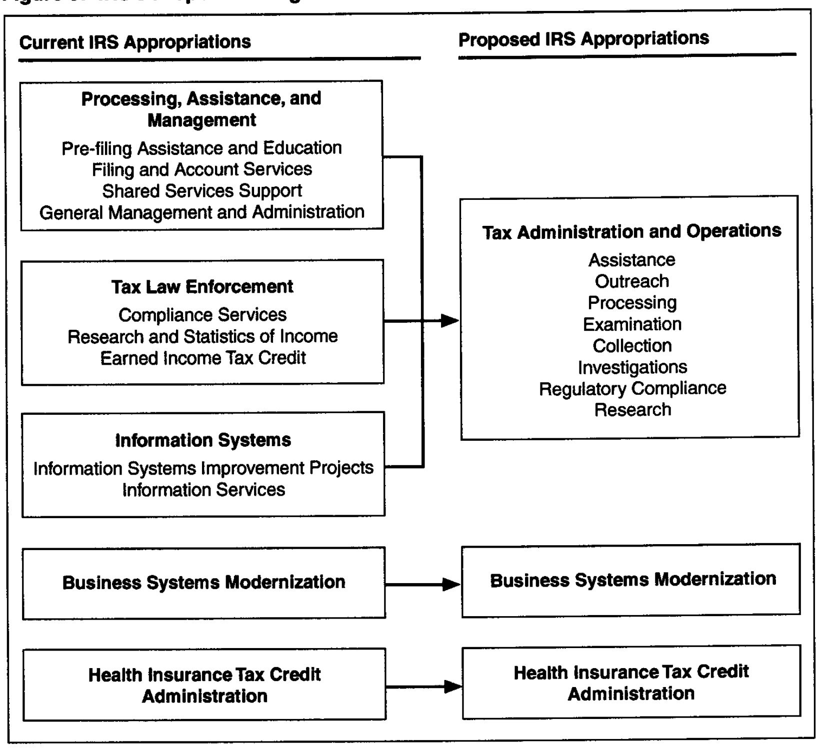
APPENDIX I.—DESCRIPTION OF IRS'S PROPOSED BUDGET STRUCTURE

IRS's proposed new budget structure as depicted in figure 5 combines the three major appropriations that the agency has had in the past—Processing, Assistance, and Management; Tax Law Enforcement; and Information Systems into one appropriation called Tax Administration and Operations. The Business Systems Modernization and Health Insurance Tax Credit Administration appropriations accounts remain unchanged. The Tax Administration and Operations appropriation is divided among eight critical program areas. These budget activities focus on Assistance, Outreach, Processing, Examination, Collection, Investigations, Regulatory Compliance, and Research. According to IRS, as it continues to move forward with developing and implementing this new structure, these program areas and the associated resource distributions will be refined to provide more accurate costing.

IRS reported that the new budget structure has a more direct relationship to its major program areas and strategic plan. We did not evaluate IRS's proposed budget structure as part of this engagement because it was not within the scope of our review. However, we have recently completed a study on the administration's broader budget restructuring effort. In that study we say that, going forward, infusing a performance perspective into budget decisions may only be achieved when the underlying information becomes more credible and used by all major decision makers. Thus, the Congress must be considered a partner. In due course, once the goals and underlying data become more compelling and used by the Congress, budget restructuring may become a better tool to advance budget and performance integration.[25]

[25] For a more detailed discussion, see GAO, Performance Budgeting: Efforts to Restructure Budgets to Better Align Resources with Performance, GAO–05–117SP (Washington, DC: February 2005).

Figure 5: IRS's Proposed Budget Structure



Source: GAO representation of IRS information.

APPENDIX II.—BSM PROJECT LIFE CYCLE COST/SCHEDULE VARIANCE AND BENEFITS SUMMARY

The table below shows the life-cycle variance in cost and schedule estimates for completed and ongoing Business Systems Modernization (BSM) projects, based on data contained in IRS's expenditure plans. These variances are based on a comparison of IRS's initial and revised (as of July 2004) cost and schedule estimates to complete initial operation[26] or full deployment[27] of the projects.

[26] Initial operation refers to the point at which a project is authorized to begin enterprise-wide deployment.
[27] Full deployment refers to the point at which enterprise-wide deployment has been completed and a project is transitioned to operations and support.

TABLE 4.—BSM PROJECT LIFE CYCLE COST/SCHEDULE VARIANCE AND BENEFITS SUMMARY

[Dollars in thousands]

Project	Cost Variance	Reported/Revised Estimated Cost	Schedule Variance (In Months)	Reported/Revised Estimated Completion Date	Reported IRS/Taxpayer Benefits
Completed projects:					
Security and Technology Infrastructure Release 1	+$8,450	$45,401	+5	1/31/02 (initial operation) [1]	Provides infrastructure for secure telephony and electronic interaction among IRS employees, tax practitioners, and taxpayers.
Customer Communications 2001	+$14,562	$60,762	+9	2/26/02 (full deployment)	Improves telecommunications infrastructure, including telephone call management, call routing, and customer self-service applications.
Customer Relationship Management Exam	−$721	$9,245	+3	9/30/02 (full deployment)	Provides commercial, off-the-shelf software to IRS revenue agents to allow them to accurately compute complex corporate transactions.
Human Resources Connect Release 1	+$200	$10,200	....	12/31/02 (initial operation) [1]	Allows IRS employees to access and manage their human resources information online.
Internet Refund/Fact of Filing	+$12,923	$26,432	+14	9/26/03 (full deployment)	Provides instant refund status information and instructions for resolving refund problems to taxpayers with Internet access.
Modernized e-File Release 1	+$21,057	$50,303	+6.5	5/31/04 (initial operation) [1]	Provides initial electronic filing capability for large corporations, small business, and tax-exempt organizations.
Ongoing projects:					
Modernized e-File Release 2	....	$16,325	....	9/30/04 (initial operation)	Provides additional functionality to support corporate electronic filing and other capabilities, including required public access to filed returns for tax-exempt organizations.
Modernized e-File Release 3	+$5,300	$27,175	....	3/31/05 (initial operation)	Provides additional functionality to support electronic filing for tax-exempt organizations and other capabilities, including the interface with state retrieval systems.
e-Services	+$102,271	$148,820	+18	4/30/05 (full deployment)	Provides a Web portal and other e-Services to promote the goal of conducting most IRS transactions with taxpayers and tax practitioners electronically.
Customer Account Data Engine—Individual Master File Release 1.	+$118,129	$182,774	+30	6/30/05 (full deployment)	Provides the modernized database foundation to replace the existing individual master file processing systems. Facilitates faster refund processing and more timely response to taxpayer inquiries for Form 1040EZ filers.

TABLE 4.—BSM PROJECT LIFE CYCLE COST/SCHEDULE VARIANCE AND BENEFITS SUMMARY—Continued

[Dollars in thousands]

Project	Cost Variance	Reported/Revised Estimated Cost	Schedule Variance (In Months)	Reported/Revised Estimated Completion Date	Reported IRS/Taxpayer Benefits
Integrated Financial System Release 1	+$73,710	$173,580	+15	6/30/05 (full deployment)	Provides a single general ledger for custodial and financial data and a platform to integrate core financial data with budget, performance, and cost-accounting data.
Custodial Accounting Project Release 1	+$91,789	$138,950	+33	11/01/05 (full deployment)	Provides integrated tax operations and internal management information to support evolving decision analytics, performance measurement, and management information needs.

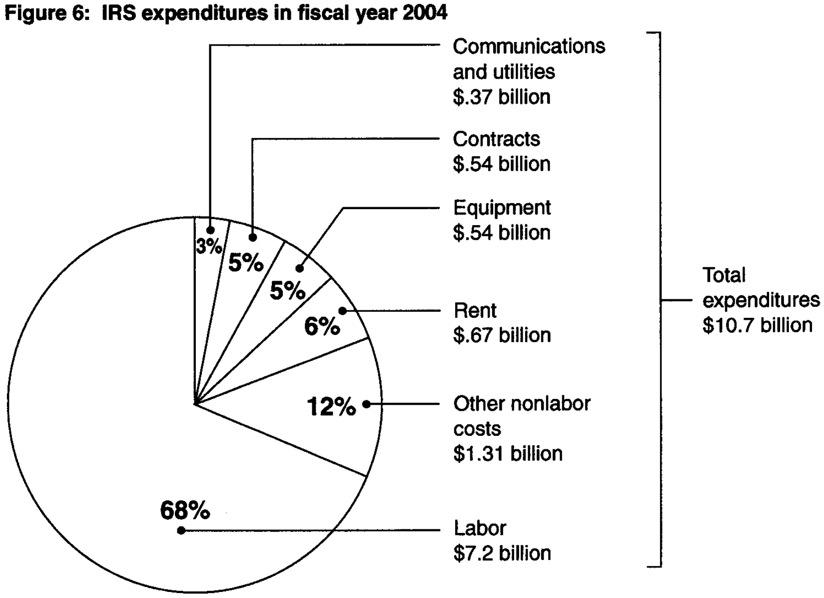
[1] Information on the costs and schedule for the full-deployment stage of these projects was not available in the BSM expenditure plans.

Source.—GAO analysis of IRS data.

APPENDIX III.—HOW IRS ALLOCATED EXPENDITURES FTES IN FISCAL YEAR 2004

Figures 6 and 7 illustrate how the Internal Revenue Service (IRS) allocated expenditures and full-time equivalents (FTEs) in fiscal year 2004. Figure 8 shows total expenditures. The percentage of expenditures devoted to contracts decreased from 9 percent in 2002 to 5 percent in 2004, because of fewer private contracts. The percentage of expenditures devoted to other non-labor costs increased from 8 percent in 2002 to 12 percent in 2004, according to IRS officials, due to of increases in miscellaneous costs.

Figure 6: IRS expenditures in fiscal year 2004

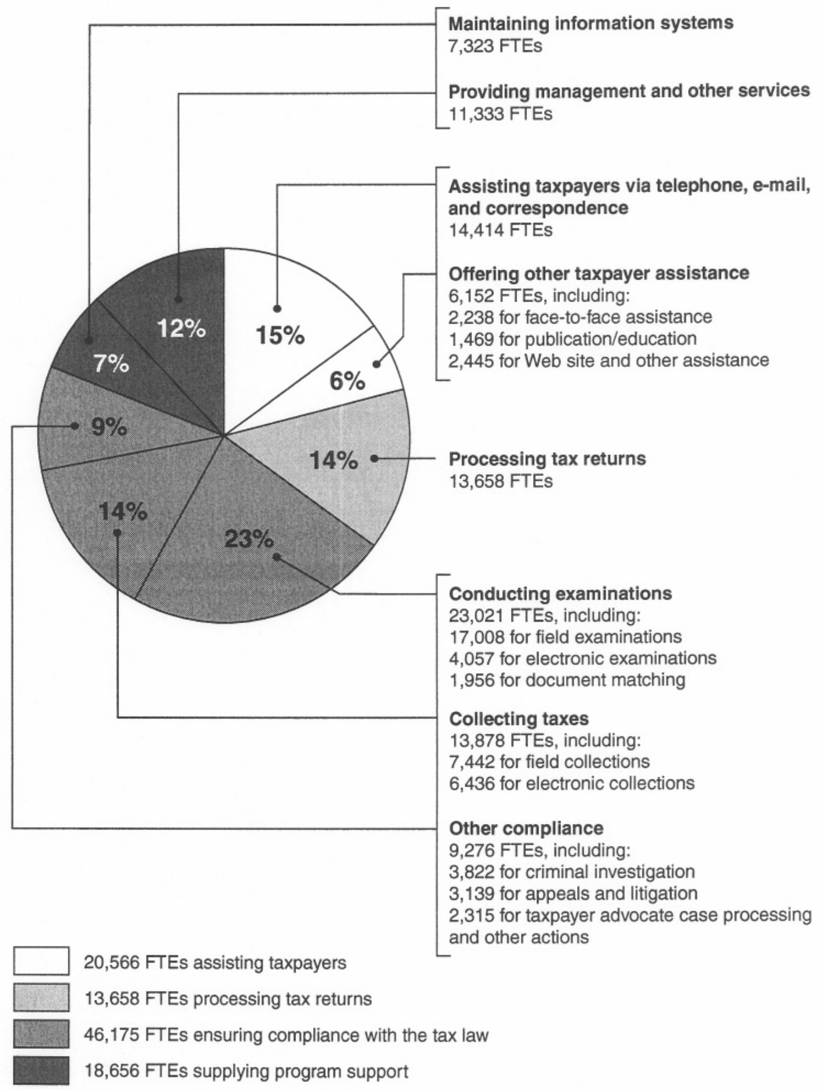


Source: GAO analysis of IRS data.

Note: Numbers do not add to the total and percentages do not add to 100 percent due to rounding.

Figure 7 shows IRS's total FTEs. Since 2002, FTEs have decreased slightly from 99,180 in 2002 to 99,055 in 2004. We previously reported that processing FTEs declined 1 percentage point between 2002 and 2003. Between 2003 and 2004, IRS's allocation of FTEs remained similar but with a 1 percent increase in enforcement activities in conducting examinations, and in management and other services.

Figure 7: How IRS spent 99,055 FTEs in fiscal year 2004



Source: GAO analysis of IRS data.

PREPARED STATEMENT OF NINA E. OLSON, NATIONAL TAXPAYER ADVOCATE

Mr. Chairman and distinguished members of the subcommittee, thank you for inviting me to submit a statement in connection with your hearing on the proposed budget of the Internal Revenue Service for fiscal year 2006.

The IRS is at a critical juncture in its history. In the 6+ years since the enactment of the Internal Revenue Service Restructuring and Reform Act of 1998, the IRS has successfully incorporated valuable customer service practices into its daily activities at all levels of the organization. It is now trying to increase its enforcement activity without eroding these taxpayer service gains. I strongly support a robust and research-driven IRS that undertakes well-designed examination and collection activities and criminal investigations. I believe that the IRS is capable of conducting these activities in an environment of superior taxpayer service. Given the size of the tax gap, I believe that the IRS needs additional resources to apply to both of these areas.

I also support increased funding for IRS Business Systems Modernization, providing the funds are spent wisely. Systems modernization is a critical component not only for the examination and collection aspects of IRS work but also for the taxpayer service component. Without sufficient funding, we are left continually apologizing to taxpayers because our systems aren't functioning; we create work for ourselves, fixing errors manually because systems create taxpayer problems rather than avoid them.

The role of taxpayer service in an environment of increasing enforcement activity is of great import to taxpayers, tax administrators, and Congress alike. I identified several areas of concern for taxpayer service in my 2004 Annual Report to Congress. Before I discuss some of these issues, I will comment generally about the balance between taxpayer service and enforcement.

THE COMPLIANCE EQUATION

In the IRS Strategic Plan for 2005–2009 and elsewhere, the IRS has emphasized that its guiding principle is "Service + Enforcement=Compliance." The proposed IRS budget for fiscal year 2006 would revamp existing budget categories to fit this guiding principle, placing 33 percent of the IRS budget into a "taxpayer service" account and 65 percent of the IRS budget into an "enforcement" account. (The remaining 2 percent of the proposed budget is allocated to Business Systems Modernization and Health Insurance Tax Credit Administration.)

At a conceptual level, the "Service + Enforcement=Compliance" principle is indisputably correct. Compliance represents the sum total of IRS's success in helping taxpayers file tax returns and pay tax, and IRS's success at enforcing the law when taxpayers fail to do what is required. What is less clear is the appropriate balance between service and enforcement, particularly in a resource-constrained budget environment. "Service + Enforcement=Compliance" does not in and of itself define a specific level of compliance. That is, each of the equation's elements is a variable. Thus, if we reduce service, there is no guarantee—no matter how much we increase our enforcement efforts—that compliance will increase overall. It is entirely possible that an increase in enforcement initiatives, offset by a decrease in taxpayer service, would result in less compliance.

How can that be? The answer is that our estimated 84 percent voluntary compliance rate is driven primarily by the fact that most income is subject to income and payroll tax withholding or to third-party income reporting. If we do not provide adequate taxpayer service to these taxpayers and their employers or payors—who are either compliant or trying to be compliant—then compliance by these taxpayers will decline. The IRS would then be forced to divert its enforcement resources, in part, to address this new source of noncompliance.

Last week, the IRS released a preliminary estimate of the tax gap based on the recent National Research Program study. This study estimates the net tax gap (i.e., the gross gap reduced by late payments and enforced payments) in the range of $257–$298 billion annually and a voluntary compliance rate of approximately 84 percent. That rate is generally consistent with the results of prior studies.

Today, there are approximately 130 million individual taxpayers. Each individual taxpayer is paying, on average, a "surtax" of at least $2,000 a year to subsidize noncompliance. That's the bad news. The "good" news, if you can call it that, is that notwithstanding claims that the decline in IRS enforcement activity in the aftermath of the IRS Restructuring and Reform Act of 1998 led to rampant cheating, the estimate of the compliance rate in the recent tax gap study is approximately the same as the compliance rate when the prior study was conducted in the late 1980's.

Even so, a principal function of the IRS is to collect all tax due, so the big question is what do we do now to increase the compliance rate? The proposed IRS budget reflects the view that enforcement activity should be increased while taxpayer service is reduced. Is that the right answer?

If I were developing a budget from scratch, I would argue that both enforcement and taxpayer service funding should be increased. The IRS is the accounts receivable department of the Federal Government, and it is clear to me that additional funding for both enforcement and taxpayer service—if spent wisely—would bring in significantly more dollars.

Given the budget realities, however, I am concerned that the IRS does not have better research to show where its dollars could be most effectively spent. Indeed, the one function I am certain requires more resources is the IRS research function. The IRS is able to track revenue collected as a direct result of its enforcement activities. While that is useful information, it is the indirect effects of IRS activities—on both the taxpayer service side and the enforcement side—that generate a far greater amount of revenue. Even if the IRS only audits about 1 percent of tax returns, for example, much larger numbers of taxpayers will choose to comply because of the possibility that they could be audited. Thus, a single audit has a "ripple" effect or, in economic terms, a "multiplier" effect.

Not all audits are created equal, however: $1 spent on auditing industries with historically high rates of noncompliance, such as the construction industry, may have a very different multiplier than an audit of a corporate tax shelter. Similarly, $1 spent on making it easier for taxpayers to comply with their tax obligations—e.g., publishing forms, advertising e-file, answering tax law questions—almost certainly has a multiplier effect as well. We simply don't have adequate research to show where the next dollar is best spent.

Moreover, in terms of improving overall tax compliance, we don't have data that show whether the "multiplier effect" is generally greater at this time for enforcement or for taxpayer service. Thus, a decision to increase enforcement and reduce taxpayer service is, to a large degree, based more on instinct than solid research. To be sure, this is not easy research to do, and in any event, it is a long-term project that will not assist in fiscal year 2006 budget decisions. But in the absence of better research, it is important to emphasize that the decision about how much to increase or decrease certain activities represents merely a policy call based on educated guessing.

If the proposed budget categories are enacted, we still face the challenge of allocating IRS costs among them. Many, if not most, IRS expenses cannot be unambiguously placed under either the "enforcement" or the "taxpayer service" umbrella. For example, the proposed budget lists the $1.3 billion cost of submission processing as a "taxpayer service." In reality, I view this cost more as a core business function. Processing tax returns provides service to the extent that it is necessary to enable the IRS to issue tax refunds. On the other hand, return processing is central to the IRS's ability to classify returns for audits and determine balances due on returns.

The proposed division of the budget into two categories has also triggered internal budget competition. Since the overall budget proposes to increase the enforcement category by 8 percent and reduce the taxpayer service category by 1 percent, operating divisions and functions clearly benefit from placing as much of their programming as possible into the enforcement category. Although final decisions have not been made, this budget approach seems to be leading to some questionable results.

For example, we have been told that more than 90 percent of the funding for the Office of Appeals and the Office of Chief Counsel will be allocated to enforcement. By contrast, we have been told that none of the funding for the Taxpayer Advocate Service (TAS) will be allocated to enforcement—indeed, that TAS will be the only function in the IRS allocated entirely to taxpayer service. Considering that 85 percent of TAS's funding is currently allocated to the Tax Law Enforcement (TLE) account and that fully two-thirds of TAS's cases are enforcement-related (i.e., cases where taxpayers seek help from TAS due to actual or perceived mistakes made by IRS examination or collection personnel), there is little principled basis for this difference in treatment. The practical effect of allocating TAS entirely to taxpayer service is that it increases the likelihood that the TAS budget will sustain significant cuts.

Among the many measures the IRS is considering to reduce taxpayer service costs, I discuss my concerns about two below.

ELECTRONIC TAX LAW ASSISTANCE (ETLA)

Electronic Tax Law Assistance (ETLA) is a service provided through a link on the official IRS website that allows taxpayers or practitioners to send tax law questions electronically to the IRS. The system is designed to allow employees to pull responses from the database of pre-written answers and thus save time researching and responding to frequently asked questions. As originally conceived, ETLA was the first stage in a multi-level approach to tax law assistance, using artificial intelligence technology to recognize and answer the easiest questions and reserving valuable IRS employees for the more complex questions. In a recent customer survey, over 90 percent of taxpayers using ETLA stated that they would use the service again.

We understand that the IRS is considering a proposal to discontinue providing tax law assistance over the Internet. I think this would be a mistake. The benefits of providing answers to taxpayer questions by Internet are significant. Most taxpayers now have Internet access, and many taxpayers prefer to write up their questions precisely and submit them electronically to avoid waiting on hold to speak with telephone assisters. In fact, in other areas of tax administration, the IRS is justifying the reduction of face-to-face service due to the availability of Internet applications. Although Internet-based assistance should not be the sole or even primary means of providing tax law assistance, ETLA is still very useful, and I understand the savings from eliminating it would be only about $1.5 million.

TAXPAYER ASSISTANCE CENTERS (TACS)

The IRS is planning to close a significant number of its approximately 400 walk-in sites (also called "Taxpayer Assistance Centers" or "TACs"). Here, the estimated savings are larger—approximately $50 million. To date, the IRS has not identified alternative means to assist taxpayers who require face-to-face assistance. This is unfortunate since taxpayers will continue to seek the assistance they require. The Taxpayer Advocate Service and other IRS offices co-located with TACs subject to closure are particularly likely to see an upsurge in taxpayer requests for assistance.

In a tax system with 130 million individual taxpayers, there is no one-size-fits-all solution to any problem. Some taxpayers strongly prefer—or, depending on personal limitations, may even require—face-to-face contacts, some need telephone contacts, and some prefer to interact with the IRS electronically. A significant study released last year by the Pew Internet and American Life Project examined how Americans communicate with the government. Generally, the study found that most Americans prefer to communicate with the government orally (either by phone or in person), rather than by letter or over the Internet. Notably, fully 20 percent of Americans reported that their most recent contact with the government was in person. In a few States, the IRS has experimented with using mobile vans to cover a greater number of areas. For example, the van might move weekly among five locations in a State. It could show up at a local library in a town every Monday, for example, and visit other cities on other days of the week. A mobile van would not be as convenient as having a fully staffed office that is open daily, but if the IRS is planning to close a significant number of offices, it should at a minimum consider whether an approach like this might allow the IRS to remain accessible at a much lower cost.

The IRS has developed a model incorporating many factors to help it determine which TACs to close. I applaud the serious effort that went into creating this model over a very short period of time—a matter of months. Built using demographic and other taxpayer data, the model provides an excellent first stage for an analysis of TAC closures. In my view, however, the IRS should supplement this model with a comprehensive survey of taxpayers' need for face-to-face service. The model's reliance on TAC usage over the last few years, as a proxy for taxpayer need, is inadequate since the IRS has reduced the services provided in TACs over that period due to resource concerns.

The speed with which the IRS is making decisions of such momentous import to taxpayer service, and the lack of stakeholder engagement, is of great concern to me. I was briefed on this model on March 22 of this year, too late to have any but the most trivial influence on its development. It is my understanding that the IRS consulted the Internal Revenue Service Advisory Committee (IRSAC) with respect to the weighting of factors used to determine closings. However, the IRS did not consult the Taxpayer Advocacy Panel (TAP), a Treasury panel of volunteer taxpayers specifically chartered under the Federal Advisory Committee Act to advise the IRS on matters pertaining to customer service. Nor did the IRS seek comments or suggestions from the Low Income Taxpayer Clinics funded by the IRS under IRC § 7526, which presumably represent the interests of a portion of the taxpayer population affected by these closings.

In light of the lack of any taxpayer-centric assessment of the need for face-to-face service, or any accurate measure of the impact of TAC closings on compliance, or any significant engagement with stakeholders, or any identification of alternative methods for providing face-to-face service, I believe that closing Taxpayer Assistance Centers at this time will irrevocably harm taxpayers.

CONCLUSION

The IRS faces significant challenges in the next few years as it attempts to increase taxpayer compliance. To achieve this goal, the IRS needs to do a better job of identifying and balancing both taxpayer needs and enforcement efforts. Rather than making resource-driven decisions that are based on inadequate research and that fail to identify equivalent alternatives, the IRS must develop a world-class research function that is the foundation for all of its customer service and enforcement activities. Research—and truly strategic planning—should inform the IRS's allocation of resources so that we achieve the maximum compliance possible by obtaining the optimal balance between service and enforcement.

ADDITIONAL COMMITTEE QUESTIONS

Senator BOND. As I've indicated earlier in my statement, it would help us a lot if we could get some funding credit in the badly out-of-date scoring systems for the money that comes in for the IRS activities that we fund. This would help Congress and the IRS to assist more taxpayers and, more importantly, bring in more revenue.

We will leave the record open until next week for my colleagues to submit questions. And we would appreciate your prompt attention to and response to these. And I thank our witnesses and those who've come to hear us.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

QUESTIONS SUBMITTED BY SENATOR PETE V. DOMENICI

CAPITAL GAINS TAX RATE FOR ART AND COLLECTIBLES AND FUEL TAX FRAUD

Question. Commissioner Everson, I am a long-time advocate of equitable treatment for all capital gains, and I plan to introduce a bill to correct the tax code's disparate treatment of various capital gains to ensure fairness for all types of investors.

My legislation would reduce the capital gains tax rate for sales of art and collectibles to 15 percent—the same rate of taxation for most capital gains relating to stock and bond sales. In addition to being fair to individuals who choose to invest in art or other collectibles, I believe that this legislation would raise revenue for the U.S. Treasury because lowering the capital gains rate would encourage people to buy and sell art and collectibles, which would increase the number of people paying tax on art and collectibles.

Would you anticipate an increase in art and collectibles sales if the capital gains tax rate were lowered for such sales?

Answer. Generally, a reduction in tax may result in an increase in affected sales. However, the Department of the Treasury has not prepared a revenue estimate that would chart the effects of this particular proposal.

Question. Will you provide me with the amount of revenue generated last year by the capital gains tax on the sale of stocks and bonds and the amount of revenue generated last year by the capital gains tax on the sale of art and collectibles?

Answer. For 2002, the most recent year for which tax data are available, total tax revenue on capital gains from stocks, bonds, and other assets subject to preferential capital gains rates was $49 billion. Separate data are not available for capital gains on sales of artworks and collectibles. This category is likely well below 1 percent of capital gains realizations and revenues, and too small to be measured meaningfully with existing sales of capital assets tax data samples.

Question. What was the administration's reasoning for lowering the capital gains tax rate for some investments, but keeping a higher tax rate for art and collectibles?

Answer. The Taxpayer Relief Act of 1997 generally reduced the maximum rate on adjusted net capital gain of an individual from 28 to 20 percent. Although both the House and Senate versions of the Act generally reduced the maximum capital gains tax rate for individuals, both versions maintained the then-current law maximum 28 percent rate for collectibles such as artwork, rugs, antiques, metals, gems, stamps or coins, and the conference report retained this rule for collectibles. The legislative history of the Act does not give a specific reason for this treatment. The Jobs and Growth Tax Relief Reconciliation Act of 2003 generally reduced the maximum rates on adjusted net capital gain of an individual from 10 and 20 percent to 5 and 15 percent. It did not modify the category of 28 percent rate gain including collectibles.

Question. Has the administration considered expanding the new, lower capital gains tax rate to apply to art and collectibles?

Answer. The administration's Budget does not include any proposed modifications to the taxation of sales or exchanges of collectibles. The President has appointed an Advisory Panel on Federal Tax Reform to consider fundamental changes throughout the tax Code. The Panel's report is due by July 31, 2005.

CAPITAL GAINS TAX RATE FOR ART AND COLLECTIBLES

Question. The legislation I mentioned would also correct the inequity afforded to artists who donate their work to charity. Under current law, if a collector donates a painting to a museum, he or she is entitled to a tax deduction equal to the fair market value of the artwork. However, if the artist who created the work were to donate the same painting, he or she is only entitled to a deduction for the paint, the canvas, and any other art supplies involved in creating the work.

This provision of the Tax Code creates a tremendous disincentive for artists to donate their work and negatively impacts museums, libraries, and schools, which depend on such donations to grow their collections. My legislation would remedy this unfairness by allowing artists to deduct the full market value of artwork they donate.

Would you expect more artists to donate their works to charity if they were subject to the same charitable contribution rules as art collectors?

Answer. Yes. We would anticipate a significant increase. The IRS anticipates a significant increase because the proposal would allow artists to claim a deduction for amounts that are not included in income. Current law does not allow a deduction for the value of donated services. This current-law rule generally produces the same tax results for individuals who assist charities by providing volunteer services as for individuals who make charitable contributions of cash.

Question. Can you tell me how many artists sought deductions for charitable contributions of their art work in 2004?

Answer. This information is not available.

FUEL TAX FRAUD

Question. Commissioner Everson, over the last several months we have been working very hard to identify ways of shoring up the highway trust fund without raising taxes. Recently a lot of attention has focused on the revenue lost to fuel tax fraud, and in this case, the ability of criminals to remove red dye from untaxed diesel fuel using straightforward techniques. I have heard from your office that the IRS is looking at various technologies to address this issue, but it is being held up because there is no field test. It certainly seems we could be simultaneously implementing more effective technology while exploring options for a more effective field test.

Why is a field test critical to the success of this program?

Answer. Each year U.S. consumers buy more then 61 billion gallons of diesel fuel and over 26 billion gallons of aviation grade kerosene. Both of these products can be and are used in highway vehicles. Currently, the IRS uses the red dye field test to monitor compliance with the payment of fuel excise taxes. When the IRS takes a sample of fuel from a motor vehicle, the results are immediate. If the sample does not show any traces of red dye, the IRS releases the vehicle and discards the sample. If the field sample shows traces of red dye, the IRS forwards the sample to its laboratory for a complete analysis, and the Fuel Compliance Officers (FCOs) gather information from the owner of the truck, which the IRS uses to assess a penalty for improper use of dyed fuel. Without such a field detection device, the IRS would have to randomly select fuel from millions of highway vehicles and tens of thousands of retail stations, and gather identifying information from them as well, in order to monitor compliance with the payment of fuel excise taxes. The IRS would have to analyze each sample at a laboratory and then would have to follow up with those individuals or businesses that failed the test.

The principal drawback to the current testing is the inability to determine immediately if the red dye has been removed from red dye diesel fuel. If this removal has been done effectively, there is no visible trace left to detect, and the fuel looks just the same as taxed fuel that has never been dyed. While the IRS agrees some type of invisible marker (such as the recently promoted molecular marker) would enable the IRS to detect dye removal, it would have to send all fuel samples to a lab for analysis to determine the presence of the marker in the fuel. Such an approach is not operationally or economically feasible. Hence, the IRS needs some type of field device by which IRS FCOs can readily detect the existence of a marker. To date, the IRS has not been shown a practical field device.

Question. It certainly appears that the Red Dye has failed as a field test, so why are we allowing perfect to be the enemy of the good and losing hundreds of millions of dollars by not implementing another method to detect fraudulent fuel?

Answer. The IRS does not believe that the red dye field test regime has been a failure. In the vast majority of cases, the red dye provisions have been successful in keeping non-taxable fuel off the highways. Upon its initial implementation, the red dye regime yielded significant tax increases and continues to be an effective deterrent today. It is only recently that the IRS has begun to see products that appear to have had the red dye removed. The extent of the removals is unknown, but the IRS does not believe that it is widespread. The IRS is not aware, nor has it stated, that it is losing hundreds of millions of dollars due to the removal of the red dye. As requested in the Appropriations bill, the IRS is continuing to look at the possibility of using the molecular marking regime and has discussed the potential usage with the American Petroleum Institute (API). They have raised significant issues regarding the blending, product quality, company indemnification and reliability of the sampling. The IRS is continuing to work with the promoter of the field screening device to reach an acceptable field performance level.

Questions Submitted by Senator Patty Murray

PRIVATE COLLECTION AGENCIES

Question. In January of 2005, the IRS briefed my staff on the schedule for implementing private debt collection over the next few years, including the number of agencies involved, and how much the IRS plans to spend in fiscal year 2005 and successive years. Please provide a detailed update of this information.

Answer. The IRS has made significant progress toward the initial implementation of the private debt collection initiative. Since the briefing in January 2005, the IRS has developed a release schedule that will provide for limited implementation in January 2006. The IRS will develop additional systemic functionality for January 2007. Full implementation of the private debt collection program is scheduled for January 2008 with enhanced reporting, monitoring and control capabilities. This schedule will allow for a controlled ramp-up of additional volumes of delinquent account placements with private collection agencies.

In March 2005, the IRS selected a software vendor to provide inventory management support of the private debt collection accounts. The vendor is a proven leader in collection inventory management applications with over 19 State deployments of their software. The inventory management vendor is on board and has been working with IRS staff to ensure successful deployment of the supporting software applications in time for placement of delinquent accounts with private collection agencies.

The IRS has prepared the statement of work to secure the services of private collection agencies, and the contracting officer provided it to potential vendors on April 27, 2005. The IRS expects to award contracts in July 2005 with initial account placements in late January 2006. The IRS has identified the initial workload for placement with private collection agencies and anticipates placing approximately 40,000 accounts within the first 9 months of operation.

The IRS has developed support structures and roles and responsibilities. The IRS has identified operational sites and is making progress on securing facilities. The IRS has identified a number of key policy concerns and successfully worked them to resolution. The IRS is drafting internal and external policies and procedures, with anticipated completion scheduled for late summer.

The IRS has developed and approved a project schedule for the limited implementation. The IRS has also developed a project budget and secured funding for the current fiscal year. Additional funding is included in the BSM spend plan requests for fiscal year 2006. The IRS has established a project governance structure and its members meet regularly with the project leadership to review progress against scheduled activities and to provide guidance to the team. With the current strong leadership in place, the IRS anticipates a successful implementation of the private debt collection efforts.

The current information technology projected costs and budget for fiscal year 2005 totals $15.5 million. This funding amount reflects the full costs of the "limited implementation" for January 2006 of $9.5 million and an additional $6 million to begin the activities that support the January 2007 implementation.

BUSINESS SYSTEMS MODERNIZATION

Question. Once finalized, the Custodial Accounting Project is supposed to be a single, integrated data repository of taxpayer account information and accessible for management analysis and reporting. However, costs for the Custodial Accounting Project have continued to increase, with the cost for the first phase in the neighborhood of $98 million. But this project is now on hold and may never go forward. What is the latest on this project's cost and do you expect it to ever come to fruition?

Answer. The BSM office designed CAP to provide integrated, reliable tax operations and internal management information to support decision analytics, performance measurement, and management information needs. CAP also provided a data warehouse loaded with detailed taxpayer account and collections information to be used for analysis and financial reporting to oversight organizations. The IRS conceived CAP as a multi-release solution, and BSM delivered the first two releases into production in September 2004 and November 2004. However, for CAP to have sustainable value to the IRS, it required two additional releases—for business master file taxpayers and for collections data. Collectively, these releases would take at least 3 years to complete and cost more than $100 million. In addition, maintenance and support for fielded CAP releases will cost more than $10 million annually. Within the current budget context, the IRS evaluated benefits and costs of continued CAP investment against the value to taxpayers and IRS employees, competing priorities such as CADE, MeF, F&PC, and maintaining core infrastructure. The IRS determined in January 2005 continued CAP investment is no longer a viable or sound business decision; however, the IRS will leverage CAP work products and knowledge gained in other BSM initiatives (e.g., BSM will use CAP data models on CADE; the IRS now performs data segmentation and analysis in a more modernized way, etc.). The CFO's office is pursuing a current production environment (CPE) upgrade alternative that meets their needs. There are no plans to revive CAP at this time.

Question. The contractor for Business Systems Modernization developed a system for the IRS known as the Security Audit and Analysis System to gather information for use in audits. Specifically, the system would enable users to detect unauthorized activities and facilitate the reconstruction of events if unauthorized activities occurred. However, problems have prevented users from accessing the data once it has been collected. When the contractor delivered the system to the IRS in 2002, the IRS was aware that the system did not meet IRS requirements but accepted the system with the understanding that it would be fixed. Have these problems with the system been resolved?

Answer. Since the initial delivery of the system in 2002, the IRS has successfully resolved several requirements issues and is pleased the Security Audit and Analysis System (SAAS) is effectively managing audit trail data for modernization systems. Security Managers and Modernization System Managers can generate Modernization Managers Security Reports (MMSR) of employee access to taxpayer data from the SAAS system. The Treasury Inspector General for Tax Administration (TIGTA) should be able to begin their pilot use of SAAS in the summer 2005. The use of the SAAS reports by TIGTA is delayed until they complete the testing of the current system audit trails. Final data updates for this capability are underway and the TIGTA should complete testing in the summer 2005. Activities continue to plan the transition of current production systems audit trail analysis capabilities to the SAAS system for TIGTA use. Mission Assurance and Security Services, TIGTA, Modernization, Information Technology Services (ITS) and the PRIME Contractor are working together to define and prioritize the implementation of additional requirements and enhancements to the SAAS system, which will be implemented in 2005 and 2006.

When IRS fully deploys SAAS, it will process two sources of "audit trail" data. One source is audit trails for modernized systems (e.g. IFS, Modernized E-file, E-services, IRFOF, etc.) and another is audit trail historic data from the legacy Integrated Data Retrieval System (IDRS) and Corporate Files on Line (CFOL) production systems. A current production system called ATLAS, which continues to function while the IRS transitions its capabilities to SAAS, currently captures this legacy system audit trail data and processes it. The TIGTA will continue to utilize ATLAS to review potential Unauthorized Access (UNAX) violations until the IRS fully tests the SAAS system in a production environment using production data. The IRS moved the ATLAS data to SAAS to provide more modern technology support to the TIGTA users, provide a single system for TIGTA to access their data instead of their accessing both ATLAS and SAAS, and to allow the retirement of the ATLAS system. The IRS previously processed and loaded the ATLAS data into a data mart containing 60 months of historic data, but the IRS is currently updating it to contain data from the last 4 months of 2004 audit trail information into SAAS, and then it will load the IDRS/CFOL data from 2005.

Once the IRS loads the remaining 2004 historic IDRS data into SAAS, the IRS needs to complete testing of multi-year report functionality. At that point, TIGTA will begin to conduct a formal customer acceptance test in the SAAS Production system. After the TIGTA completes the customer acceptance test results, the IRS will make any necessary systems changes and TIGTA will begin a 3-month parallel test of both ATLAS and SAAS in Production prior to making any decisions about retiring the current CPE system. TIGTA may determine that a second 3-month parallel test of both ATLAS and SAAS is required based on the results of the CAT testing and the initial parallel test. The current completion dates are in the SAAS Production schedule (05/31/2005 schedule) as follows:

—*Final Data Checkout on the loading of the 60 months of historic data into the SAAS DataMart*.—7/19/05;

—*Complete initial TIGTA CAT in Production*.—8/22/05.

The IRS is still working with TIGTA to reach agreement on a plan and schedule for conducting the parallel test between SAAS and ATLAS in Production. The IRS based the current schedule, which calls for this test to begin in November 2006, upon the current estimates for loading all historical audit trail data for 2005 into the SAAS data mart. Delays in loading the most current 60 months of historic audit trail data into the SAAS Production system have caused schedule delays, and the IRS is looking at options (e.g., performance enhancements, capacity upgrades) that may accelerate the current schedule estimates. The current projected completion dates in the SAAS Production schedule as of 05/31/2005 are:

—*Final Datamart load of the 2005 data*.—9/12/06;

—*Execute 3 month parallel ATLAS/SAAS Production testing*.—12/08/06;

—*Execute 2nd 3 month parallel testing*.—3/31/07—dependent on TIGTA's satisfaction following the first 3 months parallel testing;

—*Retire ATLAS*.—3/31/07 following 6-month ATLAS/SAAS parallel testing.

TELEFILE—FILING TAX RETURNS BY TELEPHONE

Question. The IRS is reducing submissions processing activities because taxpayers are filing fewer paper returns. In 2004, almost 4 million taxpayers filed by telephone—57 percent of whom had income of $20,000 or less and 97 percent had income of $50,000 or less. Additionally, nearly 1 million businesses used the TeleFile technology to file their employment tax forms. The IRS's own survey reveals that nearly 40 percent of the individual TeleFilers will go back to paper filing. Further, there is currently no electronic alternative for the businesses that use TeleFile. Nonetheless, the IRS is proposing to eliminate TeleFile because the IRS says use has declined somewhat and it is a bit more expensive to maintain than paper or electronic filing. Why was the decision made to eliminate TeleFile without first providing a viable, easy-to-access means of filing for these individuals and businesses that ensured an electronic filing rather than forcing them back to paper filing? Did the IRS look at ways to achieve efficiencies in the operation of the current TeleFile system? If so, what were they? Were these pursued?

Answer. The TeleFile program has certain requirements, such as telecom, printing and postage cost that cannot be restructured or reduced; therefore, the IRS could not develop efficiencies within the current TeleFile program.

In making the decision to sunset TeleFile, the IRS considered the declining use of TeleFile, the discontinuation of several State TeleFile programs, including California's decision to cease TeleFile in 2005, and the growth of other electronic filing alternatives, such as Free File. In fact, Free File volumes grew from 3.5 million returns in 2004 to 5.0 million returns in 2005, a 46.6 percent increase. At least 60 percent of individual filers qualify for Free File services and all TeleFile-eligible filers with access to the Internet can use Free File. Additionally, in their decision, the IRS considered the June 2004 Electronic Tax Administration Advisory Commission (ETAAC) report recommendation to discontinue TeleFile. By sunsetting TeleFile, the IRS will eliminate growing information systems operational costs of $3 million–$5 million annually and printing and postage costs of $4 million–$5 million annually.

The IRS has not developed a similar alternative for employment tax returns. The same cost and infrastructure issues that the IRS faced with Forms 1040 still persist. However, there are low cost alternatives currently available to electronically file the Form 941.

TeleFilers may initially revert to paper filing (37 percent according to a customer satisfaction survey), but research shows they rebound to electronic filing at a higher rate than the general population. Sixty-two percent of TeleFilers said they would try another e-file option if TeleFile was no longer available.

TAXPAYER SERVICES

Question. The IRS is reducing its face-to-face service providing taxpayers with information and filing assistance. Instead, the IRS wants to direct taxpayers to the

IRS website and to volunteer tax return preparers. In particular, the IRS plans to decrease the level of pre-filing services offered by Taxpayer Assistance Centers. The problem with this is that some taxpayers rely on the face-to-face service. The IRS notes, in its Strategic Plan, that it must "continue to use a comprehensive range of products and services to reach [their] customers, including those who do not use electronic services." Mr. Everson, how does the IRS's plan to reduce face-to-face services adequately provide for these taxpayers who won't use electronic services?

Answer. In recent years, the IRS has seen a significant shift in the ways Americans interact with the Service. Compared to the past, fewer taxpayers are choosing to write or call the IRS; even fewer taxpayers are using walk-in TACs. Instead, more and more Americans are turning to volunteers for return preparation and they are obtaining forms and tax information from the IRS's Internet site. In addition, most TAC services are available through the IRS's Toll-Free telephone system at a greatly reduced cost and with higher quality. In a report issued last year, the Government Accountability Office (GAO) stated, "improvement in phone service, increased web site use and the availability of volunteer sites raises a question about whether the IRS should continue to operate as many walk-in sites."

In making the business decision regarding the TACs, the IRS considered the long-standing concept of operations for Field Assistance that emphasizes accounts and collection work, with customers who need assistance increasingly served through self-service mechanisms, and reliance on community-based volunteer partners for return preparation assistance. The IRS anticipated that as these partnerships grew and increasingly met the needs of community members, the customer traffic in IRS TACs would be reduced. In making this decision, the IRS also considered changing taxpayer behavior, the availability of new and improved alternative services, and the cost benefits of these alternatives compared to walk-in service.

When taxpayers have tax law questions or questions about their accounts, the IRS's Toll-Free service will route them to the assistor who has the expertise to answer their particular question. If a taxpayer needs a form, the IRS website has every form available for download, and paper forms are available at 32,000 local libraries, banks, post offices and other outlets. When taxpayers need help preparing their returns, they can visit one of the 14,000 VITA and TCE sites available throughout the country. If a taxpayer still needs face-to-face service with an IRS representative, more than 300 TACs will still be available across the country to provide that service as well.

ACCURACY OF TAX INFORMATION

Question. Mr. Everson, if you succeed in reducing the number of Taxpayer Assistance Centers, it will become even more important that the remaining avenues available to taxpayers seeking information be accurate. Recently, the Treasury Inspector General for Tax Administration (TIGTA) found that taxpayers have alerted the IRS of possible errors on the IRS.gov website but these concerns were not always addressed. TIGTA also found that the IRS could not verify whether correct changes had been made to the website. Mr. Everson, if compliance is an utmost priority to the IRS, how can you expect taxpayers to comply if the information they receive from the IRS isn't accurate or reliable?

Answer. After the Treasury Inspector General for Tax Administration (TIGTA) review on the accuracy of IRS.gov, the IRS implemented several controls to ensure taxpayer concerns regarding the web site are directed to the appropriate IRS.gov Point of Contact (POC). The IRS also issued more specific procedures to the IRS.gov Helpdesk vendor regarding the handling of IRS.gov inquiries (comments, questions and problems) from web users, to ensure the vendor is forwarding those inquiries for resolution. Inquiries from web users regarding the accuracy of the web site or inquiries that indicate that information on the web site is different from other web documents are immediately forwarded to the IRS.gov POCs for resolution.

The IRS has also added a staff member dedicated to monitoring the resolution of inquiries forwarded to the IRS.gov POCs to ensure that these inquiries are addressed. The IRS has also implemented the use of Unresolved Escalation Reports to follow-up on unresolved inquires with the Content Area Administrators and, when necessary, management. If IRS.gov POCs do not respond to inquiries within designated timeframes, a follow-up is scheduled to ensure issues are resolved.

In addition, the IRS has updated its procedural document "Guidelines for Responding to IRS.gov Escalations" to provide specific responsibilities for IRS.gov POCs. On January 11, 2005, the IRS held a meeting with the IRS Content Area Administrators and explained the changes in procedures. Since January 2005, the new procedures have been effectively implemented.

PROPOSED CUTS TO TAXPAYER OUTREACH

Question. Funding for taxpayer outreach has steadily decreased in the past few years. Outreach activities include proactive programs for taxpayers, businesses, tax practitioners, and others to understand their tax obligations and have the information and materials necessary to do so. For fiscal year 2006, a 7 percent cut is proposed, which is almost the same as the increase proposed for enforcement. Doesn't cutting outreach directly conflict with your Strategic Plan to improve taxpayer service by making it easier for people to participate in the tax system? Have you been able to identify a decline in the need for outreach? Do you have data—has a study been completed to demonstrate this? If yes, please provide a copy. If there has been no decline in the need for outreach, how are you going to meet this need, if you are cutting outreach?

Answer. The change in the level of resources requested for the Outreach activity in fiscal year 2006 reflects the IRS's commitment to providing high-quality services to taxpayers in the most efficient and effective manner possible. However, the reduction in Outreach is not comparable to the increase in Enforcement resources. Outreach is a single budget activity with a relatively small budget, while the term "Enforcement" encompasses five budget activities with a substantially larger budget. A more appropriate comparison would be between the reduction in "Taxpayer Service" resources—encompassing several budget activities—and the increase in "Enforcement" resources. As proposed for fiscal year 2006, "Taxpayer Service" resources decline by 1 percent, while "Enforcement" resources reflect a 7.8 percent increase.

The IRS must provide strong customer service to taxpayers, but the way taxpayers pay their taxes and access IRS information is changing. In recent years, the use of IRS.gov and e-filing has increased rapidly while paper filing and visits to walk-in Taxpayer Assistance Centers (TACs) have declined. In fact, this filing season individuals filed more returns electronically than on paper, marking the first time in history that e-filing has outpaced paper returns. The closure of TAC sites and corresponding reduction in Outreach resources has been carefully evaluated to minimize the impact on taxpayers while simultaneously making additional resources available for other essential functions.

The number of taxpayers walking into a Taxpayer Assistance Center (TAC) for assistance has decreased from a high of nearly 10 million contacts in fiscal year 2000 to about 7.7 million contacts in fiscal year 2004. To date this filing season, traffic is down again by over 9 percent. This trend reflects the increased availability and quality of services that do not require travel or waiting in line. Examples include improved access to IRS telephone service, the increasing availability of volunteer assistance, and the many services now available through IRS.gov, such as access to all forms and publications, "Free File," and "Where's My Refund?"

These shifts present an opportunity to adjust the way the IRS serves taxpayers and to focus on the most efficient services. Changing the way the IRS provides customer service to meet the new ways people are dealing with their taxes in the 21st century allows the IRS to meet the needs of taxpayers while spending their tax dollars more efficiently and responsibly.

With respect to quality, Toll-Free telephone service is the best option for most customers to get a correct and complete answer to their tax law or account questions. Unlike the walk-in environment, the sophisticated capabilities of our Joint Operations Center allow Toll-Free customers to be routed to an IRS employee specifically trained to address their particular issues. This filing season, Toll-Free tax law and account accuracy are at 88 percent and 91.5 percent respectively. Treasury Inspector General for Tax Administration (TIGTA) audits assessed the walk-in level of tax law accuracy at 75 percent for the same time period; however, the IRS notes the TIGTA does not base its results on a statistically valid sample. The IRS is developing a new Field Assistance Embedded Quality Review System (EQRS) to determine the true accuracy rate, but it is still too early in development to yield measures of which the IRS is confident.

The Wage and Investment Division Stakeholder Partnerships, Education and Communication (SPEC) business model focuses upon the delivery of education and tax preparation services solely through community-based partners such as non-profit, social services, educational, financial, governmental, faith-based, and corporate organizations. Since inception in 2001, this collaborative partnership has increased the volume of volunteer tax return preparation from 1.1 million returns to over 2 million returns in 2005.

The IRS also believes it can streamline certain other outreach programs while meeting or exceeding the service expectations. In particular, the ongoing effort to realign and refocus communications, outreach, and liaison efforts within the Small Business/Self-Employed (SB/SE) Division will enable the IRS to enhance the level of service and the quality of its interactions with small business taxpayers in support of its strategic plan. The core mission of this merged organization will focus efforts in three areas—practitioner liaison; stakeholder engagement; and, support of strategic compliance initiatives—and will result in the following benefits for small businesses and practitioners:

—Centralized organization and delivery of key messages to ensure national stakeholders and partners in tax administration at the local level receive consistent, accurate and up-to-date information.
—Targeted communications with practitioner groups to provide consistent information on changes to the IRS's policies and procedures and keep our stakeholders apprised of the many services we offer—such as E-services for those who file electronically on behalf of their clients.
—An enhanced Issue Resolution program to encourage and address the feedback received from small business and practitioner stakeholders and enable the IRS to continually make improvements in examination, collection, and campus operations that benefit small businesses and practitioners.
—Continued educational outreach to meet the needs of small businesses through comprehensive curriculum, which the IRS updates for all tax code changes. The website, which is dedicated to small businesses, contains about 10,000 pages of content arranged by major industry groups and by major tax areas, such as employment taxes and depreciation. Response to this site has been overwhelming. For example, in January 2005, the site had 1.7 million visitors—more than double the number from January 2004.

Finally, the IRS believes it can achieve greater efficiencies in distributing tax products by leveraging on the continuing growth in e-filing and taxpayers' increased use of Internet. For example, consolidating the IRS's forms distribution operations from three sites to one site not only will be more efficient, but also will save staff, printing and postage resources. Other savings will accrue as increased e-filing results in the need to mail fewer tax packages, and Internet downloads allow the IRS to reduce excess quantities of tax forms, publications and other tax products.

Question. Congress created the Taxpayer Advocate so that taxpayers could receive assistance in solving their problems with the IRS. However, taxpayers aren't able to take advantage of this service if they don't know about it. Research indicates that only a small percentage of taxpayers eligible for Taxpayer Advocate Services have ever even heard of the Taxpayer Advocate. To what degree will the cuts you are proposing affect the Taxpayer Advocate? Won't these cuts further erode the public's awareness of the Taxpayer Advocate?

Answer. The IRS will continue to make taxpayers aware the Taxpayer Advocate Service is available to help them solve their problems with the IRS. The proposed changes to taxpayer service—reduced outreach spending and fewer Taxpayer Assistance Centers—may minimally reduce taxpayer awareness of the availability of the Taxpayer Advocate Service (TAS). However, outreach activities that publicize TAS should continue. The reduced outreach spending will be possible due to savings in printing and postage caused by shifts to electronic filing and by providing publications on-line, rather than through the mail. Reduced IRS face-to-face assistance may increase the TAS workload as taxpayers seek such service from TAS, especially in cases where TAS is collocated with a TAC that's been closed. However, the IRS expects these impacts to be minimal because of the overall trend toward alternate forms of assistance via the Internet and the telephone. Further, VITA assistance and SPEC and TEC outreach programs will supplement IRS reductions to face-to-face service and will maintain significant support for the awareness of TAS's services.

QUESTION SUBMITTED BY SENATOR HARRY REID

Question. The National Research Program (NRP) estimates that underreporting of tax attributable to individual income tax filers is the largest component of the tax gap. The shortfall of taxes paid to taxes owed has been estimated by the IRS at being in the range of $200 billion–$235 billion annually. Of this amount, the Service estimates that as much as $9 billion of this underpayment relates to errors in calculating taxable gains on the sale of equity assets. I understand that the NRP program used, on a limited basis, a computer program to help derive this underpayment estimate. Would an expansion of the use of this program assist the Service in reducing the underpayment of tax in this area?

Answer. The National Research Program (NRP) analyzed about 46,000 individual income tax returns for Tax Year 2001 and the Office of Research used the data collected in its update of the Tax Gap figures released in late March. NRP examiners and classifiers tested computer-based tools to determine if the calculated amount of capital gains reported by the taxpayer could easily be checked. The test was inconclusive, with some examiners and classifiers saying the tool was somewhat useful and others saying it was not helpful. In large part these results reflect the fact that taxpayers do not always list the exact purchase date for assets (such as shares of stock) they sell in a particular tax year. Often, the acquisition date is given as "various," reflecting purchases of more than one block of shares or the ongoing acquisition of shares through dividend reinvestment. Moreover, even where there is a specific acquisition date, the share price may fluctuate on that day by 10 percent or more, and it is unclear whether the taxpayer purchased the shares at the top of the range, at the bottom, or somewhere in between. Given the current level of information reporting for capital gains transactions (e.g., only gross sales proceeds are reported by brokerage firms, not the basis of the publicly-traded assets that were sold), it is not clear that the benefits generated by using a computer-based tool to help calculate basis of capital assets would exceed the costs.

Senator BOND. The hearing is recessed.

[Whereupon, at 10:50 a.m., Thursday, April 7, the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

THURSDAY, APRIL 14, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:30 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Stevens, Murray, and Leahy.

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

STATEMENT OF ALPHONSO JACKSON, SECRETARY

ACCOMPANIED BY:

KENNETH M. DONOHUE, INSPECTOR GENERAL

JOHN C. WEICHER, ASSISTANT SECRETARY FOR HOUSING

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD, and Related Agencies will come to order.

We welcome Secretary Alphonso Jackson for appearing before us today to testify on the Department of Housing and Urban Development's fiscal year 2006 budget request.

Last year, we did not have the benefit of a complete statement from you, having been newly confirmed as Secretary the night before the hearing. This year, I look forward to your comments after a year on the job.

I think I may have cautioned you about taking the job, but you do it so well, and we appreciate very much your expertise and commitment to the program.

The budget request proposes some $28.5 billion, a decrease of some $3.38 billion or almost 11 percent from the 2005 funding level of $31.9 billion.

Unfortunately, the overall 2006 funding level does not accurately reflect the requested overall spending for HUD's many programs. The budget numbers are distorted through a budget rescission request of $2.5 billion as well as by how FHA receipts are treated for purposes of the 2006 budget. In fact, the overall funding for HUD programs is far worse than OMB has indicated.

Proposed reductions to individual HUD programs include, among others, some $4.67 billion from CDBG funding, $118 million from Housing for Persons with Disabilities, $14 million from Housing for Persons with AIDS, $24 million from Rural Housing and Economic Development, $24 million from Brownfields, almost $286 million from HOPE VI, $226 million from Section 8 Project-Based Assistance, and $252 million from the Public Housing Capital Fund.

In addition, the Lead Hazard Reduction Program that Senator Mikulski and I started has been totally eliminated. This program is one of the most important things we can do to stop the lead poisoning of our children in low-income housing in many major cities.

PROPOSED RESCISSIONS

I also am especially troubled by a proposed $2.5 billion rescission for which neither HUD nor OMB has been able to or willing to identify the source of funding. I sincerely doubt there is adequate money to rescind from HUD programs without jeopardizing their mission.

These program cuts are even more disturbing because of reductions and shortfalls in other programs within the jurisdiction of the subcommittee.

Mr. Secretary, I know you have an obligation to defend the administration's budget and policy decisions no matter how problematic. I also understand and support the need for the administration to make difficult funding decisions in order to contain and reduce the Federal budget deficit.

Unfortunately, I believe that the President has been getting some very bad advice from OMB about the housing and community development needs of the Nation. The HUD budget as well as a number of other proposed legislative and policy initiatives reflect this bad advice.

Unfortunately, these problems go beyond HUD, leaving the subcommittee to confront huge challenges in trying to balance funding decisions among the many programs and priorities within the entire THUD fiscal year 2006 Appropriations Bill.

As always, HUD represents one of our largest challenges. Unfortunately, the administration's overall budget for domestic discretionary spending will make reversing many of these recommendations impossible or compel Congress to eliminate funding from other important and necessary programs.

There is a little bit of good news, Mr. Secretary. I applaud you for fighting the good fight in attempting to preserve Section 8 tenant-based vouchers at a level that will sustain current voucher use. And while I am disappointed over public housing capital and operating funding levels, I know you also staved off much larger reductions as proposed by OMB. In addition, home ownership is at its highest level in history with some 73.7 million homeowners.

PREDATORY LENDING

I also applaud your efforts to stem the abuses of predatory lending, something that this subcommittee, with Senator Mikulski leading, has been championing by banning flipping, by increasing home ownership counseling, and by putting in place more stringent appraisal requirements. Unfortunately, this is the good news, but the list is too short for an agency as important as HUD.

SACI

For the bad news, I am very disappointed that the administration has proposed to dismantle the CDBG program along with some 17 or more other programs and replace these programs with a new block grant in the Department of Commerce called Strengthening America's Community Initiative.

The administration also is proposing to fund this initiative at $3.7 billion, which is an overall reduction of almost $2 billion or 34 percent from the 2005 level for all these programs. The proposed elimination of CDBG is a tragedy, but the reduction in funding makes this proposal a double tragedy.

Communities across the Nation rely on CDBG to fund critical housing and community development programs. This program works. However, without these funds, many local programs will falter and even fail. Equally important, CDBG is a critical component of HUD's mission. CDBG helps to make HUD's housing mission successful. Without CDBG, it is the Department of Housing. And with all of the changes proposed, HUD would just be about home ownership and a few rental housing block grants. HUD would no longer merit cabinet status.

Moreover, the use of CDBG consolidated plans helps to ensure that communities tie together CDBG, housing funds, and other Federal and State resources into a comprehensive approval to local housing and community authorities. As history tell us, successful community development programs rely on a comprehensive approach to housing and community development. Without CDBG, HUD is like a one-armed pitcher trying to field a bunt.

I know CDBG has problems. CDBG funds are not always used well or effectively. Even Kansas City, Missouri, with a vibrant and progressive nonprofit community, recently identified significant abuses within the CDBG program. However, these problems are being addressed and resolved. The key is to fix the problems in good programs, not dismantle the programs.

Moreover, HUD, OMB, and certain interested parties recently ratified a consensus document to address weaknesses in the CDBG program by creating an Outcome Measurement System to establish new benchmarks and better oversight. Since the document addresses many of OMB's concerns, I am puzzled by the administration's effort to dismantle a program that has been redesigned to become more effective according to administration requirements.

HOPE VI

I am also very much concerned about the administration's approach to public housing. The administration is seeking to eliminate HOPE VI as well as rescind the HOPE VI fiscal year 2005 funding of $143 million.

As an alternative, the administration has issued a proposed regulation that will authorize PHAs to demolish the remaining obsolete public housing.

As you may know, I set the stage for HOPE VI by including a demonstration project in the 1990 National Affordable Housing Act that allowed the demolition and replacement of the Pruitt-Igoe public housing in St. Louis with vouchers and new housing.

Before this demonstration, PHAs could not be demolished without a one-for-one hard unit replacement. Because of the cost of this policy, public housing programs were limited to the warehousing of the poor in obsolete and deteriorating PHA high-rises.

HOPE VI provided for the demolition of this obsolete housing along with the creation of mixed-income, private and public housing. This program also leveraged private investment and promoted the revitalization of entire communities.

While HOPE VI is not a perfect solution to all the woes of obsolete public housing, it has transformed many PHAs and communities, including many in Missouri, which is now, I believe, a shining example of how it can work, by replacing obsolete public housing with mixed-income, public and private housing. In many cases, HOPE VI housing has leveraged new investment in communities. This means new business, an increased tax base, better schools, and safer communities. It is unfortunate that the budget rules do not recognize these very tangible economic and social benefits. However, I think you and I know from personal experience that these benefits are real and significant.

NEGOTIATED RULE-MAKING

The administration has also broken a promise to develop a new operating fund formula by negotiated rule-making. Over the last 5 or more years, HUD has worked with PHAs through negotiated rule-making to develop a new budget-based operating plan formula to ensure a more equitable system of allocating operating subsidies to PHAs. Millions of dollars have been spent on the process. Nevertheless, a negotiated rule went into OMB's rule-making review process and came out a much different flavor of sausage.

One expects OMB to make modest changes to a regulation under review but one does not expect wholesale revisions in violation of the spirit of legislation that required the negotiated rule-making. I have not yet had an opportunity to review the rule. But to highlight my concerns, I am advised that under the negotiated rule, 62 Missouri PHAs would have gained operating subsidies while 41 PHAs would have lost subsidies. Under OMB's changes, only 13 Missouri agencies would gain and 91 would lose funding. There is something wrong here.

PUBLIC HOUSING CAPITAL FUND

Equally troubling, HUD's 2006 budget request includes a $252 million reduction in the Public Housing Capital Fund despite an estimated $20 billion backlog in modernization needs.

BLOCK GRANT SECTION 8 VOUCHER ASSISTANCE AND HOMELESS FUNDING

HUD also is proposing new legislation to block grant both Section 8 voucher assistance and homeless funding. I have not yet seen the proposal to block grant homeless assistance funding. I support the approach assuming it is adequately funded and includes meaningful oversight. Nevertheless, the process needs sunshine.

I have seen the Section 8 voucher block grant proposal and it fails on a number of levels. First, the proposal fails to allow jurisdictions with real flexibility to use these funds for project-based assistance even in areas of the Nation where vouchers do not work because of tight rental markets. This means the administration only wants to provide flexibility on its own terms and not based on local needs and conditions.

More disturbing, the Section 8 proposal would eliminate the requirement that 75 percent of all vouchers go to extremely low-income families, those at or below 30 percent of median income. This is a critical requirement that ensures those with worst case housing needs receive priority in the award of scarce Section 8 housing assistance. Without the requirement, the number of homeless will continue to grow without real housing alternatives. This runs counter in my view to the administration's promise to end chronic homelessness within 10 years. This will promote homelessness rather than end it.

ZERO DOWNPAYMENT HOME OWNERSHIP PLAN

Finally, I am very troubled by the proposed FHA Zero Downpayment Home Ownership plan. As with last year, the proposal continues to pose substantial financial risks over time to the FHA Single Family Mortgage Insurance program, the Mutual Mortgage Insurance Fund. Without downpayments, new home buyers will have no stake in their new homes and will have limited ability to pay for any substantial repairs like a failed furnace or a leaky roof. As we discussed last year, FHA was close to bankruptcy in the late 1980's due to defaults from assisting families to purchase homes with high loan-to-value ratios. These houses were often in marginal neighborhoods. And once the homeowners defaulted, the housing would often remain unsold and thus drive down the housing values throughout a neighborhood. Some of the neighborhoods are still trying to recover from the foreclosures. Also, families in default have their credit ruined.

According to HUD's IG audit of FHA's financial statements for 2004 and 2003, the Mortgage Insurance Program suffers increasing default rates and claims. Over the last 5 years, defaults have increased from 3 percent in fiscal year 2000 to almost 7 percent in 2004. Claims have risen from $5.5 billion in 2000 to $8.5 billion in 2004.

Clearly, FHA has effectively become the lender of last resort, taking on the most risky mortgages with greatest risk of default. A new zero downpayment program will only enhance that risk.

I have been working on housing and community development since I was governor of Missouri. And despite my continuing efforts to reform HUD and support housing and community developments, HUD continues to remain in decline, characterized by failed programs and policy. I still believe this trajectory of failure can be stopped, but I am dismayed at the lack of support from OMB.

And I know, Mr. Secretary, you face an uphill battle with an administration that seems to have little interest or commitment to

HUD's programs and seems to be committed to dismantling the modest success that HUD has achieved.

I do not understand. When housing and community development investments work well, everyone benefits through more jobs, an increased tax base, better schools, and improved communities. Where we fail to create the right programs or fail to invest in these programs, neighborhoods deteriorate and the quality of peoples' lives suffer. It is that simple.

I am not looking for big increases in HUD programs. I believe that we need to preserve existing programs and try to build on successes where possible. We may not agree on everything, but I know you believe in the importance of HUD's mission and the need for HUD to be a leader and partner in housing and community development across the Nation.

PREPARED STATEMENT

I look forward to continuing to work with you. However, we need to revitalize and rebuild the public's confidence in HUD, and I look forward to hearing your vision for the department's future.

Now, with apologies for the length of the statement, I had to get it off my chest, and I now turn to my ranking member, Senator Murray.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD and Related Agencies will come to order. We welcome Secretary Alphonso Jackson for appearing before us today to testify on the Department of Housing and Urban Development's fiscal year 2006 budget request. Last year we did not have the benefit of a complete statement from you, having been newly confirmed as Secretary the night before the hearing. This year I especially look forward to your comments after a year on the job.

The administration's budget request for HUD for fiscal year 2006 proposes some $28.5 billion, a decrease of some $3.38 billion, or almost 11 percent, from the fiscal year 2005 funding level of $31.9 billion. Unfortunately, the overall fiscal year 2006 funding level does not accurately reflect the actual requested overall spending for HUD's many programs. Instead, the overall budget numbers are distorted through a budget rescission request of $2.5 billion as well as by how FHA receipts are treated for purposes of the fiscal year 2006 budget. In fact, the overall funding for HUD programs is far worse than the administration has indicated.

Proposed reductions to individual HUD programs include, among others, some $4.67 billion from CDBG funding, $118 million from Housing for Persons with Disabilities, $14 million from Housing for Persons with AIDS, $24 million from Rural Housing and Economic Development, $24 million from Brownfields, almost $286 million from HOPE VI, $226 million from Section 8 Project-Based Assistance, and $252 million from the Public Housing Capital Fund. I also am especially troubled by a proposed $2.5 billion rescission for which neither HUD nor OMB has been able or willing to identify the source of funding.

These program cuts are even more disturbing because of proposed reductions and shortfalls in other programs within the jurisdiction of this subcommittee. Mr. Secretary, I know you have an obligation to defend the administration's budget and policy decisions no matter how problematic. I also understand and support the need for the administration to make difficult funding decisions in order to contain and reduce the Federal budget deficit. Unfortunately, I believe that the President has been getting some very bad advice about the housing and community development needs of the Nation.

The HUD budget as well as a number of newly proposed HUD legislative and policy initiatives reflect this bad advice. Unfortunately, these problems go beyond just HUD, leaving this subcommittee to confront huge challenges in trying to balance funding decisions among the many programs and priorities within the entire TTHUD fiscal year 2006 Appropriations bill in an extraordinary tight funding year.

As always, HUD represents one of the largest challenges. Unfortunately, the administration's overall budget for domestic discretionary spending will make reversing many of these administration recommendations impossible or compel the Congress to eliminate funding from other important and necessary programs.

To start with the good news, Mr. Secretary, I applaud you for fighting the good fight in attempting to preserve section 8 tenant-based vouchers at a level that will sustain current voucher use. And while I am disappointed over the public housing capital and operating fund levels, I know you also staved off much larger reductions, as proposed by OMB. In addition, home ownership is at its highest level in history with some 73.7 million homeowners. I also applaud your efforts to stem the abuses of predatory lending by banning flipping, increasing home ownership counseling and putting in place more stringent appraisal requirements. Unfortunately, this is the good news but the list is much too short for an agency as important as HUD.

Now for the bad news. First, I am very disappointed that the administration has proposed to dismantle the CDBG program along with some 17 or more other programs and replace these programs with a new block grant in the Department of Commerce called the Strengthening America's Communities initiative. The administration also is proposing to fund this initiative at $3.7 billion which is an overall reduction for all these programs from the fiscal year 2005 level of almost $2 billion or 34 percent.

The proposed elimination of CDBG is a tragedy, but the reduction in funding makes this proposal a double tragedy. Communities across the Nation rely on CDBG to fund critical housing and community development programs. Without these funds, many local programs will falter and even fail. Equally important, CDBG is a critical component of HUD's mission; CDBG helps to make HUD's housing mission successful. Moreover, the use of CDBG consolidated plans helps to ensure that communities tie together CDBG, housing funds and other Federal and State resources into a comprehensive approach to local housing and community development needs. Without CDBG, HUD's mission will be reduced to almost solely housing. As history tells us, successful community development relies on a comprehensive approach to housing and community development. Without CDBG, HUD will be like a one-armed pitcher trying to field a bunt.

I know CDBG has problems; CDBG funds are not always used well or effectively. Even Kansas City, Missouri, with a vibrant and progressive nonprofit community, recently identified some significant abuses within its CDBG program. However, these problems are being addressed and resolved. The key is to fix problems in good programs, not dismantle the programs.

Moreover, recently, HUD, OMB and certain interested parties recently ratified a consensus document to address weaknesses in the CDBG program by creating an Outcome Measurement System to establish new benchmarks and better oversight. Since this document addresses many of OMB's concerns, I am puzzled by the administration's efforts to dismantle a program that has been redesigned to become more effective and successful according to administration requirements.

I also am very concerned over the administration's approach to public housing. The administration is seeking to eliminate HOPE VI as well as rescind the HOPE VI fiscal year 2005 funding of $143 million. As an alternative, the administration has issued a proposed regulation that will authorize PHAs to demolish the remaining obsolete public housing.

As you may know, I set the stage for HOPE VI by including a demonstration project in the 1990 National Affordable Housing Act that allowed the demolition and replacement of Pruitt-Igoe Public Housing in St. Louis with vouchers and new housing. Before this demonstration, PHAs could not be demolished without a one-for-one hard unit replacement. Because of the cost of this policy, the public housing program dictated the warehousing of the poor in obsolete and deteriorating PHA high-rises. HOPE VI allowed for the demolition of this obsolete housing and the creation of mixed income private and public housing that anchored private investment and the revitalization of entire communities.

While HOPE VI is not a perfect solution to all the woes of obsolete public housing, it has transformed many PHAs and communities, including many in Missouri, by replacing obsolete public housing with mixed income public and private housing. In many cases, HOPE VI housing has leveraged new investment in these communities. This means new businesses, an increased tax base, better schools and safer communities. It is unfortunate that the budget rules do not recognize these very tangible economic and social benefits.

The administration also has broken a promise to develop a new operating fund formula by negotiated rulemaking. Over the last 5 or more years, HUD has worked with PHAs through negotiated rulemaking to develop a new budget-based operating plan formula to ensure a more equitable system of allocating operating subsidies to

PHAs. Millions of dollars have been spent on this process. Nevertheless, a negotiated rule went into OMB's rulemaking review process and came out a much different flavor of sausage. One expects OMB to make changes to regulations under review; one does not expect wholesale revisions in violation of legislation that required negotiated rulemaking. I have not yet had an opportunity to review the rule. But to highlight my concerns, I am advised that, under the negotiated rule, 62 Missouri PHAs would have gained operating subsidies while 41 PHAs would have lost subsidies. Instead, under the OMB's changes, only 13 Missouri agencies would gain while 91 would lose funding. There is something wrong here. Equally troubling, HUD's fiscal year 2006 budget request includes a $252 million reduction in the Public Housing Capital Fund despite an estimated $20 billion backlog in modernization needs.

HUD also is proposing new legislation to block grant both section 8 voucher assistance and homeless funding. I have not yet seen the proposal to block grant homeless assistance funding but I support the approach assuming it is adequately funded and includes meaningful oversight.

I have seen the section 8 voucher block grant proposal. Once again, the proposal fails on a number of levels. First, the proposal fails to allow jurisdictions with real flexibility to use these funds for project-based assistance even in areas of the Nation where vouchers do not work because of tight rental markets. This means the administration only wants to provide flexibility on its own terms.

More disturbing, the section 8 proposal would eliminate the requirement that 75 percent of all vouchers go to extremely low-income families—those at or below 30 percent of median income. This is a critical requirement that ensures those with the worst case housing needs receive priority in the award of scarce section 8 housing assistance. Without this requirement, the number of homeless will continue to grow without real housing alternatives. This runs counter to the administration's promise to end chronic homelessness within 10 years.

Finally, I am very troubled by the proposed FHA Zero Downpayment Homeownership program. As with last year, this proposal continues to pose substantial financial risks over time to the FHA Single Family Mortgage Insurance program and the Mutual Mortgage Insurance Fund—without downpayments, new homebuyers will have no stake in their new homes and will have limited ability to pay for any substantial repairs such as a failed furnace or leaky roof.

As we discussed last year, FHA was close to bankruptcy in the late 1980's due to defaults from assisting families to purchase homes with high loan-to-value-ratios. These houses were often in marginal neighborhoods, and once these homeowners defaulted, the housing would often remain unsold and, thus, help drive down housing values throughout a neighborhood. Some of these neighborhoods are still trying to recover from those foreclosures, and the families in default often ruined their credit.

According to the HUD IG's audit of the FHA's financial statements for fiscal years 2004 and 2003, the FHA mortgage insurance program continues to suffer increasing default rates and claims. Over the last 5 years, defaults have increased from 2.99 percent in fiscal year 2000 to 6.9 percent in fiscal year 2004. Moreover, claims have risen from some $5.5 billion in fiscal year 2000 to some $8.5 billion in fiscal year 2004, a 54 percent increase while insurance-in-force has decreased 13 percent to $430 million during the same period. Clearly, FHA has effectively become the lender of last resort, taking on the most risky mortgages with the greatest risk of default. A new zero downpayment program will only enhance this risk.

I have been working on housing and community development issues for most of my career from the governor's office in Missouri to my current position on the Appropriations Committee in the Senate. Unfortunately, despite my continuing efforts to reform HUD and support housing and community development initiatives, the Department of Housing and Urban Development remains in decline, characterized by failed programs and policies. I still believe that this trajectory of failure can be stopped, but I am dismayed by the lack of progress.

Mr. Secretary, I know that you face an uphill battle with an administration that seems to have little interest or commitment to HUD's programs and instead seems committed to dismantling the modest successes that HUD has achieved. I do not understand—when housing and community development investments work well, everyone benefits, jobs are created, taxes are collected, and schools and communities improve. Where we fail to create the right programs or fail to invest in these programs, neighborhoods deteriorate and the quality of peoples' lives suffer. It is that simple.

I am not looking for big increases in HUD programs. I do, however, believe that we need to preserve existing programs and try to build on these modest successes where possible. We may not agree on everything, but I know you believe in the importance of HUD's mission and the need for HUD to be a leader and partner in housing and community development initiatives throughout the Nation. I look forward to continuing to work with you on making the Department a strong leader and partner. However, we need to revitalize and rebuild the public's confidence in HUD, and I look forward to hearing your vision for the Department's future.

Thank you. I turn now to my Ranking Member, Senator Murray.

STATEMENT OF SENATOR TED STEVENS

Senator STEVENS. Mr. Chairman and Senator Murray, I have to Chair the Commerce Committee markup, but would you permit me just 3 minutes.

Senator BOND. Senator Stevens.

Senator STEVENS. I am here to ask you to meet me in Alaska this year before this bill is marked up, before this bill is reported to the floor.

IHBG FUNDING IN ALASKA

There have been developments in your Department that affect our State that are staggering. Our field office is down in Stockton, California. Your Department has recognized now what I call rogue villages and taken away from a regional housing authority the jurisdiction over housing and given it to—in one instance to a group that calls themselves a village, but their traditional village is 200 miles from where they say they have the right to conduct housing.

And they have taken some 55 villages away from the existing housing authority and turned it over to this rogue group and they are not building housing. They are just employing their own people.

What is going up our way now is just staggering as far as the activities of your Department. And if we cannot get together on some understanding of what is going to happen, I am going to offer a series of amendments to this bill to mandate that these practices be changed.

We cannot exist this way. Your people, who never come to Alaska, sit down in the field office in California and decide what is right in Alaska. Now, that just cannot go on.

The relationships with the State are so strained that the people down there reduced the housing allowance for operations in Alaska, the highest in the Nation, a 53 percent cut in Alaska compared to an average 20 percent throughout the country.

Now, we have some people who are really in need for housing in the villages. But people sitting down in California, I do not know what they are doing down there. But these decisions are—I did not know it till just recently, and they are staggering.

PREPARED STATEMENT

I would urge you to come up and let us go out and look at these things and you meet the people that claim to be—that have the right to build these houses in an area they never lived in, they do not represent, and the people in the area oppose them. That is other than a few people that are off the reservation, so to speak.

But I do think this has to be changed. And I ask that my statement appear in the record. I appreciate your courtesy.

[The statement follows:]

PREPARED STATEMENT OF SENATOR TED STEVENS

Good morning Secretary Jackson—I am pleased to see you here this morning.

I must leave this hearing shortly to chair a markup session of the Commerce Committee, but I would like to ask for your help on some matters within your agency that are causing problems for us in Alaska.

The first is the matter of how HUD allocates its Indian Housing Block Grant funding. Within the State of Alaska, we now have some 231 federally-recognized "tribes," some with no or only a few members. This was a policy promulgated by the previous administration and is one with which I do not agree. In Alaska, our Native housing programs were traditionally operated by regional Native housing organizations which were large enough to bring economies of scale to housing programs across our vast State. Since the passage of the Native American Housing and Self Determination Act in 1996, and especially since the 2000 census, HUD has been moving to transfer some of this funding away from regional housing authorities and put it into the hands of small villages and "tribes" in Alaska. The most egregious example of this misguided policy has occurred in the Cook Inlet Region, which includes Anchorage. The Cook Inlet Housing Authority has been stripped of a substantial portion of its Indian housing funds. Those funds have been awarded to a so-called tribe called Kanatak to cover the entire Mat-Su Valley part of the Cook Inlet region. However, Kanatak's traditional lands are located hundreds of miles away on the Western coast of Alaska, and have not been occupied since 1956. As a result, the Cook Inlet Housing Authority's funding now covers only 8 communities in the region, down from the 55 communities it has traditionally covered and should be covering right now.

I hope you will agree to help resolve this situation in the near future—it is making it very difficult to provide economical housing for our Alaska Native population.

On another matter, I have heard from our Alaska Housing Finance Authority that your department is proposing to cut the operating subsidy it receives to operate public housing across Alaska by 53 percent the largest cut proposed for any housing authority in the Nation. I also understand that changes in the operating subsidies—the so-called "Allowable Expense Levels" are being proposed as a result of a study done by Harvard University. However, that study did not examine the particular conditions in Alaska, but still proposed a cut almost twice as large as the next largest cut. The AHFC has told my staff that they will not be able to continue to operate public housing in Alaska if a cut of this magnitude is allowed to go forward.

I believe a number of these problems stem from the Department's senior management not being familiar with Alaska. We used to have a HUD Field Office in Alaska, but that was closed about 10 years ago, and now our field office is located in Santa Ana, California—a place that has little in common with Alaska. I hope you will give some consideration to establishing more of a presence in my State, which covers an area one-fifth the size of the entire lower 48.

Mr. Secretary, I invite you to bring your senior staff and come to Alaska to see for yourself what our housing problems look like and how they differ from those in most lower-48 communities. I hope you will do that and will work with me to solve these and other problems.

Senator BOND. Thank you, Senator Stevens.

And, Mr. Secretary, you have only been in this position about a year, but I would suggest to you that those suggestions are ones which you should adopt.

I will explain to you later if you have any questions.

Now I turn to Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Well, thank you very much, Mr. Chairman, and I will join with you welcoming Secretary Jackson to our subcommittee this morning.

Mr. Secretary, you have had a distinguished career serving in the public housing field in Dallas, St. Louis, and Washington, DC. Your expertise and your commitment are needed as families throughout our country are really struggling with the high cost of housing.

Unfortunately, Mr. Secretary, you have been handed a very difficult budget to defend. I have always said that a budget is a statement of priorities. In looking at this budget, it is hard to reach any other conclusion than that housing is not a priority for this administration.

And we are not just talking about numbers. The cuts and problems in this budget will affect the lives of some of our most vulnerable neighbors.

I wish the Bush Administration valued them more and was willing to give us a budget that does make housing a priority. But sadly this appears to not be the case.

So we will do our best with the budget the administration has sent us. But I do want to note that the situation is actually worse than some of the figures we are going to be hearing today.

In looking at the budget before us, some might see a 12 percent cut from last year. But when you take a closer look at the numbers, you see the cuts are actually closer to 20 percent. And that is because this budget calls for a large number of rescissions, $2.65 billion.

I know last year before HUD came under the jurisdiction of our subcommittee, the administration sought approval to cut about $1.5 billion that were appropriated but never spent. Now the administration wants to go into the current year's budget and cut an additional $2.65 billion.

So when you add in the rescissions on top of the regular budget cuts, the size of the administration's proposed cuts to HUD grows to almost $6.5 billion or a 20 percent cut from last year.

That is a very dark picture for American families and for cities and for communities that are really trying to help and develop distressed areas.

As I look at these rescissions, what I see is troubling. But what I do not see is even more troubling. I do not see a detailed explanation specifying where $2.5 billion of the proposed rescission is coming from.

It is like the administration is asking us for a sledgehammer and then telling us not to worry about where they are going to use it. Well, I want you to know I am worried.

Under these proposed rescissions, HUD is granted the blanket authority to take away the funding from any program in the agency. That means that additional cuts can come from programs serving the homeless or the disabled or individuals living with HIV and AIDS. They can eliminate housing vouchers for the working poor or cut back on locally based Meals on Wheels programs.

All that is in addition to the administration's proposal to eliminate the Community Development Block Grant Program and the variety of support programs and services it funds.

So the administration is saying not only are we going to cut funding for HUD programs, but we are asking to open up a previous appropriations act and cut another $2.5 billion however we see fit. That could have a very painful impact on many of our neighbors.

HOPE VI

The only part of the rescission that the administration has provided any information about concerns the HOPE VI program. So let us look at what the administration proposes.

The HOPE VI program has the worthy goal of tearing down old, dilapidated public housing units and replacing them with affordable housing units for mixed-income populations. The President plans to eliminate that program for next year.

But it gets worse. The administration also wants us to go back and rescind the $143 million that we already appropriated for this program for this current year.

So it is not enough just to kill it for next year, they want us to gut it this year and undo Congress' work of the past year. Together these proposals represent the elimination of some $300 million in HOPE VI grants.

This idea of unaccountable, undefined, blanket rescissions really concerns me deeply, Mr. Chairman. I have served on the Appropriations Committee for the great majority of my almost 13 years in the Senate and I believe we have a responsibility when we appropriate taxpayer dollars to know where they are going.

And by the same measure, when we are asked to take funds away from agencies that have already received them, I want to know precisely what projects or grants or services that we already funded will now be cut.

So I hope to use a portion of the hearing this morning to get a clear and precise answer from Secretary Jackson as to the likely impacts of this budget proposal and what will result if he is required to cancel more than $4 billion in funding already appropriated to his agency over the course of this year and next.

The challenges that are facing the Department of Housing and Urban Development are daunting and the administration's proposed budget cuts make it even worse.

PREPARED STATEMENT

I cannot make the administration treat housing like a priority, but I can do everything possible to make sure we do not make things worse. I want to give the Secretary the resources he needs to protect and expand housing opportunities for the poor and community development programs for local communities.

Thank you, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF SENATOR PATTY MURRAY

Thank you, Mr. Chairman.

I want to welcome Secretary Jackson to the subcommittee this morning.

Mr. Secretary—you have had a distinguished career serving in the public housing field in Dallas, St. Louis, and Washington, DC.

Your expertise and your commitment are needed as families throughout the country struggle with the high cost of housing.

Unfortunately, Mr. Secretary, you've been handed a very difficult budget to defend.

I've always said that a budget is a statement of priorities, and looking at this budget it's hard to reach any other conclusion than that housing is not a priority for this administration.

And we're not just talking about numbers. The cuts and problems in this budget will affect the lives of some of our most vulnerable neighbors.

I wish the Bush Administration valued them more—and was willing to give us a budget that makes housing a priority.

But sadly that is not the case, so we will do our best with the budget the administration has sent us.

But I do want to note that the situation is actually worse than some of the figures we'll hear today.

In looking at the budget before us, some might see a 12 percent cut from last year.

But when you take a closer look at the numbers—you see that the cuts are actually closer to 20 percent.

That's because this budget calls for large number of rescissions—$2.65 billion.

I know that last year—before HUD came under the jurisdiction of this subcommittee—the administration sought approval to cut about $1.5 billion dollars that were appropriated but never spent.

Now the administration wants to go into the current year's budget and cut an additional $2.65 billion.

So when you add in these rescissions—on top of the regular budget cuts—the size of the administration's proposed cuts to HUD grows to almost $6.5 billion, or a 20 percent cut from last year.

That is a very dark picture for American families and for cities and communities that are trying to develop distressed areas.

As I look at these rescissions, what I see is troubling—but what I don't see is even more troubling.

I don't see a detailed explanation specifying where $2.5 billion of the proposed rescission is coming from.

It's like the administration is asking us for a sledgehammer and then telling us not to worry about how they'll use it. Well I am worried.

Under these proposed rescissions, HUD is granted the blanket authority to take the funding from any program in the agency.

That means additional cuts can come from programs serving the homeless, the disabled, or individuals living with HIV/AIDS.

They can eliminate housing vouchers for the working poor or cut back on locally-based meals-on-wheels programs.

All that is in addition to the administration's proposal to eliminate the Community Development Block Grant program and the variety of support programs and services it funds.

So the administration is saying not only are we going to cut funding for HUD Programs, but we're asking to open up a previous appropriations act and cut another $2.5 billion however we see fit.

That could have a painful impact on many of our neighbors.

The only part of the rescission that the administration has provided any information about concerns the HOPE VI program—so let's take a look at what the administration proposes.

The HOPE VI program has the worthy goal of tearing down old, dilapidated public housing units and replacing them with affordable housing units for mixed income populations.

The President plans to eliminate this program next year.

But it gets worse.

The administration also wants us to go back and rescind the $143 million that we already appropriated for this program for the current year.

So it's not enough to kill it next year—they want to gut it this year and undo Congress's work in this area.

Together, these proposals represent the elimination of some $300 million in HOPE VI grants.

This idea of unaccountable, undefined blanket rescissions concerns me deeply.

I have served on the Appropriations Committee for the great majority of my almost 13 years in the Senate.

I believe we have responsibility when we appropriate taxpayer dollars to know where they are going.

By the same measure, when we are asked to take funds away from agencies that have already received them, I want to know precisely what projects, grants or services—that we already funded—will now be cut.

So, I hope to use a portion of our hearing this morning to get clear and precise answers from Secretary Jackson as to the likely impacts of this budget proposal and what will result if he is required to cancel more than $4 billion in funding already appropriated to his agency over the course of this year and next.

The challenges facing the Department of Housing and Urban Development are daunting. And the administration's proposed budget cuts make it even worse.

I can't make the administration treat housing like a priority, but I can do everything possible to make sure we don't make things worse.

I want to give the Secretary the resources he needs to protect and expand housing opportunities for the poor and community development programs for local communities.

Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Murray. Senators Durbin and Leahy have submitted written statements which will also be made a part of the record.

[The statements follow:]

PREPARED STATEMENT OF SENATOR RICHARD J. DURBIN

Mr. Jackson, thank you for testifying before this subcommittee today. I am very concerned about the housing cuts that have been proposed for HUD. These cuts could severely hinder HUD's ability to address community development needs in cities, towns, and communities across the country. They jeopardize housing for low-income individuals, families, the elderly, and the disabled.

I remain troubled about the President's proposal to eliminate the Community Development Block Grant (CDBG) program and replace it with a new initiative within the Department of Commerce. CDBG has supported State and local governments' community development and neighborhood revitalization activities for over 30 years. It has provided more than just economic opportunities. The funds have been used to conserve and expand affordable housing, improve access to public water and sewer facilities, create jobs, and improve lives. These are the building blocks for our neighborhoods.

Communities across Illinois, like Pekin, a town with approximately 34,000 people, or Cooksville, a village with slightly over 200 people, received CDBG funds for revitalization efforts. In Chicago, a community group received a CDBG grant to start a "Safe Passages" program—a shuttle service for children in the neighborhood tutoring program. It provided students with free transportation—a safe passage—from tutoring programs, through some of the toughest gang territories in Chicago, to a Boys and Girls Club where the children can swim, play sports, and eat a snack or a meal. Before "Safe Passages" and the CDBG grant, kids in this neighborhood stayed home after school or hung out on the corner and were recruited by gangs. Today, they have a way out.

I am also concerned about the President's request for $268 million for the Housing for Persons with AIDS (HOPWA) program, a cut in funding from the $282 million appropriated last year. Of the 15,000 people in Chicago who may be homeless on any given night, 8 percent have HIV. Nationwide, the Centers for Disease Control estimates that there are 886,575 people living with HIV/AIDS, and approximately 50 percent need some form of housing assistance. HOPWA provides this vital assistance and creates access to medical care and support services. In 2005, HOPWA provided support for 122 jurisdictions eligible for formula allocations. HUD announced that two additional jurisdictions will be eligible for funds in 2006, but overall funding for the program continues to decrease. Senator Martinez and I are currently circulating a letter that will be sent to this committee urging $385 million for fiscal year 2006. I hope this committee will take the request into consideration.

I have concerns about several other programs that are slated for cuts. For instance, this is the third consecutive year that the President has proposed eliminating HOPE VI. This funding has been crucial for several Illinois communities.

In fiscal year 2002, the Winnebago County Housing Authority received a HOPE VI revitalization grant for $18.8 million. The funding was granted to demolish Champion Park Apartments, 61 subsidized low-rise apartments, and replace them over the next 2 years with 156 homes throughout the neighborhood.

I was pleased to see an increase in the President's budget for Homeless Assistance Grants. Last year, 20 of my colleagues and I sent a letter to this committee urging funding for renewals of expiring grants to permanent supportive housing serving the homeless. Although our request was not granted, the committee and the administration have acknowledged the importance of permanent supportive housing in the fight against chronic homelessness.

If the administration is going to continue to live up to its commitment to end chronic homelessness, we must also ensure that the proper infrastructure is in place. The Housing Choice Voucher Program has been a large part of that infrastructure. But, with formula changes and funding shortfalls, the wait lists are growing and families with vouchers are being told that they are losing their assistance. We must ensure that funding for vouchers is made available so that those in need of subsidized housing don't add to the number of people on the streets.

Finally, Mr. Jackson, you have spoken about home ownership as part of the President's vision of an "ownership society"—that it "is the key to financial independence, the accumulation of wealth, and, stronger, healthier communities." I agree that home ownership is often a key to achieving the American dream. However, in light of the proposed HUD budget cuts, we must not lose sight of those who will be left alone—those who cannot achieve home ownership. We must continue to focus attention and funding on community development and on increasing our supply of decent, safe and affordable housing for all.

I appreciate the opportunity to speak with you today. I look forward to hearing your testimony.

PREPARED STATEMENT OF SENATOR PATRICK J. LEAHY

Secretary Jackson, I would like to welcome you today in your first appearance before our newly reconstituted and renamed subcommittee. It's a new name, but I think you will see some familiar faces. Mr. Secretary, Senator Bond and Senator Murray—I look forward to working with you all as we tackle this new bill in the upcoming fiscal year.

This is my first hearing as a member of the subcommittee and I have to say that I wish it could start on a more positive note. Unfortunately the President's proposed budget for the work of your department is one that again invites disappointment and even incredulity, not praise.

For the fifth year in a row the President has sent up a budget that ratchets down affordable housing among our budget priorities, and that would increase, not lessen, the burden put on the shoulders of our Nation's struggling low-income families.

The budget before us signals a substantial retreat in our commitment to help provide access to safe and affordable housing for all Americans. The public housing operating fund has been reduced by 10 percent, funds for housing for persons with disabilities have been cut in half, HOME formula grants have been reduced, fair housing programs have been slashed and lead-based paint grants have been cut.

Most egregious is the complete elimination of the Community Development Block Grant program—a proposal that has been met with what can be mildly described as skepticism by most members for the United States Senate. When all is said and done, the HUD budget is reduced by 12 percent. One of the few programs to see an increase in this budget proposal is the Section 8 program, and even that increase will only be enough to restore half of the cuts that were made this year as a result of inadequate funding in fiscal year 2005.

If a budget is a reflection of priorities, and of course it is, the message being sent here is that the people who struggle in our society and who need the helping hands offered by these programs to put decent shelter over their heads do not matter. Our Nation's core affordable housing and community development programs are being chipped away, year after year. I hope to hear from you today about the vision you have for the Department of Housing and Urban Development and how you expect to run efficient and effective programs like these, when they are slowly being starved to death.

Senator BOND. And now, Secretary Jackson, we welcome your statement. The full statement will be made a part of the record as always and we would appreciate your advising us orally of the things that you think should be especially highlighted.

STATEMENT OF ALPHONSO JACKSON

Mr. JACKSON. Thank you. Chairman Bond, Ranking Member Murray, and distinguished members of the subcommittee, thank you for inviting me here this morning.

And I am honored to outline the 2006 budget proposed by President Bush for the United States Department of Housing and Urban Development. And I appreciate you letting me submit the whole record to the committee.

HOME OWNERSHIP

Over the past 4 years, HUD has expanded home ownership, increased access to affordable housing, fought housing discrimination, tackled homelessness, and renewed its commitment to those most in need.

HUD's $28.5 billion budget for 2006 seeks to build on our success and lend a compassionate hand to individuals in need, while also using taxpayers' money more wisely.

In June 2002, President Bush challenged the Nation to create 5.5 million new minority homeowners. In 2004, more Americans achieved the dream of home ownership than at any other time in our Nation's history. Today, nearly 70 percent of all American families own their homes, an all-time record.

Since the President challenged us in August of 2002, 2.2 million more minority families have become homeowners. This represents about 40 percent of the goal. As a result, for the first time in the history of minority home ownership, it is over 51 percent.

Despite this progress, we have a long ways to go. For many families, high down payment and closing costs represents the greatest barrier of home ownership.

Since President Bush signed the American Dream Downpayment Act into law in December of 2003, HUD has distributed $162 million in funds to over 400 State and local governments.

These funds have already helped thousands of families purchase their first home and more than 50 percent of the buyers were minorities.

The 2006 budget requests $200 million to fully fund the program and help an estimated 40,000 homeowners. The budget also proposed $40 million for housing counseling to assist some 700,000 families to become homeowners.

SECTION 8 REFORM

The fiscal year 2006 budget will make government a better steward of the taxpayers' money. Reform of the Section 8 Housing Choice Voucher Program is important.

In fiscal year 2001, HUD's three Section 8 programs consumed 43 percent of the annual budget. That percentage has increased to 57 percent in 2005.

The rate of increase combined with the extreme complex set of laws and regulations has resulted in a program that is difficult to sustain.

In the past, funds were distributed to the public housing authority for a specific number of vouchers based upon the number of units leased. Congress recently converted the unit-based allocation system to a budget-based system.

However, for the budget-based system to work, program requirements must be simplified and PHAs must have greater decision-making flexibility.

Chairman Allard, who is on the Appropriations Committee, has introduced and authorized legislation to implement the Section 8 reform. Section 8 programs will fill an important component of HUD's mission and I am committed to it and its success.

HOMELESSNESS

Throughout the budget, we will strengthen the assistance to the most needy. That is children from low-income families, the elderly, those physically and mentally disabled, victims of predatory lending, and families living in housing contaminated by lead-based paint.

The administration is committed to ending homelessness and has aggressively pursued the policy to move more homeless families and individuals to permanent housing.

The budget provides a record-level resource of permanent and supported housing for the homeless. This budget provides $1.4 billion for homeless assistance grants. Twenty-five million will go to the present Re-entry Initiative.

The budget also proposes $39 million in funds for HUD's Fair Housing Programs to ensure that everyone has access to suitable living conditions, and a suitable living environment that is free from unlawful discrimination.

All of us share the goal of creating housing opportunities for America. And we have done a great job in the past 4 years. We should be proud of a lot of the things that we have done, but we should not be satisfied because there is an awful lot to be done.

I look forward to the challenges ahead and will seek the open communications to new home ownership, affordable housing opportunities, economic growth, and prosperity.

PREPARED STATEMENT

I would like to thank you, Mr. Chairman, and the ranking member of the subcommittee for your support and for your continued support in the future. And I will look forward to your guidance.

[The statement follows:]

PREPARED STATEMENT OF ALPHONSO JACKSON

Chairman Bond, Ranking Member Murray, distinguished members of the subcommittee, thank you for the invitation to join you this morning. I am honored to outline the fiscal year 2006 budget proposed by President Bush for the U.S. Department of Housing and Urban Development (HUD).

Over the past 4 years, HUD has expanded home ownership, increased access to affordable housing, fought housing discrimination, tackled homelessness, and made a new commitment to serving society's most vulnerable. The Department has implemented innovative solutions to address our Nation's housing needs, and our results have been impressive and measurable.

HUD's $28.5 billion in new net budget authority for fiscal year 2006 seeks to build on our success and lend a compassionate hand to individuals in need, while also using taxpayer money more wisely and reforming programs in need of repair. The HUD budget proposed by the President reflects this intent through three broad, yet focused strategic goals: promoting economic opportunity and ownership, serving society's most vulnerable, and making government more effective.

In his February 2 State of the Union Address, the President underscored the need to restrain spending in order to sustain our economic prosperity. As part of this restraint, it is important that total discretionary and non-security spending be held to levels proposed in the fiscal year 2006 budget. The budget savings and reforms in the budget are important components of achieving the President's goal of cutting the budget deficit in half by 2009 and we urge the Congress to support these reforms. The fiscal year 2006 budget includes more than 150 reductions, reforms, and terminations in non-defense discretionary programs, of which eight affect HUD programs. The Department wants to work with the Congress to achieve these savings.

The funding reductions, reforms, and terminations contained within HUD's fiscal year 2006 budget represent difficult choices in an era of significantly diminished resources for all domestic discretionary programs. These decisions were made thoughtfully, following an analysis of each program's current funding levels and an assessment of future needs.

PROMOTING ECONOMIC OPPORTUNITY AND OWNERSHIP

The President's vision of an "ownership society" has been a central theme of his administration. Ownership—and home ownership in particular—is the key to financial independence, the accumulation of wealth, and stronger, healthier communities.

Home ownership creates community stakeholders who tend to be active in charities, churches, and neighborhood activities. Home ownership inspires civic responsibility, and homeowners are more likely to vote and get involved with local issues. Home ownership offers children a stable living environment, and it influences their personal development in many positive, measurable ways—at home and at school.

Home ownership's potential to create wealth is impressive, too. For the vast majority of families, the purchase of a home represents the path to prosperity. A home is the largest purchase most Americans will ever make—a tangible asset that builds equity, good credit, borrowing power, and overall wealth.

In 2004, more Americans achieved the dream of home ownership than at any time in our Nation's history. Today, nearly 70 percent of American families own their homes—an all-time record—and minority home ownership has surpassed 51 percent for the first time in history.

That figure, however, points to a significant home ownership gap between non-Hispanic whites and minorities. In June 2002, the President challenged the Nation to create 5.5 million new minority homeowners by 2010. Since the President's challenge, 2.2 million minority families have joined the ranks of homeowners, and we are on track to meet the 5.5 million goal.

The administration is working to make home ownership more affordable and more accessible. Government should do everything it can to help families find the security, dignity, and independence that come with owning a piece of the American Dream.

For many Americans, high downpayments and closing costs represent the greatest barrier to home ownership. To help overcome this obstacle, the President proposed the American Dream Downpayment Initiative to provide low- and moderate-income families with the funds and support needed to purchase their first home. On December 16, 2003, President Bush signed the American Dream Downpayment Initiative into law, and since then, HUD has distributed $162 million in downpayment funds to over 400 State and local governments. These funds have already helped over 3,500 families purchase their first homes—of which more than 50 percent were minorities. The 2006 budget requests $200 million to fully fund the Initiative.

Helping families learn about the loan products and services available to them and how to identify and avoid predatory lending practices is critical to increasing home ownership. Housing counseling has proven to be an extremely important element in both the purchase of a home and in helping homeowners keep their homes in times of financial stress. The fiscal year 2006 budget proposes $40 million for Housing Counseling to assist over 700,000 families to become homeowners or avoid foreclosing on their homes. This effort will fully utilize faith-based and community organizations.

To remove two of the largest barriers to home ownership—high downpayment costs and impaired credit—the budget proposes two mortgage programs. The Zero Downpayment Mortgage allows first-time buyers with a strong credit record to finance 100 percent of the home purchase price and closing costs. For borrowers with limited or weak credit histories, a second program, Payment Incentives, initially charges a higher insurance premium and reduces premiums after a period of on-time payments. In 2006, these new mortgage programs will assist more than 250,000 families achieve home ownership.

The President is also proposing a new Single Family Homeownership Tax Credit that could increase the supply of single-family affordable homes by an additional 50,000 homes annually. Under the President's plan, builders of affordable homes for moderate-income purchasers will receive a tax credit. State housing finance agencies will award tax credits to single-family developments located in a census tract with median income equal to 80 percent or less of area median income and will be limited to homebuyers in the same income range. The credits may not exceed 50 percent of the cost of constructing a new home or rehabilitating an existing property. Each State would have a home ownership credit ceiling adjusted for inflation each year and equal to the greater of 1.75 times the State population or $2 million. In total, the tax credit will provide $2.5 billion over 5 years.

As you know, tax legislation is the responsibility of the Treasury Department, but we will be working with Treasury's Office of Tax Policy to ensure that the credit legislation addresses issues such as disclosures, so that the credit operates smoothly.

The Homeownership Voucher program, while still new, has successfully paved a path for low-income Americans to become homeowners. Together with pre- and post-home ownership counseling, strong and committed collaboration among Public Housing Authorities (PHAs), local non-profits, and lenders has proven to be essential in making the program work for families across the country. The greatest challenge to the success of the program is finding lenders who are willing to participate.

Government-sponsored enterprises were chartered to help low- and moderate-income families secure mortgages. HUD recently published a rule that requires Fannie Mae and Freddie Mac to increase their purchases of mortgages for low- and moderate-income households and underserved communities. These new goals will push the GSEs to genuinely lead the market in creating home ownership opportunities for those traditionally underserved by the mortgage markets, particularly first-time homebuyers.

In addition to increasing the housing goals annually from 2005 through 2008, HUD's rule establishes new home purchase subgoals in each of the three goal areas. This is intended to focus the GSEs' efforts on the purchase of home mortgages, not refinancings. HUD projects that over the next 4 years, GSEs will purchase an additional 400,000 home purchase loans that meet these new and more aggressive goals as a result of the new rule.

As the primary Federal agency responsible for the administration of fair housing laws, HUD is committed to protecting the housing rights of all Americans, regardless of race, color, national origin, religion, sex, familial status, or disability. This commitment is reflected in HUD's budget request for fiscal year 2006.

The goal of HUD's fair housing programs is to ensure that all families and individuals have access to a suitable living environment free from unlawful discrimination. HUD contributes to fair housing enforcement and education by directly enforcing the Federal fair housing laws and by funding State and local fair housing efforts through two programs: the Fair Housing Assistance Program (FHAP) and the Fair Housing Initiatives Program (FHIP).

The fiscal year 2006 budget will provide $23 million through FHAP for State and local jurisdictions that administer laws substantially equivalent to the Federal Fair Housing Act. The budget also provides $16 million in grant funds for non-profit FHIP agencies nationwide to directly target discrimination through education, outreach, and enforcement.

The fiscal year 2006 budget requests $583 million to fund Native American Block Grants (NABG). These grants are used by tribes and tribally designated housing entities to develop new housing units to meet critical shortages in housing. Although NABG funding has been reduced in fiscal year 2006, HUD expects that all program requirements will be met, including new housing development, housing assistance to modernize and maintain existing units; housing services, including direct tenant rental subsidy; guaranteed lending; crime prevention; administration of the units; and certain model activities.

SERVING SOCIETY'S MOST VULNERABLE

Ending Chronic Homelessness.—The administration is committed to the goal of ending chronic homelessness, and has aggressively pursued policies to move more homeless families and individuals into permanent housing. A chronically homeless person suffers from a disabling developmental, physical, or mental condition or a substance abuse addiction. They have been homeless for a year or more, or they have had repeated periods of extended homelessness. They may occasionally get help and leave the streets, but they soon fall back to a life of sidewalks and shelters.

Research indicates that although just 10 percent of the homeless population experiences chronic homelessness, these individuals consume over half of all emergency homeless resources. Housing this population will free Federal, State, and local emergency resources for families and individuals who need shorter-term assistance.

In July 2002, the President reactivated the Interagency Council on Homelessness for the first time in 6 years, bringing together 20 Federal entities involved in combating homelessness. Since its inception, the Interagency Council has helped State and local leaders across America draft plans to move chronically homeless individuals into permanent supportive housing, and to prevent individuals from becoming chronically homeless. Today, 47 States and more than 200 county and city governments have joined the Federal effort.

The budget provides a record level of resources for permanent supportive housing for homeless individuals who have been on the streets or in shelters for long periods. The 2006 budget provides $1.44 billion for Homeless Assistance Grants ($25 million of which is for the Prisoner Re-Entry Initiative), $200 million more than in 2005. Altogether, the administration requests $4 billion in 2006 for Federal housing and social service programs for the homeless, an 8.5 percent increase.

Housing for Special Populations.—Housing Opportunities for Persons with AIDS (HOPWA) provides formula grants to States and localities to provide housing to ensure persons with AIDS can continue to receive health care and other needed support. The program also provides competitive grants to nonprofit organizations. In fiscal year 2006, HOPWA will fund an estimated 25 competitive grants and will provide formula funding to an estimated 124 jurisdictions and in total will provide an estimated 67,000 households with housing assistance.

The fiscal year 2006 HOPWA funding request represents a 5 percent decrease from the fiscal year 2005 funding level. The reduction was one of a number of difficult choices the administration made in formulating the fiscal year 2006 budget, but one which is in consistent with the goal of restraining spending in order to sustain economic prosperity. HUD is seeking changes in the HOPWA formula that will improve the targeting of the program, so that HOPWA better supports those whom it was created to serve—the most vulnerable persons, and individuals who are homeless or with very low incomes—ahead of other low-income households.

The fiscal year 2006 budget proposes to fund grants of $119.9 million for Supportive Housing for Persons with Disabilities (Section 811). Section 811 provides assistance to expand the supply and the availability of affordable housing for persons with disabilities. The administration is proposing the elimination of the program's new construction component, resulting in a $118.2 million funding decrease from fiscal year 2005. The Section 811 program will continue to support all previously funded housing subsidies under the program and up to 1,000 new housing vouchers. The administration intends to undertake a study of the Section 811 program to determine the most efficient use of the limited funding available for it.

HUD's Office of Lead Hazard Control and its Healthy Homes Initiative work to eradicate childhood lead poisoning and prevent other housing-related childhood diseases and injuries. The fiscal year 2006 budget proposes $119 million to fund these two programs, a net decrease of $47.6 million from the fiscal year 2005 appropriation. The Lead Demonstration Project accounts for $46.6 million of this decrease. Areas with high incidence of lead poisoning have now developed greater capacity, and therefore activities previously funded under the Demonstration program will be addressed through the regular grant program.

MAKING GOVERNMENT MORE EFFECTIVE

Reforming Community and Economic Development Programs.—The budget proposes a new program within the Department of Commerce to support communities' efforts to meet the goals of improving their economic opportunity and ownership. This initiative will consolidate programs such as Community Development Block Grants into a more targeted, unified program that sets accountability standards in exchange for flexible use of the funds.

Reforming Low-Income Housing Assistance.—Another way in which the fiscal year 2006 budget will make government a better steward of taxpayer money is through reform of the Section 8 Housing Choice Voucher Program.

HUD has three major rental assistance programs that collectively provide rental subsidies to approximately 4.8 million households nationwide. The major vehicle for providing rental subsidies is the Section 8 program, which is authorized in Section 8 of the U.S. Housing Act of 1937. Under this program, HUD provides subsidies to individuals (tenant-based) who seek rental housing from qualified and approved owners, and also provides subsidies directly to private property owners who set aside some or all of their units for low-income families (project-based).

The Housing Choice Voucher Program, the best known of the Section 8 rental assistance programs, provides approximately 2 million low-income families with subsidies to afford decent rental housing in the private market. Generally, participants contribute up to 30 percent of their income towards rent, and the government pays the rest.

In the past, funds have been appropriated for a specific number of vouchers each year. These funds were then given to PHAs based on the number of vouchers they awarded and at whatever costs were incurred.

In 2001, the Housing Certificate Fund, under which both the project-based and tenant-based Section 8 programs are funded, consumed 43 percent of HUD's annual budget. That had risen to 57 percent in fiscal year 2005, and the trend line continues to increase dramatically in the Department's fiscal year 2006 budget. This rate of increase, combined with an extremely complex set of laws and rules that govern the program, has resulted in a program that increasingly is difficult to sustain.

In response to rapidly increasing costs, Congress recently converted this "unit-based" allocation system to a "budget-based" system. This made sense, but for the budget-based system to work, program requirements need to be simplified and PHAs need to be provided with greater flexibility.

The administration proposes to simplify Section 8 and give more flexibility to PHAs to administer the program to better address local needs. Building on changes in the 2005 Consolidated Appropriations Act, the administration will shortly submit authorizing legislation to this committee that expands the "dollar-based" approach.

PHAs will continue to receive a set dollar amount as in 2005, but they would have the freedom to adjust the program to the unique and changing needs of their communities, including the ability to set their own subsidy levels based on local market conditions rather than Washington-determined rents. Local PHAs will be able to design their own tenant rent policies, and in turn, reduce the number of errors that are made and create incentives to work. The administration's plan will eliminate many of the complex forms that are currently required to comply with program rules, saving both time and money. Furthermore, the administration's proposal will reward PHAs for good management through performance-based incentives. These changes would provide a more efficient and effective program, which helps low-income families more easily obtain decent, safe, and affordable housing.

Human Capital.—After many years of downsizing, HUD faces a large number of potential retirements and the loss of experienced staff. HUD's staff, or "human capital," is its most important asset in the delivery and oversight of the Department's mission. HUD has taken significant steps to enhance and better use its existing staff capacity, and to obtain, develop, and maintain the staff capacity necessary to adequately support HUD's future program delivery. HUD has revamped its hiring practices, and now fills jobs in an average of only 38 days, instead of the 96-day average originally cited by the Government Accountability Office. Moreover, HUD has synchronized the goals and performance plans of its managers with the overall aims of the agency, and is developing a new managerial framework through recent hiring and executive training programs.

Competitive Sourcing.—In April, HUD announced its first public-private competition, focusing on the contract administration and compliance monitoring functions associated with its assisted multifamily housing properties. Through this competition and others that are being considered, HUD hopes to realize cost efficiencies and significantly improve performance.

Improved Financial Performance.—HUD has striven to enhance and stabilize its existing financial management systems operating environment to better support the Department and produce auditable financial statements in a timely manner. While still suffering from internal control weaknesses, HUD met the accelerated timetables for producing its performance and accountability report, and improved the reliability, accuracy, and timeliness of financial systems. HUD is continuing efforts to reduce its internal control weaknesses from 10 to 7 by next year.

E-Government.—HUD completed security reviews for all of its information systems in calendar year 2004, and plans are in place to eliminate security defects by next year. HUD awarded its large contract for core IT infrastructure, successfully resolving a protest that lasted for 2 years.

HUD Management and Performance.—Today, public and assisted housing residents live in better quality housing with fewer safety violations than 4 years ago. HUD increased the percentage of projects meeting its physical condition standards in public housing by 9 percentage points (from 83 percent in 2002 to 92 percent in 2004) and in subsidized private housing by 8 percentage points (from 87 percent in 2002 to 95 percent in 2004). HUD now turns around at least 45 percent of public housing authorities classified as "troubled" within 12 months rather than the 2 years allowed by regulation. New rules and procedures have virtually eliminated property flipping fraud from the FHA insurance programs, and close monitoring will continue to prevent such abuses. New rules and procedures have forced out bad appraisers from the FHA program and our "Credit Watch" lender monitoring initiative will continue to bar other individuals who improperly raise the risk of loss in these programs. Since 2002, HUD has worked with stakeholders to streamline their Consolidated Planning process into an easy-to-use and helpful tool for communities.

Faith-Based and Community Initiative.—HUD expanded its outreach to community organizations, including faith-based organizations, attempting to level the playing field for its formula and competitive grants. HUD has removed all discriminatory barriers to participation by such organizations. HUD's technical assistance has helped these organizations understand the application process as well as the responsibilities for implementation. These organizations are beginning to compete more widely and effectively as shown in their success in increasing the number of grants from 659 in 2002 to 765 in 2003, a 16 percent improvement.

Improper Payments Initiative.—At the beginning of the President's first term, HUD committed to working with its stakeholders to reduce the improper payment in rental subsidies by one-half by 2005. At that time, over 60 percent of rental subsidies were incorrectly calculated by program sponsors due to improper interviews, inadequate income verifications, misunderstood program rules, and computational errors. Other errors resulted from inadequate verification of tenants' self-reported incomes. Four years later, HUD has achieved exactly what it committed to do. There has been a 27 percent reduction in improper subsidy determinations by program sponsors over the past 4 years. More importantly, there has been a 50 percent reduction in improper payments amounting to $1.6 billion.

Beginning in 2005, HUD will expand the verification of tenant self-reported incomes to include recent wage data. This has the dual benefit of both improving accuracy and providing more privacy because income data will be matched electronically whereas current procedures require a paper verification letter to the tenant's employer. These stewardship efforts improve confidence that the right person is getting the right benefit in a timely, dignified, and private manner as intended under law. Because this is the first quarter that agency efforts were rated, progress scores were not given.

All of us share the goal of creating housing opportunities for more Americans. We have done great work over the past 4 years, and we should be proud of everything we have accomplished together. But we should not be satisfied, because our work is far from being finished.

I look forward to the work ahead, as we seek to open the American Dream to more families and individuals, and open our communities to new opportunities for growth and prosperity.

I would like to thank all the members of this subcommittee for your support of our efforts at HUD. We welcome your guidance as we continue our work together.

Thank you.

Senator BOND. Thank you very much, Mr. Secretary.

CDBG AUDIT OF PROGRAM ABUSE

Mr. Secretary, you are probably well aware, as we are all too well aware in Missouri, of a recent audit conducted for the City of Kansas City that revealed that a not-for-profit agency has billed for some $1.1 million in Federal housing funds for just two homes on Tracy Avenue. The audit found the contracts may have violated Federal regulations.

As you know, there is great concern in Kansas City over misuse of dollars. I have visited there. I have called on the IG to investigate. I visited the area with HUD officials because we understand that the abuse of taxpayer dollars cannot be tolerated.

While I understand this is an ongoing investigation, I would like to know what you can tell me directly about it and what HUD is doing to prevent possible abuses from happening again as well as your assurance that there will be continued attention to this matter.

Mr. JACKSON. First, Mr. Chairman, I want to thank you for bringing the matter to our attention. We quickly began the process of evaluating exactly what has taken place.

We are in the process of finding out and we will, when it is finished, make our findings to you. We will also take the appropriate action.

As you know, we allocate the funds to the cities and the cities have the responsibility to make sure that there is checks and balances. But that does not in any way relieve us of our responsibility. I take that responsibility greatly.

So I will tell you that, as you know, we sent a General Deputy Assistant Secretary out with you to make the finding——

Senator BOND. Right. We appreciate that.

Mr. JACKSON [continuing]. We will continue to do that. We are going to make every effort to make sure that that does not happen again. I will report to you as soon as we have the final findings.

Senator BOND. Thank you very much, Mr. Secretary.

Is Mr. Ken Donohue, the HUD IG, available?

Mr. JACKSON. Yes.

Senator BOND. Mr. Donohue, could you come up to the microphone. You know I asked you to review the use of CDBG funding as it pertains to the rehabilitation of the two houses on Tracy Avenue. I know that you have been reviewing the city's use and I would like to know what your views are or what you can tell us at this time.

Mr. DONOHUE. Yes, Mr. Chairman. Thank you very much.

As you know, we did conduct a series of audits with regard to the Kansas City housing programs. The most recent being the HEDFC Program.

And I really do appreciate the chairman's interest with regard to the Tracy Avenue project. You agree an expensive amount of rehabilitation was spent on those two single-family homes.

I want to assure you that we are continuing to review this matter and follow-up on your concerns. I can report out to you today that based on these audits, the Department has issued a limited denial of participation on the HEFDC and some of its officials.

This will require the City of Kansas City to assume control of the $50 million to $80 million with regard to the portfolio administered by HEFDC. And I believe the city is currently in negotiations to award a contract.

Senator BOND. We thank you and we look forward to your final report.

When I was there with the representative of Secretary Jackson and the Mayor of Kansas City, the City Manager expressed a strong commitment to take over the administration of the program and to deal with those abuses.

I know there are many more steps, but we appreciate your role in undertaking that.

REVIEW OF HOMELESS ASSISTANCE GRANTS

Mr. Secretary, another, if you will permit me, another parochial interest, very important to the City of St. Louis. I recently sent a letter March 11 asking HUD to review the award of only $4.2 million in homeless assistance grants to the City of St. Louis.

The City was eligible to receive $10.8 million if it scored 82 points on a continuum of care application. It scored 81 points and gets $4.2 million instead of $10.8 million.

This funding is critically important. And I know that there are difficulties in reviewing and sometimes they are subjective.

I would like to know the status and would also like to know what steps HUD takes to ensure the results in the reviews are just, especially when the loss of funds by the narrowest margins is such a large magnitude.

Mr. JACKSON. Mr. Chairman, thank you very much.

We are totally evaluating the allocation. There was a technical mistake. And clearly from my perspective, it deserves us to look again at the process that we used.

I think you said it well. In many cases, yes, we try to be objective, but sometimes it is very subjective.

We hope to have an answer to you very quickly, as I have said, because it is important that St. Louis receive those monies.

Senator BOND. Thank you very much, Mr. Secretary.

Now I turn to Senator Murray.

Senator MURRAY. Thank you, Mr. Chairman.

RESCIND UNOBLIGATED CASH AND CARRY-OVER FUNDS

Mr. Secretary, your fiscal year 2006 budget seeks authority to rescind $2.5 billion in unobligated cash and carry-over funds from fiscal year 2005 and previous years.

Your language allows you to take this funding from any account within HUD. I was not on the subcommittee that funded HUD last year and I am troubled by this practice where you kind of "one hand giveth and the other hand taketh away".

Can you please tell us today precisely which programs you intend to cut in order to achieve your proposed rescission of $2.5 billion?

Mr. JACKSON. Ranking Member, I cannot. And what I will do is in all honesty go back and look at possibilities.

Initially we had said the Section 8 program, but it permitted us to take it from other places within our budget.

I can respond to you for the record and get that to you specifically.

Senator MURRAY. Well, do you think you will be in a position to identify where these cuts are coming from before we mark up this appropriations bill probably in July?

Mr. JACKSON. We have the next 18 months to identify. And usually we will not start that process until June or July.

Senator MURRAY. So when we are marking up the appropriations bill, we will have no idea where you are going to be taking those from?

Mr. JACKSON. I will tell you we will have to in all honesty look at the budget. It is a very, very tight budget that we are operating under and I do not want to give you specifics today and then find out that 6, 7 months from now those are not the specific areas where the rescission will come.

And I am trying to be as straightforward as I can with you. I cannot today give you the specific areas.

Senator MURRAY. Well, I think that makes it really hard for this subcommittee to write a bill when we do not know where you are going to be taking money away from.

A similar rescission totaling $1.5 billion was imposed on this current year. And you do plan to accommodate that rescission, I understand, by recapturing unused voucher funds from Section 8?

Mr. JACKSON. That is correct.

Senator MURRAY. Can you guarantee me that a rescission of $2.5 billion as recommended in your budget will not result in the loss of housing or other essential services to any of our low-income individuals or families served by HUD?

Mr. JACKSON. No, I cannot do that.

Senator MURRAY. So it could possibly come from those?

Mr. JACKSON. Yes.

Senator MURRAY. Well, I understand that many of your grants to actually eliminate homelessness remain unobligated because the grants are not transmitted to the housing agencies until late in the year.

Can you guarantee that none of your proposed $2.5 billion will be derived by limiting available assistance to the homeless?

Mr. JACKSON. Homelessness is an extreme priority for us just like the Section 8 program. I will do everything within my power to make sure that those are not rescinded.

Senator MURRAY. Well, Mr. Secretary, there are very few programs I know of that have such wide bi-partisan support by members of Congress, governors, mayors. We have been flooded by people supporting the Community Development Block Grant.

The administration is planning to merge this program with 17 others and then cut the available funding by more than a third. The rationale that has been presented in the President's budget for consolidating and cutting these programs is that the existing programs are cumbersome, duplicative, ineffective, and unaccountable.

Do you feel that CDBG is unaccountable under your authority?

Mr. JACKSON. Absolutely not. And that is not the basis for the consolidation. What we are saying is to try to get all of the economic development programs in one place.

And I think it would be very hypocritical on my part, having been chairman of two community development agencies, one in St. Louis and one in Washington, DC, and I have seen the effects of those programs which are very positive around the country, specifically in Washington. It has been extremely effective in Seattle and Spokane.

So I think to say that the program has been ineffective—there are problems in the program. There is no question, as just the chairman just said.

But you have to note that once those were brought to our attention by OMB, the thing that I did specifically was to compel people in the profession, the industry, and members of OMB staff to go out and make recommendations how we could better make the program work.

And we came back with those specifics and we have submitted those to your committee and to the Senate and to the House as to how we can better make the program work.

CDBG CONSOLIDATION

Senator MURRAY. Mr. Secretary, in the President's budget, he said that he is consolidating and cutting these existing programs because they are cumbersome, duplicative, ineffective, and unaccountable. Those are the administration's words.

So you are telling me they are not unaccountable?

Mr. JACKSON. I am telling you the Community Development Program is not unaccountable. I am saying to you that the Economic Development Program for consolidation purposes, yes, a number of them exist around six or seven different agencies and they are encumbered because some, I do not think, should be——

Senator MURRAY. Well, what is cumbersome or ineffective? Meals on Wheels, elderly and child day care? What programs that CDBG supports are cumbersome and unaccountable?

Mr. JACKSON. Well, I do not think they are not specifically talking about the Community Development Program. We are talking about the Economic Development Program. We are consolidating for the purpose of economic development.

Senator MURRAY. Well, the administration is planning to merge CDBG with 17 others and then cut that funding by a third. And in the budget itself, the President said the reason he is merging CDBG is because it is unaccountable and duplicative and ineffective.

And so I am just asking you which programs under CDBG? Is it Meals on Wheels? Is it child care? What is it that is cumbersome, unaccountable and ineffective?

Mr. JACKSON. I am saying to you, Ranking Member, that is not my perspective of what the bill says. We are talking about economic development programs, not the Community Development Program per se. And that to me is a very different perspective.

You are asking me their ineffectiveness——

Senator MURRAY. I am just reading the words of the President's budget.

Mr. JACKSON. I understand what you are saying. I am saying to you, are you asking me there is ineffectiveness in the Community Development Program? Yes. I think you have seen one example which the chairman gave. But I'm saying overall, there is a great deal of good that comes from the Community Development Program.

Senator MURRAY. Thanks, Mr. Chairman.

RESCISSION OF $2.5 BILLION FOR FISCAL YEAR 2006

Senator BOND. Thank you, Senator Murray.

Let me go back to this proposed rescission of $2.5 billion. My staff has asked HUD and OMB for justification of the rescission.

Where did you come up with it? I hope that this was not a Professor Swag estimate of $2.5 billion. Is there some kind of analysis that is performed to justify the level of rescission in the budget? There has to be a rationale for a $2.5 billion cut. What is it or where is it or when are we going to get it?

Mr. JACKSON. As I said to the ranking member, Mr. Chairman, we will start the process probably in June or July looking at where the rescissions will occur. To tell you specifically where they will occur, I am not in that position to do that today.

Senator BOND. Well, Mr. Secretary, we understand the House is going to act on all these bills in June. We are going to be acting on them in July. And we need to know what we are buying.

Are we buying a pig in a poke or are we buying a rational plan? At this point, I lean towards the pig. I want to see the plan. And June or July, unfortunately I tell you, is not an adequate time for us to do our work. We have got to have it before we start trying to allocate the headaches that this budget causes us. So, please, we need this by the end of April.

Mr. JACKSON. I will make every effort to get it to you as quickly as possible.

Senator BOND. Thank you. We need it by the end of April.

TRANSFER CDBG PROGRAMS TO COMMERCE

Moving on to the CDBG, I got this wonderful November 20, 2004, consensus document, where a joint HUD, OMB, grantee outcome measurement working group reached consensus on an outcome measurement system to implement the CDBG program. This group spent significant time to make CDBG more effective. I do not understand after we have gone through all this effort to make it work why the administration wants to eliminate CDBG and begin again at Commerce.

But I have got some practical questions. How could a new block grant work even if enacted this year? Even if we were to pass it—and I am going to do my best to make sure we do not—how could the Department of Commerce or any department actually get a new program on track, create regulations, educate grantees, and get the money out the door?

What is going to happen to existing projects? Where does all this go and how does some other agency get a handle on it?

Mr. JACKSON. I think, not passing the buck, Mr. Chairman, I think you are going to have to ask the Secretary of Commerce.

We simply zeroed out $4.5 billion out of our budget for 2006. How it is going to be implemented, what is going to occur, legislation now is being drafted by Commerce to that effect.

And we will have input in that legislation. But that question I cannot answer at this point.

STAFFING REQUEST

Senator BOND. Well, I would look at your staffing request, staffing and salaries. HUD is requesting an increase of $32.5 million over the 2005 level, a total of $1.15 billion for salaries. At the same time, the administration is proposing elimination of CDBG block granting, homeless, Section 8, as well as reduced regulatory requirements over PHAs. Your staffing requests are going up while the OMB budget requests for programs are going down.

How could you need even half that amount if we were to adopt all of the draconian cuts and removals from HUD jurisdiction? What are your true S&E needs were we to enact all these changes?

Mr. JACKSON. Those are our true S&E needs. And I will tell you that we have cut our staff substantially over the last 2 years. And it is because in many cases, we have had an increase in the cost of living, increase in merit salary that in essence requires us to cut the staff but at the same time to meet the criteria.

We feel today that it is very difficult for us to carry out some of our missions without an increase in staff and we are asking, as we have said before, for the increase in staff. And that is what we are projecting within the budget because we have to.

Let me say this to you, Mr. Chairman. When I go out into the field—and I am probably one of the few secretaries that has ever spent any time in the field. I think I have been, of our 81 field offices, I think have been to 53 of them. I have been to every one of our regions.

And when I walk in there and realize that there is not enough personnel within those specific field offices or regional offices to carry out the work, I think it is imperative that I ask not only the administration but also the Congress to give me leeway to make sure that those positions are filled.

Senator BOND. Thank you, Mr. Secretary. We want to see that your programs work. We want to see that the ones that should be in HUD stay in HUD. I know you are going to have to travel to Alaska and the great Northwest but please stop in the Midwest on the way back.

Mr. JACKSON. And I can assure you I am going to stop by Senator Murray's State, too, before I get there or on the way back, one of the two.

Senator BOND. Yes. All right. Well, I will turn the questioning over to Senator Murray now.

Senator MURRAY. We are a stop on the way to Alaska, so it does work.

NEW CDBG FUNDS TO BE SPENT ON HOUSING ACTIVITIES

Mr. Secretary, you are the chief administrator for the Nation's housing needs. So can you tell me what percentage of the Bush Administration's new Consolidated Block Grant Program will be spent on housing activities?

Mr. JACKSON. No, I cannot. I think again until the legislation is developed by Commerce, I cannot.

I can tell you 2005, $4.5 billion.

Senator MURRAY. We have not gotten any authorizing legislation yet. You say that is going to be developed by the Department of Commerce?

Mr. JACKSON. Yes.

Senator MURRAY. And that you would not have any say in that at all?

Mr. JACKSON. No. We will have input in it, yes.

Senator MURRAY. So you will have input?

Mr. JACKSON. Yes.

Senator MURRAY. So I will assume you will advocate for housing needs?

Mr. JACKSON. Absolutely.

Senator MURRAY. And you know that roughly a quarter of CDBG funds today are used for housing. What would you advocate for under the new——

Mr. JACKSON. Again, I will tell you that, as I said a few minutes ago to you, I am convinced that the Community Development Block Grant Program has some ineffectiveness. But as a whole, it is a very excellent program that has done a lot for cities in this country.

So I will continue to advocate the flexibility and that as much money as can be appropriated be appropriated for housing and community development, that is infrastructure, development zones.

Senator MURRAY. As this authorizing legislation is put together and you are advocating to the Department of Commerce, what programs will you tell them should not be cut or what current uses under CDBG will you tell them have to remain as part of authorizing legislation? What do you think is important?

Mr. JACKSON. I think all of it is important.

Senator MURRAY. So you are not going to tell them that anything is not eligible anymore? Everything will still be eligible? Is that what you——

Mr. JACKSON. I think that we have sent over to Congress some suggestions and that is for a proposal as to how we can best redistribute the Community Development Block Grant fund on an equity basis. That is for you all to decide.

We did not make a recommendation because we thought that clearly that was not within our purview. And let me tell you why we did that. It is because there are some inequities that exist within the program.

Once OMB did the pilot study for us, we said let us look at this and make the best recommendation to Congress that we can make. As a whole, I think we have done that. We have also made recommendations how to best administer the program.

So when you start looking at the program, it is a very difficult process to say what should or should not be cut. In my perspective, all of those programs are very important.

Senator MURRAY. So everything that is currently eligible for use under CDBG you believe will still be eligible for——

Mr. JACKSON. I will truly advocate that they should be.

Senator MURRAY. So we are going to take CDBG, combine it with 17 other programs, and then cut the funding by a third and everything is still eligible?

Mr. JACKSON. My position is—again, I will go back. We reduced our budget by $4.5 billion. How that is going to play out in Commerce, I do not have the legislation before me. And once we have input in the process, I will tell them what I think is very important.

Senator MURRAY. But you cannot give us any programs? Meals on Wheels, do you think that is affected? Child care? Elderly care?

Mr. JACKSON. Yes.

Senator MURRAY. It is going to be tough, Mr. Chairman. I am looking forward to seeing the administration's proposal.

All right. Well, let me ask one more question in my time then.

FOSTER CARE HOUSING

Mr. Secretary, there are some studies out there indicating that the primary reason why as many as 30 percent of our children who are in foster care today cannot be reunited with one or both of their parents is because they do not have adequate housing.

These are the cases where a parent has gotten over their substance abuse problems, fulfilled other requirements, and the judge is ready and prepared to reunite the kids with their parents as long as they find adequate housing.

Now, the average welfare family has 2.7 children and the cost to the taxpayer of keeping those kids in foster care is about $48,000 a year. Your agency, however, provides housing for families of this kind for a subsidy of about $13,500 a year.

Do you not think it makes more sense both for the families and for the taxpayer to make an aggressive effort to find housing for this population so kids can get out of foster care and be reunited with their parents?

Mr. JACKSON. I surely do. And let me tell you that that is why we have increased the homeless budget by $1.4 billion, but we have also created the Interagency on Homeless where we have four agencies working together to deal with the homeless problem from a holistic point of view, but from a whole perspective.

I had a chance about 5 weeks ago to be out in California with Governor Schwarzenegger to see a program called Path that is doing exactly what the President has set forth.

It starts with the person who has been on the streets or family that has been on the streets more than 90 days. And they start with basically looking at them from a physical, mental, and medical perspective, then training them for job training and putting them through.

So I totally agree with you that it is much cheaper and much more productive to house them the way you have said with our program than to keep a child in foster care.

Senator MURRAY. Okay. I understand that the Tenant Protective Fund has a special designated program just for family reunification. In fact, I believe Senator Bond was instrumental in getting that program authorized.

Mr. JACKSON. That is correct.

NEW VOUCHERS FOR THE TENANT PROTECTIVE FUND

Senator MURRAY. But I also understand that no new vouchers have been issued for that program for the last 4 years and I just want to know why your agency has not issued any new vouchers to get some of those families reunited.

Mr. JACKSON. We are issuing the vouchers. And let me say this to you. Most housing—well, not most—all housing authorities realize that the homeless families take priority on their waiting list.

If we can find or if you can denote to me those that are not doing that, I will be happy to speak with them. But that is a top priority of every housing authority in this country.

Senator MURRAY. Well, I understand you are issuing renewals, but you are not issuing any new vouchers. And I have heard that that is because you want to leave that funding available for your rescissions. Is that correct?

Mr. JACKSON. That is not true.

Senator MURRAY. Okay. So why have no new vouchers been issued?

Mr. JACKSON. We do not have new vouchers to actually issue at this point. I mean, we have funded the program and the new Section 8 voucher program by $1.1 billion increase.

What is occurring is this, and we are going to have to deal with this, is that pre-1998, housing authorities received a budget base amount of money. And I can tell you because I am probably the only Secretary ever to appear before you have ran a housing authority.

In Dallas, we got $20 million as an example and we housed as many people as we could. Today it is unit-based. Well, we just moved away from the unit-based. But it was unit-based.

And what occurred is this. With the unit-based, we also put another appendage to it that 75 percent of those vouchers must be used for people 30 percent or less of median.

What that created was a symptomatic problem. When we did that, 90 percent or over 90 percent of those people do not pay anything to live. In fact, we pay them to live in subsidized housing. We pay their utilities. We pay their expenses.

So what we have seen is the Section 8 budget rise exponentially, but we are not housing any more people. If I go back to 1995, when I left the Housing Authority in Dallas, I will bet you that today that 60 percent of the people who were on that waiting list are still there today.

Senator MURRAY. That is right because housing prices have increased.

Mr. JACKSON. No, they have not. They have increased in your area. They have increased on the east coast. But west, southeast, the housing costs for apartments have gone down. But, yet, we are paying extremely high prices because the unit-based system has protected landlords to charge what they wanted just to get a person in.

I think competitively, once we go back to a system where people are paying, I think we will have a different situation. That is why we have suggested that we raise the limit to 60 percent of median where we do have people.

Pre-1998, a person spent about 3.5 years on a voucher.

Senator MURRAY. Are you going to protect areas that have higher housing costs?

Mr. JACKSON. Today they're spending 8.

Senator MURRAY. Are you going to protect areas like the Northwest and Northeast that——

Mr. JACKSON. Absolutely. And I think that that flexibility in the flexible voucher program gives the housing authority with a budget-based process and the flexibility they have to decide what they want to pay for a voucher.

Senator MURRAY. My time is up.

Senator BOND. Thank you, Senator Murray.

HOPE VI

I am going to try to wrap up my questions on this round. Obviously as you might expect, I have an extensive question on the HOPE VI rescission since I spent so long working to get it established and know how it works.

I am going to give you some time and maybe somebody at OMB can help you write a rationale of why you are trying to not only gut it but also rescind prior year funding.

IMPACT OF THE BUDGET-BASED SECTION 8 VOUCHER PROGRAM

Let me move to the Section 8 vouchers. You know, we work with you and I think we reformed the Section 8 voucher program as a budget-based program by requiring HUD to allocate funds by a budget-based formula. Unfortunately, we have not been able to get the data for the 2005 bill to make sure we included enough funding. We did the best we could, but I would like to ask you what is the impact of the approach? Are the number of vouchers going to decrease from the high point? What is HUD doing to ensure that PHAs are providing better data? Are they lowering payment standards and what has been the impact of this new budget-based program for Section 8 tenants?

Mr. JACKSON. I welcome that question and let me tell you why, Mr. Chairman, because I think we have not held the public housing authorities accountable in the unit-based system.

I do believe that the passage of the budget-based program last year, if with the passage of the flexibility this year, will give housing authorities the abilities to house more people and to have a tremendous turnover.

I think we have to look at the basis for the Section 8 program. And I think over the years, we have lost that perspective and I am not talking about the Congress. I am talking about the housing authorities.

The Section 8 program was created as a transition between public housing and conventional housing. And when I say that, I mean whether it is affordable rental property or home ownership.

We have, over the last 15 years, made it a substitute for public housing. And since 1998, we have made it basically public housing in many ways when we said only 30 percent or less must get 75 percent of the vouchers.

To me, there are still people in this country at 60 percent of median who can use a voucher for a period of time. Pre-1998, we spent about 3 years with the voucher, 3.5 years. Since 1998, it has gone to about 8 years.

But the key to it is that we are not serving any more people. We are serving the lowest of the lowest and we have planned projected prices that clearly should not be paid in many parts of the country.

That is not in Senator Murray's area in the West Coast or in the East Coast. Maine, Massachusetts, yes, those are very high markets. But in the Southeast, the South, and the Southwest, the markets are not that high. In the Midwest, the markets are not that high. We have ample rental apartments, but still we are paying this unit-based cost.

So my contention is, Senator, if we can pass the flexible part of the Voucher Program now that it is already budget based, we can begin to house more people and they will not be on the program as long.

NEGOTIATED RULE-MAKING

Senator BOND. I raised concern earlier about the public housing negotiated rule-making. The negotiated rule was based on a study conducted by the Harvard University Graduate School of Design. Unfortunately, the OMB-revised rule appears to deviate significantly from the negotiated rule. Is not this revision, substantial revision a violation of the negotiated rule-making process which we are required by statute?

Mr. JACKSON. I had a meeting yesterday with the leadership of the three major entities that represent housing authorities. That is the Council on Large Housing Authorities, five of the Public Housing Authority directors, Ann Clap of the Council on Large Housing Authorities. They perceived that it is.

We think that we were very candid with them in our process of negotiation when we said that there is always possibilities that there will be changes. During the comment period, you will have a chance to make your wishes known.

We think that probably 85, 90 percent of what we negotiated is within the rule today. Were there changes? Yes. Will they have a chance to make sure that their voices are heard? Absolutely. Are the housing authorities losing? Yes.

But the majority of the housing authorities are gaining under the present negotiated rules, Chairman Bond. And, you know, we think 80, 85 percent of them are gaining. Will we ever get 100 percent? No.

But we believe—and we are open, as I told all three of the representatives yesterday, to listening to them and to go back and see if there is some efforts we can make to correct some of the concerns that they have.

FHA MORTGAGE INSURANCE

Senator BOND. One final question is going to be on FHA mortgage insurance. And I would invite Mr. Donohue to come back up to the table and just give us a quick summary of what is happening with the increasing FHA defaults and what is your assessment of the Zero Downpayment program based on the audits you have conducted on the FHA mortgage insurance program.

Mr. DONOHUE. We have done substantial work as far as audits with regard to the FHA default and we concur with the spiked increase of defaults in the past few years. I believe you quoted 6.9 percent for 2004.

I believe in our review, the zero down payment or no out-of-pocket money for the recipient has inherent problems that can impact on the FHA funds even though I know FHA is increasing the premium amounts, but I do think that this could have an impact on the function and operation of FHA.

Senator BOND. Mr. Secretary, home ownership is at an all-time high, 73.7 homeowners. However, some people are not ready for home ownership.

Mr. JACKSON. That is correct.

ZERO DOWNPAYMENT ACT

Senator BOND. Why should we take the risk to the FHA fund when it appears that the only way you can reach out is to provide people no-cost housing which we have seen unfortunately leads to defaults? And it is not only disastrous for the community but disastrous for the credit history and the reputation of the families who get this so-called benefit.

Mr. JACKSON. Mr. Chairman, FHA claims are down 15 percent from last year. And why I think it is necessary, I will tell you. Again—and I do not say this for advisement. I am probably the most traveled Secretary to the persons that we serve.

I would just like to use an example of a family that I met in Las Vegas, the Gonzaleses, who came to this country, I think, some 20 years ago. The wife works in the hotel, but she works in the maid service. The husband works in the kitchen of another major hotel.

Together they make about $40,000 each. I believe that the most difficult things that they said to me with them is the ability to make the down payment and closing costs. They are paying about 42, 43 percent of their money for rent.

If we can get them into a home, I am convinced in my heart that they are going to stay in that home. They will probably be paying about 30 percent of their income for rent.

See, I believe this. I will not call the name of my friend because if I call him, you and I will both know him. But I have a friend who is a major doctor who has defaulted on two homes and both of them were zero down payments. He still has another million dollar home with a zero down payment.

I believe that if we can give low-and moderate-income persons the same opportunities, we will not have a huge default rate. I believe we should give them that opportunity.

And, you know, I will just close with this, something that my mother used to say, and this is why I stress home ownership a lot but also affordable housing. To live with a dream might be madness, but to live without a dream is insanity.

There are a lot of people who want home ownership. I think if we can help them through what the President has put forth with the American Dreams Down Payment Act and Zero Downpayment Act a number of people who would not have the opportunity to be homeowners will be.

Senator BOND. I appreciate your explanation. But when you look at what happens, I am afraid that is a path for a lot of hardship for communities and families.

Senator Murray.

FARM LABOR HOUSING

Senator MURRAY. Thank you. I just have a couple more questions and I will submit some. I have some more on HOPE VI too.

But I wanted to ask you about a significant need across the country and my home State and that is for seasonable and permanent farm labor housing.

I am aware of the assistance of the Department of Labor and Agriculture in this area as well, but it really is not enough to meet the needs out there.

Can you talk to us about what HUD's current authority is and activities related to farm labor housing and do you think your agency is doing everything it can in that area?

Mr. JACKSON. I am just not sure. I have to ask the Assistant Secretary Weicher.

Mr. WEICHER. I am sorry, Senator Murray. We do not have responsibility for——

Mr. JACKSON. I did not think so.

Mr. WEICHER [continuing]. Lending. We do not have the responsibility for the Rural Housing programs and the Old Farmer's Home Administration. We can make loans in rural areas and we do, but those are separate programs.

Senator MURRAY. So you do nothing for farm labor housing?

Mr. WEICHER. I beg your pardon?

Senator MURRAY. You know, I notice that you talked a lot about homelessness and I know that the President reactivated the U.S. Interagency Council on Homelessness so cabinet-level leaders can work together on that problem.

The farm labor community is one of the most poorly-housed populations in the Nation and the only government solutions really are spread out over three different departments.

Mr. Secretary, you are the lead national official for the Nation's housing needs and farm labor housing is one of those.

Would you see any merit in convening a cabinet-level working group to address farm labor housing and would you be willing to work with me on this?

Mr. JACKSON. Absolutely.

Senator MURRAY. Well, I would like to——

Senator BOND. Senator Murray, excuse me. I have been summoned back to my office and if you don't mind, I will give you the——

Senator MURRAY. Great.

Senator BOND. I thought you might just like a little bit of practice in case. So with that——

Senator MURRAY. Senator Leahy and I will be more than——

Senator BOND [continuing]. I thank you, Mr. Secretary, for your noble efforts to answer some unanswerable questions. I intend to ask others the same questions.

And, Senator Leahy, you can continue with Senator Murray.

Senator MURRAY [presiding]. I just have one additional question——

Mr. JACKSON. Thank you, Mr. Chairman.

Senator MURRAY [continuing]. And I will turn it over to Senator Leahy. But thank you, Mr. Chairman.

Mr. Secretary, I have one other question. I do want to follow up the farm labor housing with you. It is a critical housing issue and we have not done enough. We need to do more and I want to work with you on that.

ERROR IN DISTRIBUTION OF SECTION 8 FUNDS

But let me ask you one other question. I recently heard from King County Public Housing Authority. It is one of the largest public housing authorities in my State. And they tell me that as a result of a computing error that was executed by HUD in the distribution of Section 8 funds, they are enduring a loss of $800,000 this year.

And I am told that HUD staff admitted to them that this was done in error, but HUD is also telling them they now do not have the money to rectify that error, their error.

As a result, this agency is contemplating sending out a letter to all the families on their waiting list explaining that as a result of those losses, they are going to be terminating that waiting list since no families on the waiting list will have any hope of getting a housing voucher at any time in the future.

There are currently 5,000 seniors, disabled people, single parents, and refugees who are on that waiting list who are about to get that notice because of an error made by HUD.

Are you familiar with this situation?

Mr. JACKSON. Yes.

Senator MURRAY. Well, I would appreciate your response then today on what——

Mr. JACKSON. We are resolving that situation and it should be resolved immediately with the King County Housing Authority.

Senator MURRAY. And will we be getting a phone call today regarding that?

Mr. JACKSON. I cannot say today, but Assistant Secretary Liu has been in contact with the executive director there.

Senator MURRAY. Well, as of last night, they had not heard anything. Can we have someone call us today——

Mr. JACKSON. I surely will if they have not.

Senator MURRAY [continuing]. And let us know when that phone call is going to be made and how that will be rectified?

Mr. JACKSON. I sure will, Senator.

Senator MURRAY. Thank you very much.

Senator Leahy.

STATEMENT OF SENATOR PATRICK J. LEAHY

Senator LEAHY. Thank you. Thank you, Senator Murray.

Secretary Jackson, I would like to welcome you, in your first appearance before our newly reconstituted and renamed subcommittee. Sometimes it is hard to keep track of all the name changes.

I see some familiar faces here, of course, Senator Bond, who just stepped out, and Senator Murray, two people with a great deal of experience.

So I am looking forward to working with all of you as we tackle this new bill in the upcoming fiscal year.

This is my first hearing as a member of the subcommittee, although I have been on the full committee for nearly 30 years. I wish we could start on a more positive note.

But if we look at the President's proposed budget, it calls for a total of 12 percent in cuts to housing and community development programs. Some days I wish our housing and community development programs were treated with the same expanding budget as they are if they are in Baghdad or somewhere in Iraq and not here in the United States.

ELIMINATION OF CDBG PROGRAM

Most egregious I find is the complete elimination of the Community Development Block Grant programs. I know that has been raised this morning, but I have got a couple of questions on it.

And I am not suggesting it is an either/or thing with Iraq, but we do fall over ourselves to increase, for example, law enforcement money for Iraq at the same time we eliminate the Cops program here in the United States.

We work to increase housing in Iraq, we cut it here. We increase some of the educational funds for Iraq, we cut it here in the United States.

And after a while, people are justified in asking do we have to be an either/or as a great nation?

CDBG is the largest program up for elimination. And the President says he calls it a Strengthening America's Communities Initiative, some of us however call it the Abandoning America's Communities initiative.

Under the proposal, 18 community and economic development programs would be abolished. A new block grant program will be established at the Department of Commerce.

Now, I see no specifics in the goals of this program. We have no information on how the money is going to be allocated. We have no information on what activities will be eligible. We do know however that it is going to be $2 billion less than was spent last year in community and economic development.

And considering the fact that your agency, Secretary Jackson, is principally responsible for housing and community development, why would you agree to turn this over to the Department of Commerce? They have no experience in this field.

Your department has decades of experience. You have superb professionals at HUD, from both Democratic and Republication administrations. Commerce has none of that expertise.

How do you justify this?

Mr. JACKSON. Senator, as I said before the House Committee, we made what we perceived as a logical argument as to where the Economic Development Program should be housed, that is the Strengthening America's Community Initiative Program. The decision was made that it would go to Commerce.

We are in full agreement that the economic and development programs from those 17, 18 departments should be consolidated. We felt that we could do the job at Housing. But Commerce also had an economic and development program.

And the decision was made and I fully support the consolidation. I will tell you that right now of those programs.

Senator LEAHY. Does this not eliminate community development as part of HUD's core mission?

Mr. JACKSON. We have zeroed out $4.5 billion that was allocated for the Community Development Program. We still have the HOME program and other programs that were under the community development——

Senator LEAHY. If you have got 37 percent less money, how are you going to do it?

Mr. JACKSON. Senator, as I said to the Ranking Member Murray, we zeroed out $4.5 billion out of our budget. I cannot comment on what the budget will look like or what the programs will look like at Commerce.

What I said to her is that we will use our vast experience in giving advice to Commerce as to what we think is very important with the Community Development Program.

Senator LEAHY. Do not hold your breath waiting for them to take that advice because basically they cut the money, they got rid of HUD's core mission, and handed it over to somebody who has no experience.

The budgets for HUD when they've come up here over the years have been littered with bullet holes. One year, it is Section 8. Next it is Public Housing. Next it is CDBG.

It appears to me that the administration just abandoned HUD. Obviously you feel differently. Your testimony says you feel differently. But it is awfully hard to see it otherwise.

ADDITIONAL COMMITTEE QUESTIONS

Thank you, Senator Murray. If I have other questions, I will submit them for the record.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

QUESTIONS SUBMITTED BY SENATOR ARLEN SPECTER

CDBG AND LOCAL COMMUNITY SUPPORT

Question. The President's fiscal year 2006 Budget proposes to consolidate 18 economic development programs, including HUD's CDBG program, into one program within the Department of Commerce. In fiscal year 2005, the CDBG program was allocated $4.11 billion. However, the President's fiscal year 2006 Budget would provide only $3.7 billion for the consolidated initiative, which includes all 18 programs. I have heard from many Pennsylvania communities that the CDBG program provides critical funding to support many community development activities such as housing rehabilitation, public facilities, public services and economic development.

With the elimination of the CDBG program—the largest source of Federal assistance to State and local governments for community and economic development projects, how do you propose to work with local communities to continue to meet HUD's mission to support community development and address the housing needs of society's most vulnerable?

Answer. HUD will continue to administer all its housing and homeless assistance programs that provide much needed assistance in accordance with HUD's mission. The new program, Strengthening America's Communities Initiatives (SACI), at the Department of Commerce will also address community and economic development needs in a productive and targeted manner.

HOPE VI

Question. HOPE VI enhances communities by decentralizing poverty and giving families an opportunity to live in mixed-income neighborhoods with better educational and employment opportunities. I have visited HOPE VI sites throughout Pennsylvania and have discovered the critical impact that reconstruction in these public housing developments has on revitalizing neighborhoods. In the past, HUD officials have cited problems with the slow pace of HOPE VI reconstruction and high costs, in comparison to other HUD programs. However, I have often heard from my constituents that delays of HOPE VI projects were linked to HUD's approval process. Can you respond to the concerns raised by my constituents that delays in HOPE VI projects were often the result of HUD policies?

Answer. Since its inception as a demonstration program, HOPE VI has pursued the ambitious and complex goal of revitalizing the Nation's most severely distressed public housing developments. In pursuit of this objective over the last 12 years, the program has evolved significantly in its structure, methodology, and administration, offering an unprecedented learning opportunity for HUD and HOPE VI grantees.

As the program evolved, the mixed-finance development approach was incorporated into the HOPE VI program. In accordance with 24 CFR 941, subpart 6, which controls such development, the Department has been reviewing the PHAs' development proposal and legal documents for each construction phase in each HOPE VI grant. Due to the size of the HOPE VI grants, combined with other leverage funds that the PHAs have obtained, each grant may be broken out into 5 or 6 construction phases, resulting in a complex, and potentially time-intensive review process. Despite the complexity of the mixed-finance approach, the time it takes to complete construction has actually decreased significantly over the life of the HOPE VI program. Where the average grant completion time was 8 years HUD is endeavoring to lower that average to 4½ years.

This reduction in time is due to the heightened emphasis HUD continues to place on meeting deadlines and completing HOPE VI developments. Earlier in the HOPE VI Program, grantees were having difficulty constructing the required housing units in accordance with their original production schedules. HUD made significant strides to improve its oversight of HOPE VI grantees and management of the HOPE VI program between 2001 and 2004 in an effort to increase unit production and decrease delays in completing HOPE VI developments. These changes resulted in a shift from oversight and management approaches that included fluid production deadlines and expectations to a more balanced approach that makes HOPE VI grantees and HUD staff accountable for the progress of HOPE VI projects. Although grantees have clearly grown in capacity since the inception of the program, HUD's attention to deadlines and timely completion of developments has forced grantees to adhere to schedules and complete projects as planned. In turn, HUD continues to work internally to minimize the time necessary for review and approval by developing model documents, waiver opportunities and other streamlining procedures.

Question. Additionally, as HOPE VI has accomplished one of its goals of demolishing 100,000 units—which suggests to me that the program has been effective—how does HUD propose to accomplish this level of reconstruction in the future if HOPE VI is eliminated?

Answer. Rather than funding new rounds of HOPE VI grantees in fiscal year 2006, the Department believes that it is more responsible for the Department to aggressively manage and complete the grants currently awarded, many of which are years from completion. This pause will also give the Department time to continue to develop better methods for assessing distress, develop new financing tools and delivery mechanisms that are less costly and more efficient, and explore the need for a new public housing revitalization program that is designed to address the scope of severe distress present in today's public housing inventory.

The Department recognizes the importance of addressing the current capital backlog within the public housing inventory. In most cases, this need can be more appropriately met through other modernization and development programs operated by the Department e.g., the Capital Fund, Capital Fund Financing Program and Mixed-Finance development. The Department continues to encourage housing authorities in need of this assistance to submit project proposals to these programs. To date, the Department has approved over $2.4 billion in transactions using the Capital Fund Financing Program, with approximately $94 million in additional funds in the pipeline. Of the approved transactions, over $254 million will be used for development activities.

MOVING-TO-WORK

Question. Moving-To-Work (MTW) has enabled public housing authorities to implement federally-funded housing programs based on local needs by providing budget flexibility and regulatory relief. On December 15, 2005, I, along with 11 Senators, sent you a letter supporting the extension of MTW agreements to 2011 for public housing authorities that request an extension of their current demonstration term. We have received your response and understand that participants whose agreements are expiring in 2005 will be offered a 1-year extension. While we thank you for your response and the 1-year extension, could you please clarify why some public housing authorities initially received MTW extensions through 2011?

Answer. No housing authorities have received an extension to continue their MTW demonstration until 2011. Agreements for three of the demonstration participants have expiration dates that far out. Oakland and Baltimore only recently executed their agreements and were given the now standard 7-year term. Their Agreements expire in 2011 and 2012 respectively. Due the complexities of Chicago's Transformation Plan, their initial Agreement provided for a 10-year demonstration term, which expires in 2011.

Question. You also stated in your letter that HUD is currently examining potential legislation to determine if a successor program to MTW would be useful. Why is HUD examining this possibility, rather than expanding the current MTW program?

Answer. The examination of the MTW Demonstration and the overwhelming support it has received has led to the proposed legislation embodied in Title III of the State and Local Housing Flexibility Act of 2005. Title III would expand the program to allow even more Housing Authorities to participate. It would also establish a permanent program that includes features derived from the MTW Demonstration: the fungibility of programs, and flexibility to develop different approaches to providing housing assistance. At the same time, the proposal corrects some of the difficulties in the Demonstration that made it difficult to administer and to measure. These include requirements for uniform reporting and provision of uniform evaluation measures.

OPERATING FUND

Question. The Quality Housing and Work Responsibility Act of 1998 requires that HUD develop a formula for allocation of Public Housing Operating subsidies through a negotiated rule making process that includes the active participation and consensus of stakeholders. In 2000, Congress further directed HUD, in conjunction with the Harvard University Graduate School of Design, to conduct a study of the cost of operating a well-run public housing authority. It is my understanding that following completion of the cost study that HUD worked through a negotiated rule making process to develop a consensus with public housing authorities, private housing professionals and affordable housing advocates on the amount of subsidies, as well as transitional costs to implement the rule. I am gravely concerned that public housing authorities throughout Pennsylvania have contacted me recently asserting that the published rule alters this negotiated agreement reached on a consensus basis. Could you please provide me with an in-depth explanation of why HUD made changes to the negotiated funding rule prior to publication?

Answer. Consistent with requirements under Executive Order 12866 entitled "Regulatory Planning and Review" and other rulemaking authorities, the negotiated rule underwent further HUD and Executive Branch review prior to publication. As a result, certain of the committee's recommendations were revised to better reflect the administration's policies and budgetary priorities. Although changes were made to certain of the committee's recommendations, the proposed rule stays committed to the Harvard Cost Study and Negotiated Rulemaking recommendations.

Question. Additionally, HUD's fiscal year 2006 Budget proposal was developed after the conclusion of meetings conducted as part of the negotiated rulemaking process. Does your budget request accurately reflect the funding necessary to implement the negotiated rule, including transitional costs?

Answer. The 2006 request of $3.4 billion represents approximately 89 percent of operating subsidy PHAs that are eligible under the proposed Operating Fund Rule. The proposed rule retains the Negotiated Rulemaking recommendation for a transition policy of up to 5 years to allow time for PHAs to align their resources with the new funding. The proposed rule provides PHAs with tools to convert to new asset management by providing monthly fees beyond the Harvard cost study for information technology, asset management, and asset repositioning. The proposed rule also provides PHAs with the ability to maximize other revenues streams without receiving an offset in subsidy. PHAs currently have approximately $2.8 billion in operating reserves that they can use for transition costs.

Questions Submitted by Senator Pete V. Domenici

COMMUNITY DEVELOPMENT BLOCK GRANTS

Question. The President proposes a reorganization of economic and community development programs by consolidating them in the Department of Commerce. This consolidation includes taking the CDBG program out of HUD and transferring it to the Department of Commerce.

Eighteen programs from 5 agencies are involved in the proposed consolidation. The administration requests $3.7 billion for the new "Strengthening America's Communities Grant Program." These programs are currently funded at $5.3 billion, so the proposed consolidation comes with a reduction in funding of $1.6 billion below the current level. By far the largest program in the proposal is the CDBG program, which currently receives about $4.7 billion. The administration knows Congress will not approve the proposed restructuring of economic and community development programs. We have seen proposals such as this from previous administrations. However, the proposed funding reduction will have a significant impact on the ability of the Appropriations Committee to support ongoing programs in the fiscal year 2006 spending bills. Mr. Secretary, is your department working on actual legislative language to reorganize the economic and community development programs of the Federal Government?

Answer. The Department of Commerce has the lead on developing the legislative package to implement the Strengthening America's Communities Initiative (SACI). HUD has provided consultative support.

Question. If your department isn't doing so, is another department or agency within the administration working on such legislation?

Answer. The Department of Commerce has the lead on developing the legislative package to implement the Strengthening America's Communities Initiative (SACI). As stated, HUD has provided consultative support.

Question. Do you anticipate that the administration will actually submit such legislation to the Congress?

Answer. HUD is advised that the Department of Commerce is developing legislation that will be submitted to Congress.

Question. Since Congress has no intention of approving the proposed reorganization, what impact do you anticipate your Department to experience when Congress has to reduce ongoing programs by $1.6 billion to stay within the overall discretionary spending gap proposed by the President?

Answer. It is important to note that overall funding for 35 Federal community and economic development programs is only reduced 4 percent, roughly in line with other domestic spending. The President, via his 2006 Budget, has proposed to consolidate 18 programs (from five agencies) within the Department of Commerce, including the CDBG Program. These programs would be consolidated into one new program—The Strengthening America's Communities Initiative. This initiative would support communities' efforts to meet the goal of improving their economic conditions through, among other things, the creation of jobs.

Question. Are you concerned about this eventuality?

Answer. As you know, CDBG funds are distributed according to statutory formula. If CDBG funds are significantly reduced, we are still required to distribute them according to the law. Nevertheless, HUD employees remain committed to the goals of promoting economic opportunity through community revitalization, home ownership, servicing society's most vulnerable—homeless individuals and families—and ending chronic homelessness.

QUESTIONS SUBMITTED BY SENATOR PATTY MURRAY

CDBG TRANSFER

Question. The administration has stated publicly that so-called affluent communities should not receive assistance from its new smaller substitute community development program. What will this mean for communities that might be comparatively affluent but still have significant pockets of poverty in their service area?

Answer. It is important that Federal funds for housing and community development be distributed in a way that maximizes their impact. In general, affluent communities possess the resources and tax base to provide services to their pockets of poverty, while distressed communities often lack adequate tax bases. While the distribution of funds cannot be changed without authorizing legislation, HUD will continue to examine certain policies and/or regulatory issues that would improve the program's effectiveness. For example, HUD's recently released CDBG formula study identified four distinct alternatives to the current formula, but Congress could opt for a variety of other approaches that HUD, or a new program, would implement. A policy review of this nature could provide an extensive menu of options for changing the allocation of Federal community and economic development funds. Further, CDBG grantees continue to express a need for HUD to provide technical assistance that would help improve grantee performance.

Question. Will they be blocked from participating in your smaller substitute community development program?

Answer. According to the Department of Commerce, the final number of communities that receive funding will depend on eligibility criteria, but the administration believes that funding should be targeted to those communities most in need. This will provide a greater level of funding to many communities than they currently receive. According to the Department of Commerce, for example, by funding only communities with poverty rates above 10 percent, approximately 700 communities and 50 States could receive funding that is higher than their fiscal year 2005 CDBG funding levels.

Question. A great many communities across the Nation build low income housing through the Section 108 loan guarantee program. With HUD's approval, they obtained a loan guarantee by pledging their future year CDBG funds. What would become of this Section 108 loan guarantee commitments if the CDBG program were eliminated?

Answer. The fiscal year 2006 Budget proposes to eliminate the Section 108 Loan Guarantee Program. However, we believe that existing Section 108 funded activities will continue to be viable because of other collateral that was pledged before the loan was approved.

Question. Will HUD still expect the communities to pay off these guarantees after you have gone ahead and eliminated the CDBG program?

Answer. Communities will continue to have obligations for Section 108 loan guarantee repayment. In some cases, communities may need assistance in meeting their obligations. This is being taken into consideration as part of the development of the Strengthening America's Communities Initiative (SACI) legislation.

CAPITAL NEEDS OF PUBLIC HOUSING

Question. Mr. Secretary, the most recent study of the capital needs of public housing was published in 1998. That study, which was financed by HUD, estimated that there was an estimated capital needs backlog of $22.5 billion. The study also found that an additional $2 billion in needs was likely to accrue each year thereafter.

Your budget asks us to cut the Capital grant program by a quarter of a billion dollars. You also want us to rescind almost $150 million in dollars already appropriated for the HOPE VI program and zero out the program next year.

Mr. Secretary, I understand that, in a hearing before the House Financial Services Committee last month, you stated that the capital backlog has been reduced to $18 billion over the last 4 years.

How is it that the capital backlog has been reduced by $4.5 billion when funding for all your capital programs have barely kept pace with the level of accruing deterioration each year?

Answer. The administration's proposed budget provides sufficient funds to cover the accrual needs of Public Housing Authorities (PHAs). HUD commissioned a study of the capital needs of PHAs, which was released in 1998. That study identified an annual accrual of capital needs of approximately $2 billion per year, as well as a backlog of capital needs. The administration's proposed budget would provide Capital Fund Program (CFP) monies in excess of the annual accrual need, allowing

PHAs to meet their accrual capital needs, as well as enabling them to address some of their backlog capital needs.

Further, activities such as the demolition and disposition of public housing projects have resulted in the demolition of more than 100,000 units of public housing since the preparation of the capital needs report in 1998. The vast majority of these units were distressed and therefore were the most expensive to maintain. This reduction in the number of public housing units has served to reduce both the backlog of physical needs as well as the annual accrual. It should also be noted that replacement units added to the inventory since the preparation of the report are new and therefore less expensive to maintain.

In addition to annual appropriations PHAs now are able to access the private financial markets and unlock the value of their portfolios. HUD has been implementing the Capital Fund Financing Program (CFFP), which was authorized under the Quality Housing and Work Responsibility Act of 1998 (QHWRA). Through the CFFP, PHAs leverage funds from the private market via a pledge of their future CFP grants. HUD has approved CFFP Proposals in excess of over $2.4 billion, involving over 102 PHAs in more than 40 transactions. Funds derived from the CFFP have enabled PHA's participating in the program to address a significant amount of backlog physical needs.

In the future, HUD looks forward to expanding the CFFP to permit PHAs to use the Federal Public Housing Operating Fund in the same manner, and expand the use of mortgages to raise additional private capital.

Question. Does HUD have a new study to back up your assertion that the capital backlog has been reduced by $4.5 billion? Would you please provide that study to the committee?

Answer. The Department is proposing to conduct a study of backlog needs in 2007.

FARM LABOR HOUSING

Question. Mr. Secretary, in our Hearing on April 14, 2005, I addressed the significant needs in Washington State for seasonal and permanent farm labor housing. As you are aware, the farm labor community is one of the most poorly housed populations in the Nation and the only government solutions are spread out over three different departments. Since you are the national official responsible for the Nation's housing needs, I asked that you raise this issue to the highest level by convening a cabinet level working group to look at creative solutions, including working with the private sector to address this problem. Mr. Secretary, I would like to thank you for agreeing to this request and working with me on this issue.

Can you tell me the progress of your efforts with this goal?

Answer. As you know, I am dedicated to increasing the minority home ownership rate in the United States, as well as expanding home ownership opportunities for very low-income populations. Under my leadership, HUD has expanded the resources and opportunities available to farm labor populations, and is now actively implementing policy recommendations that enhance the management, coordination, and delivery of HUD programs and services that improve the lives of farm labor populations throughout the United States. At my direction the Department continues to make enormous strides in delivering programs and services to these marginalized populations. These efforts are occurring through HUD's competitive and formula grant structures, as well as ongoing program processes which collectively have allowed HUD to invest over $32 million in fiscal year 2004 in farmworker communities and colonias areas.

Some of this assistance includes: (a) $2.3 million in Housing Counseling Grants awarded to organizations providing counseling services to migrant/permanent farmworker communities and colonias located in Washington, Oregon, Florida, New Mexico, California, and Arizona; (b) $3.2 million in Continuum of Care/Emergency Shelter Homeless Assistance that entails funding to communities with high concentrations of migrant and permanent farmworker populations and colonias regions, and; (c) $3.2 million in Rural Housing and Economic Development (RHED) grant funds.

I am very committed to insuring that HUD continues proactive efforts to improve the deplorable housing and living conditions of farm labor populations. These proactive efforts include equipping organizations that provide services to farm labor populations with the tools necessary to initiate and sustain housing and development services. One such technical assistance effort is the Rural Housing and Economic Development Gateway. A joint collaborative project between HUD and the Housing Assistance Council (HAC), a nonprofit organization that has been helping local organizations build affordable homes in rural areas since 1971. The Rural Gateway assists rural communities—including farm labor populations—improve local housing and economic conditions by providing information resources, technical assistance, training, and investment capital to rural communities.

I know that decent, safe and sanitary housing is a critical foundation for farm labor populations. However, there are other basic necessities that play a vital role in addressing the plight of these communities. This is why I have given my unyielding support to the development of the Federal Interagency Partnership for Colonias and Migrant/Farmworkers Communities. The Partnership, initiated by HUD, provides a continuous dialogue with other Federal agencies that provide services to these distressed communities to join in coordinated joint ventures that expand the benefits to farm labor and colonias populations. The Federal Interagency Partnership includes 14 organizations within Federal agencies that have agreed to identify, collaborate and streamline service delivery available to these distressed communities. In sum, the Partnership allows for the maximization of Federal services assisting farm labor and colonias populations. In addition to HUD, Partnership members include:

—Corporation for National Service;
—Department of Agriculture/Office of Rural Housing Service;
—Department of Education/Office of Migrant Education;
—Department of Health and Human Services/Offices of Minority and Special Populations and International/Global Health Affairs;
—Department of Justice/Office of Civil Rights;
—Department of Labor/Employment and Training Administration;
—Department of Treasury/Community Development Financial Institutions Program and the Community Adjustment and Investment Program;
—Environmental Protection Agency/Office of Pesticide Programs, and Office of Environmental Justice;
—Federal Deposit Insurance Corporation;
—General Services Administration/Computers for Learning Program;
—Internal Revenue Service/Stakeholder Partnership, Education and Communication (SPEC) Group/Wage and Investment Division.

These entities are working with HUD to implement collaborative projects, such as the Legal Working Group and the Government Kiosk Project, that introduce and expand housing resources and opportunities to farm labor and colonias populations.

I have also given my support to the Legal Working Group for Colonias and Farmworker Populations. The Legal Working Group, a direct product of the Federal Interagency Partnership, consists of attorneys from 10 Federal departments and agencies who have jurisdiction over colonias and farmworker issues. The Legal Working Group works to address civil rights violations perpetrated on migrant and permanent farmworker populations as well as colonias residents. Residents of these communities face unique legal issues ranging from discrimination based on national origin to predatory lending and illegal land sales. The Legal Working Group was started to assist local community organizations—including legal aid groups—across the Nation address the unique needs of these marginalized populations. The goal of the Legal Working Group is to connect Federal, State, and local government agencies with community organizations so they can discuss and solve legal problems that impact farmworker populations in a timely manner. By working in a collaborative and coherent fashion, government agencies and the respective services they provide are more effective and responsive in addressing local problems.

Another effort that I enthusiastically support is the Department's Government Kiosk Project, which provides very low-income populations with useful and timely information. The Department of Education, Department of Labor, Internal Revenue Service, and Environmental Protection Agency have recently joined HUD in bringing information the public needs, right to them. These Departments are a part of the project's efforts to provide information in a user—friendly format, and that dispenses important and useful government information to citizens—particularly low-income residents and those who do not have ready access to the Internet. The Government Kiosks are located in visible, high traffic areas such as shopping malls and mass transit centers, which assist in delivering useful and critical information—in both English and Spanish languages—to underserved populations. Visitors can access information on how to buy a home, apply for student loans, make their homes safe from pests, save for retirement, and find out if they are eligible for a Federal income tax credit.

The Department is also responsible for conducting the National Fair Housing Policy/Training Conference. This conference provides another avenue for enhancing services to migrant and permanent farmworker communities and colonias residents. I know that many attendees found the information on predatory lending practices and persistent obstacles limiting equal access to housing very beneficial and insightful.

Question. Will you work closely with me and my staff and provide the support and technical assistance necessary to address barriers and find solutions needed to properly address this problem?

Answer. I am unequivocally committed to providing the necessary support and technical assistance required to alleviate existing barriers and develop sustainable housing and development solutions that introduce and expand affordable housing units to farm labor populations throughout the United States.

My commitment is illustrated in the recent phase one completion of a Geographic Information System Statewide Mapping effort that identifies communities utilizing HUD's HOME Investment Partnerships Program (HOME) and Community Development Block Grant (CDBG) funds. This map identifies specific farm labor housing projects that have recently been completed, or are currently under development. Utilizing this information, HUD will provide tailored services such as housing counseling and financial literacy education, to identified farm labor populations.

At my insistence HUD has also been providing needed technical assistance and funding to units of local government and non-profits providing services to farm labor populations in the Pacific Northwest, including the State of Washington. This assistance has led to the development of over 500 temporary or permanent housing units and related water and wastewater infrastructure systems.

The Department also provides assistance to areas with high concentrations of farm labor populations, such as the Yakima Valley area of Washington. One recent effort connects economic development projects with local and regional farm labor housing efforts. Subsequently, new farmworker housing is being developed while simultaneously expanding job creation opportunities for this population.

An additional benefit of this proactive activity is that HUD is now working with the Diocese of Yakima Housing Service and the Office of Rural Farmworker Housing to develop a needs assessment for the local farm labor population. The results of the assessment will provide a framework from which CDBG, HOME and other public funding resources will be pulled together to design and build affordable housing units, as well as introduce job creation opportunities for the farmworker population.

The Yakima Valley Needs Assessment project mirrors a similar project that HUD recently completed in Manatee County Florida. The Manatee County Florida Farmworker Needs Assessment was initiated to address unmet local needs and capitalize on existing assets and partnerships with local governments, nonprofit groups, faith-based organizations, and local housing providers. Due to the absence of farmworker data and statistics, local organizations were challenged to obtain funding that would address the deplorable living conditions of area farmworkers. In response, HUD funded the design and implementation of a survey instrument that collected local farmworker housing statistics, work conditions, income, area demographics, financial literacy levels, and health conditions.

The collected data has been analyzed and is having an enormous positive impact. Nonprofit and government entities are now able to accurately demonstrate the fundamental needs of the local farmworker community. A collateral benefit is that the survey has prompted local service providers to develop a farmworker profile, an outreach plan, and an action strategy from which to address identified needs.

As these examples and technical assistance projects illustrate, I know the value and importance technical assistance brings to communities that so desperately need affordable housing and economic development opportunities. I will continue to work and provide technical assistance and other resources that alleviate the plight of farm labor populations. I look forward to working with you and your staff.

Question. What are HUD's current authorities and activities related to farm labor housing?

Answer. The Department administers the Southwest Border Region Colonias and Migrant/Farmworker Initiative (SWBR Initiative), to help these distressed communities to address their respective needs. The SWBR Initiative is not a program and as such, does not have specific grant dollars, but works to coordinate HUD services and programs going to these communities. The SWBR Initiative also works to identify existing resources, and collaborate with Federal, State and local partners to improve the plight of colonias and farmworker communities. The mission of the SWBR Initiative is to improve the housing and living conditions of migrant and permanent farmworker communities located throughout the United States, and colonias located along the U.S.-Mexico border.

To maximize resources HUD staff routinely conducts joint workshop sessions that combine information on, and access to, several resources together, such as conducing sessions that consist of housing counseling, financial literacy education and other asset building resources.

Over the past few years HUD, working through the SWBR Initiative, has invested over $120 million in farmworker communities and colonias through the Department's competitive and formula grant structures, as well as on-going program processes.

Under my direction, during the past few years, HUD has initiated a number of projects that address the needs of farmworkers and their families residing in the Pacific Northwest. HUD sponsored a Practitioners Conference entitled "Harvesting Hope for Our Communities—A Tri-State Practitioners' Conference" that was held in Yakima, Washington. The conference brought together nearly 300 attendees to not only discuss the challenges faced by farmworker communities, but also to develop useful and practical strategies, share techniques and methods, and formulate new partnerships to spur action and activities.

Recent HUD efforts include conducting the first annual Yakima Valley Homeownership Fair at the Sun Dome in Yakima, Washington. The fair attracted over 1,750 attendees and over 25 exhibitors. The fair was held in Yakima Valley, the agricultural center of Washington State and home of a large migrant and permanent farmworker population. Informational materials, and on-site workshops, were available in both English and Spanish languages.

With my support, HUD has also been proactive in outreach activities. In fact, only recently HUD staff participated in a bilingual (English and Spanish) radio broadcast (KDNA) in Granger, Washington that highlighted HUD's Federal Housing Authority home ownership information. The listening audience consists of over 25,000 Spanish-speaking daily listeners located in Central Washington and South Central Oregon. These areas consist of very large populations of migrant and permanent farmworkers.

This proactive activity also includes the recent distribution of HUD excess computers to various educational institutions located throughout the Yakima Valley of Washington. The recipient educational institutions have large populations of very low-income students that have no access to computers. Over 20 educational institutions, including rural communities with large farm labor populations, received over 125 excess HUD computers and related equipment.

Another proactive activity that I am happy to report on is the placement of a HUD government kiosk in Sunnyside, Washington. As I mentioned earlier, HUD's government kiosk provides and dispenses important and useful government information—such as how to buy a home, save for retirement, and eligibility for a Federal income tax credit—to citizens, particularly low-income residents and those who do not have ready access to the Internet. Information is accessible in both English and Spanish languages.

The placement of a government kiosk in Sunnyside, Washington is especially beneficial when one considers that Sunnyside has one of the largest concentrations of migrant and permanent farm labor populations in Washington State. The importance and utility of the government kiosk is demonstrated in the fact that this particular kiosk is the fourth active in the Nation, with a monthly average of nearly 900 hits a month.

At my insistence, HUD has also been actively engaged in expanding our partnerships with Community and Faith-Based organizations. Only recently, HUD staff met with 90 individuals representing faith and community-based organizations at a 2-day grant-writing workshop. The workshop took place at the Holy Family Activity Center, Diocese of Yakima and was conducted by HUD's Faith Based and Community Liaison. The session provided attendees with effective grant writing techniques and assisted in strengthening the capacity of emerging organizations to compete for HUD and other Federal grant opportunities.

An additional technical assistance workshop that also recently took place was entitled, "Making Connections through Housing and Economic Development." The workshop facilitated discussion and cultivated partnership opportunities between housing and economic development organizations, professionals and public agencies that provide a variety of services to the Yakima Valley farmworker population.

HUD has also been actively engaged in expanding the positive benefits of existing service providers. One example is HUD's assistance to a non-profit—La Clinica Self-Help Housing—based in Pasco, WA. La Clinica, has been in operation for the past 11 years, and is responsible for the development of 160 homes located in Benton, Franklin, Yakima, Grant and Adams County, Washington.

With HUD's assistance La Clinica has now started to work with several additional funding resources, including the U.S. Department of Agriculture Rural Development program, and HUD's Community Development Block Grant program, HOME Investment Partnerships program, and the Housing Counseling program. These efforts recently allowed La Clinica to dedicate 10 new homes to local farmworker families in Pasco, Washington.

My directions to staff have served as a catalyst for HUD staff to become actively and intimately engaged with local and regional efforts. This can be seen in HUD's recent participation in the Washington State Farmworker Housing Trust (WSFHT) Advisory Board. The WSFHT is a non-profit organization founded in 2003 to bring new resources to meet the need for decent and affordable farmworker housing in Washington. The Trust is a unique collaboration of growers, farmworker advocates, housing providers and community leaders.

To advance the objectives of the WSFHT, HUD recently provided technical assistance funds that were utilized to organize and facilitate the WSFHT Capacity Conference in Yakima, Washington a few months ago. Participants at the conference developed a plan that will focus on building capacity to produce and effectively manage farmworker housing in the State.

HUD's recent participation also includes providing assistance to the WSFHT Board that centered on how to design, structure and implement an effective needs assessment instrument. The WSFHT hopes to design and implement a farmworker needs assessment survey that will be used to define the magnitude and scope farmworker housing and living conditions and related needs in the State of Washington.

Question. Do you believe your agency is doing all that it can in this area?

Answer. As exemplified by my instructions and guidance to HUD staff, and subsequently by the proactive actions of HUD staff I believe that the Department is maximizing available resources and efforts to address the housing and living conditions of farm labor populations throughout the United States. As demonstrated by these actions I am firmly committed to ensuring that decent, safe and affordable housing is made available to migrant and permanent farm worker populations. My unyielding advocacy and support of HUD's Southwest Border Region Colonias and Migrant/Farmworker Initiative underscores the importance I place on introducing and expanding HUD services and programs to these marginalized populations. I am working to institutionalize HUD services and programs that benefit these communities so that they are not one-time successes.

The benefits of this focused and concerted effort can be seen in the investment of over $120 million in the past few years that benefited migrant and permanent farmworker populations throughout the United States.

To further the efforts and critical work that the SWBR Initiative continues to undertake, I am reassigning personnel to the State of Washington whose task will be to continue to introduce and expand HUD services to migrant and seasonal farm labor populations located in the Pacific Northwest Region.

Through the Federal Interagency Partnership for Colonias and Migrant/Farmworker Communities, I will continue to support the identification of existing resources, and collaborate with Federal, State and local partners to improve the plight of these communities, as well as the collaborative joint-ventures, such as the Legal Working Group for Colonias and Farmworker Communities and HUD's government kiosk project.

During my tenure, HUD has made enormous advances to ensure housing and development efforts are made available to farm labor populations. I will continue to make available every resource so that the plight of these populations is alleviated to the fullest extent possible.

CONSORTIA

Question. Your agency has consistently encouraged public housing authorities to streamline their operations to reduce the demand for administrative funds. Many public housing authorities in Washington State participate in a consortium so that they can achieve economies of scale in their purchasing of services. However, efforts to form consortia like these have been frustrated by HUD's inability to fully implement the consortia provisions required by the 1998 Quality Housing and Work Responsibility Act (QHWRA). In the 6 years since this law was enacted, HUD has not yet made its data and regulatory systems compatible with joint filing by consortia. Why has the Department not yet fully implemented consortia provisions of QHWRA?

Answer. PHAs have always had the ability to form consortia for purchasing and contracting activities and the Department has encouraged that. Formation of consortia under Section 13 of QHWRA allows for PHAs to band together under a formal consortium agreement and subject to a joint PHA Plan filed with HUD for the administration of their public and assisted housing programs. Both types of consortia have been addressed in HUD's procurement handbook for Public and Indian Housing Authorities. HUD has not made its data and regulatory systems compatible with joint filing by consortia of all PHA reporting requirements because consortia are not legal entities HUD contracts with directly, which forms the foundation for all HUD systems. Consortia do not meet the standards of a reporting entity. Financial statement reporting and audits are governed by HUD's Uniform Financial Reporting Standards (UFRS), which follow Generally Accepted Accounting Principles (GAAP) and Government Accounting Standards Board (GASB) Statement 14, which defines financial reporting entities. Following from this, HUD assesses individual PHA performance pursuant to the funding and regulatory contracts between both parties, and includes as components of the evaluation process individual PHA financial statements, audits, and the physical condition of contractually covered public housing units.

Question. For example, I understand that the Department has not yet enabled agencies to jointly file with HUD items like tenant-income data, Public Housing Authority Plans, and audits. If you are serious about encouraging PHAs to reduce the demand on administrative funds, shouldn't these long overdue technology upgrades be a very high priority for the agency?

Answer. PHAs can and do submit joint PHA Plans to HUD. The PHA Plan template used for submitting plans includes a consortia designation. HUD has also substantially streamlined annual PHA Plan contents for PHAs with less than 250 units, which represents a group very likely to also form consortia, and reduces administrative burdens. Joint filing of tenant data and audits is not possible for consortia because PHAs are legal entities that contract directly with HUD for funding under various Federal housing programs. PHAs are regulated under Annual Contributions Contracts, grant agreements, and other funding instruments that require PHA level reporting to HUD. Financial statement reporting and audits are governed by HUD's Uniform Financial Reporting Standards (UFRS), which follow Generally Accepted Accounting Principles (GAAP) and Government Accounting Standards Board (GASB) Statement 14. GASB Statement 14 defines financial reporting entities. Consortia are not legally created organizations and do not otherwise qualify as reporting entities, and thus joint filing of audits for consortia is not possible. Where HUD treats multiple PHAs as one entity for consolidated reporting purposes, it is because they are legally and organizationally consolidated into one PHA entity. They transferred their units, funding, contracts, physical assets, and program administration to a consolidated PHA, which could include a regional, metropolitan, State, or county PHA.

MOVING-TO-WORK DEMONSTRATION PROGRAM

Question. Mr. Secretary, three of the larger PHAs in my State—Seattle, King County, and Vancouver, participate in your "Moving to Work" demonstration program. This program helps ensure that low-income individuals will not be penalized by losing their tenant support as they struggle to transition off of public assistance. I understand that HUD has submitted legislation to the authorization committee to expand the number of PHAs that can participate in the Moving to Work program. If your legislation is not enacted, is there any risk that the PHAs currently participating in the program will have their participation terminated?

Answer. No. The proposed Moving-To-Work (MTW) provisions in the State and Local Housing Flexibility Act will not terminate current program participants. This legislation provides automatic 3-year extensions for those MTW agreements that expire in 2005 and 2006. PHAs have the opportunity to enter the program automatically with the enactment of the legislation. At the end of any expired agreement period under the MTW Demonstration, PHAs can opt into the MTW program as described in the legislation under the established eligibility provisions. All existing MTW agreements would be honored to the end of their term. If legislation is not enacted, MTW PHAs would have to seek extensions on an individual basis.

Question. Is there anything in your legislation that imposes new requirements on those PHAs that already participate in the program?

Answer. Yes. Section 302(h)(1) provides that a PHA's performance in the MTW Demonstration and in the MTW Program would be assessed under applicable assessment systems that evaluate a public housing agency's performance with respect to public housing and voucher programs. This means that a PHA in the MTW Demonstration would be assessed by the Public Housing Assessment System (PHAS) or the Section Eight Management Assessment Program (SEMAP) until January 1, 2008. Thereafter, the MTW PHA in the demonstration or in the program would be required to meet performance standards developed pursuant to Section 302(h)(2). In addition to the requirements of section 302(h)(1), Title III may or may not affect current MTW agencies depending on existing individual agreements. Housing agencies in the demonstration negotiated contracts that provided specific conditions and imposed requirements, some of which may be different from the requirement of the proposed program. Housing agencies that elect to join the MTW Program when their contracts expire, or those that elect to opt out of the MTW Demonstration early and enter the MTW Program, will then be subject to the requirements of the program.

SECTION 8 VOUCHERS

Question. Mr. Secretary, we have heard from many housing groups that, during last year's consideration of the Appropriations bill, HUD understated the amount of funding that would be needed to maintain the same number of Section 8 vouchers that were active in 2004. As a result, the program was under-funded by roughly $570 million and 80,000 vouchers have been lost. We have also been told that your fiscal year 2006 request will restore half or 40,000 of these vouchers. Are these figures accurate in your view?

Answer. No. HUD did not understate the amount of funding that would be needed to maintain the same number of vouchers that were needed based on the May through July 2004 reporting period. The fiscal year 2005 Appropriations Act provided a specific amount for the Housing Choice Voucher program to fund the voucher needs for that period and for the adjustments allowed for enhanced vouchers and the first time renewal of tenant protection vouchers and HOPE VI vouchers. As a result, the Department had to prorate downward the 2005 budgetary allocations to PHAs by approximately 4 percent. Our fiscal year 2006 Budget request seeks to restore the entire 4 percent proration reduction.

Question. Will the actual number of vouchers decline by 80,000 this year?

Answer. No. A recent analysis of actual costs and leasing levels per data submitted by PHAs to the Voucher Management System through April 2005 are very constant over the 12-month period ending April 30, 2005. The difference in vouchers leased for the period May through July 2004, compared to February through April 2005, is less than 3,000 vouchers.

Question. If not, what are your precise estimates for the number of vouchers that were funded in 2004 and 2005?

Answer. Actual vouchers leased and funded for calendar year 2004 were 2,024,553.

Based on the funding provided in the fiscal year 2005 Appropriations Act, the Department expects to fund approximately 1,980,000 vouchers in calendar year 2005.

Question. How many vouchers will be funded if we fully fund your request for 2006?

Answer. It is too early in the calendar year to estimate how many additional vouchers can be funded since only 4 months of data is available in 2005. Assuming the existing leasing levels and HAP costs can be sustained using the 2005 budgetary allocations, and existing inflation assumptions hold true, it is reasonable to conclude that an additional 40,000 to 50,000 families may be assisted.

Question. Based upon HUD's ongoing monitoring of rent burdens, can you tell me the percentage of families paying more than 30 percent of adjusted income for rent as a national average in fiscal year 2003 and fiscal year 2004? Can you tell me the current percentage?

Answer. Current percentages are as follows:

—Fiscal year 2003—68 percent;
—Fiscal year 2004—66 percent;
—Current—69 percent.

Under existing program requirements, new families and movers may elect to pay up to 40 percent of their income towards rent. For existing families in the program who chose not to move, there is no limitation on the percentage of their income they can pay towards rent.

Although the percentages provided above indicate that the number of families paying more than 30 percent of income ranges between 66 and 69 percent, more than 60 percent of those families' rent burden is between 30 and 35 percent of adjusted income. The average rent burden for all vouchers is approximately 39 percent and does not represent a significant increase in the 35 percent average rent burden measured in 1990.

Question. What percentage of families has a rent burden exceeding 40 percent of adjusted income?

Answer. The percentage of families in public housing who have a rent burden exceeding 40 percent of adjusted income is as follows:

—Fiscal year 2003—14 percent;
—Fiscal year 2004—16 percent;
—Current—18 percent.

Question. The Department's fiscal year 2005 voucher funding implementation notice States that HUD will reduce existing voucher payments reserves from the previous standard of 1 month's funding, to no more than 1 week's reserve level. Some portion of this reduction was to be used to satisfy fiscal year 2005 rescission requirements.

Does the Department plan to recapture or reduce reserves for any agency below the 1-week level during fiscal year 2005?

Answer. It is not the Department's intention to reduce any PHA's reserves below the 1-week level during fiscal year 2005 or fiscal year 2006.

REUNIFICATION OF CHILDREN WITH THEIR PARENTS

Question. I understand that the Tenant protection Fund has a special designated program for family reunification. In fact, our Chairman, Senator Bond was instrumental in getting this program authorized. However, I understand further that no new vouchers have been issued for this program since fiscal year 2001 and historically HUD has made approximately 39,000 vouchers available for the family unification program. I also understand that it is up to each individual PHA to decide if these vouchers keep their identity after they expire. How many of the original 39,000 family unification vouchers are still used for that purpose and if you are under the authorized level, can PHAs move traditional vouchers into the family unification program?

Answer. PHAs that received Family Unification Program (FUP) vouchers were obligated to use those vouchers for that targeted population for 5 years. HUD awarded 3,920 FUP vouchers in fiscal year 2000 and 958 FUP vouchers in fiscal year 2001, so 4,878 vouchers are still required to be used for family unification purposes. PHAs that decide to voluntarily continue the FUP voucher program after the 5-year requirement is completed are not required to report those vouchers as FUP vouchers in HUD data collection systems. HUD therefore does not know the actual number of vouchers originally allocated for FUP that continue to be voluntarily used for this purpose.

Under the housing choice voucher program, PHAs may establish local selection preferences for admission to the program that reflect the local needs and priorities of the community. PHAs may use vouchers that were not originally allocated as FUP vouchers for family unification purposes by establishing a local selection preference for qualifying families.

Question. Why hasn't your agency requested or issued new vouchers to get more of these families reunited over the last 4 years?

Answer. PHAs currently have the ability to use their vouchers to promote family unification by establishing local preferences for admission to the regular voucher program for qualifying families. A special set-aside of vouchers is not necessary in order for PHAs to serve this particular population. The Housing Choice Voucher Program has grown into a complex, overly prescriptive program that is increasingly difficult to administer. The present program has separate rules for more than a dozen different types of vouchers. A major component of program reform and simplification is to allow local PHAs to decide how best to use vouchers to address the needs and priorities of their community, rather than to continue to dictate these decisions from Washington through a myriad of complicated boutique voucher programs.

Question. Is there any truth to the assertion that you have not issued new vouchers out of the Tenant Protection Fund because you want to leave that funding available for your proposed rescissions?

Answer. No. There is no truth to the assertion that HUD has not funded tenant protection voucher requirements. HUD has and is issuing new vouchers out of the Tenant Protection Fund for tenant protection assistance to assist families impacted by public housing relocation and replacement activities and conversion actions related to HUD's multifamily portfolio. As of June 9, 2005, HUD has allocated 16,211 new vouchers out of the tenant protection line item appropriated in the fiscal year 2005 Consolidated Appropriations Act.

Question. Do you intend to propose rescissions from the Tenant Protection fund for fiscal year 2005, or if we accept your proposal for fiscal year 2006?

Answer. The rescission language enacted under the Housing Certificate Fund gives the Department flexibility to take the rescission from any account within the Department. The Tenant Protection set-aside can certainly be subjected to the rescission if there are unobligated balances remaining under this set-aside. However, at this time there is no specific proposal to rescind Tenant Protection funds.

HOMELESSNESS

Question. Mr. Secretary, does HUD intend to provide a legislative proposal for the "Samaritan Initiative," and if so does it limit supportive services such as case management and would this have a negative impact because providers and communities would not be able to fund the housing and supportive services necessary to achieve the goal of ending homelessness?

Answer. As presented in the 2006 Budget request, HUD proposes to consolidate its 3 competitive homeless grant programs into a single program. This new consolidated program will include the eligible activities similar to the Samaritan Initiative, which will focus on the chronically homeless, and will combine housing subsidies paired with quality case management. A key ingredient to the overall success of ending chronic homelessness is to effectively access mainstream healthcare, social services and employment resources so that HUD's limited homeless assistance funding can be increasingly devoted to housing.

HOPE VI

Question. Mr. Secretary, your budget proposes to eliminate all funding for the HOPE VI program next year, and you are also asking us to rescind every penny of the $143 million that we appropriated for the program this year.

This program is designed to assist public housing agencies in demolishing their most dilapidated housing units and replacing them with new, safe and affordable units for mixed-income individuals. I understand that part of your agency's rationale for decimating the HOPE VI program is that you believe that the program has already achieved its intended goals.

Do you believe that we have already eradicated all of the dilapidated public housing units in America?

Answer. The Department has not had the opportunity to eradicate every unit of dilapidated public housing in America. However, HUD has met its goal to eliminate 100,000 units of the worst public housing through HOPE VI Revitalization and Demolition grants, as well as other funding and approval mechanisms. Since surpassing the goal to eliminate 100,000 units of severely distressed public housing by fiscal year 2003, HUD has continued its commitment of removing this housing from the public housing stock. Through fiscal year 2004, HUD had approved for demolition a cumulative total of 165,155 units and PHAs had completed demolition of 116,545 total units.

Since the Department has met this demolition goal, the HOPE VI program is no longer necessary. However, the Department recognizes that there is an estimated $18 billion capital backlog in the public housing inventory. While there is clearly serious need for investment in the inventory, it is not clear how much of this backlog is represented by severely distressed units needing wholesale demolition and replacement as articulated by HOPE VI. Current definitions used by the Department to define severe distress were developed in response to a sub-set of the public housing inventory that by and large no longer exists i.e., severely distressed, super-block, high-rise, public housing developments with significant social problems in major cities like Cabrini Green and Robert Taylor Homes in Chicago. A new method for assessing severe distress, one that considers the nuances of today's public housing inventory and is more objective, should be developed before HUD funds additional wholesale revitalization of public housing communities.

In the interim, the needs of the remaining public housing inventory can be more appropriately met through other modernization and development programs operated by the Department e.g., the Capital Fund, Capital Fund Financing Program and Mixed-Finance development. The Department continues to encourage housing authorities in need of this assistance to submit project proposals to these programs. To date, the Department has approved over $2.4 billion in transactions using the Capital Fund Financing Program, with approximately $94 million in additional funds in the pipeline. Of the approved transactions, over $254 million will be used for development activities.

Question. I understand that HUD wants to address the remaining dilapidated public housing units by finalizing regulations requiring all the public housing authorities to demolish their most dilapidated housing. That will be a huge undertaking.

Are you proposing to give the public housing agencies any additional resources to accomplish this massive goal of demolishing all dilapidated public housing?

Answer. The Quality Housing and Work Responsibility Act of 1998 (QHWRA) revised Section 202 for mandatory conversion, and added another possibility for removals by crafting a voluntary conversion option as well. More than 140,000 severely distressed housing have been demolished over the last 10 years. As a result, it is anticipated that mandatory conversions will affect the last remaining units that do not meet the minimal threshold conditions and the related formula cost test. The Department has requested additional vouchers to cover Mandatory conversion needs for fiscal year 2006. PHAs will be responsible for using their existing resources to pay demolition and relocation costs as they do now under Section 18, Demolition and Disposition.

Question. Your budget is proposing that capital grants to the public housing authorities be reduced by over a quarter of a billion dollars or almost 10 percent next year. Some experts have observed that cuts in funding to help housing authorities maintain their units will mean that we will just create more dilapidated buildings that will be eligible for HOPE VI grants.

How do you respond to that assertion?

Answer. The administration's proposed budget provides sufficient funds to cover the accrual needs of Public Housing Authorities (PHAs). HUD commissioned a study of the capital needs of PHAs, which was released in 1998. That study identified an annual accrual of capital needs of approximately $2 billion per year, as well as a backlog of capital needs. The administration's proposed budget would provide Capital Fund Program (CFP) monies in excess of the annual accrual need, allowing PHAs to meet their accrual capital needs, as well as enabling them to address some of their backlog capital needs.

Further, activities such as the demolition and disposition of public housing projects have resulted in the demolition of more than 100,000 units of public housing since the preparation of the capital needs report in 1998. The vast majority of these units were distressed and therefore were the most expensive to maintain. This reduction in the number of public housing units has served to reduce both the backlog of physical needs as well as the annual accrual. It should also be noted that replacement units added to the inventory since the preparation of the report are new and therefore less expensive to maintain.

In addition to annual appropriations, PHAs now are able to access the private financial markets and unlock the value of their portfolios. HUD has been implementing the Capital Fund Financing Program (CFFP), which was authorized under the Quality Housing and Work Responsibility Act of 1998 (QHWRA). Through the CFFP, PHAs leverage funds from the private market via a pledge of their future CFP grants. HUD has approved CFFP Proposals in excess of over $2.4 billion, involving over 102 PHAs in more than 40 transactions. Funds derived from the CFFP have enabled PHA's participating in the program to address a significant amount of backlog physical needs.

In the future, HUD looks forward to expanding the CFFP to permit PHAs to use the Federal Operating Fund in the same manner, and expand the use of mortgages to raise additional private capital.

PROPOSED SECTION 811 CUT

Question. Mr. Secretary, why is Section 811 Housing for Persons with Disabilities being singled out for a 50 percent cut in this budget including the elimination of all funding for new production and rehabilitation of accessible housing units?

Answer. The cut in the Section 811 Budget was one of several difficult decisions that the Department had to make this year. As you know, significant cuts and changes were also proposed for other programs, such as the Community Development Block Grant program.

Question. This proposal to eliminate the project-based side of Section 811 appears to be completely at odds with the administration's stated goal of promoting community-based alternatives to costly and ineffective institutional settings for people with severe disabilities.

Why is HUD seeking to cut Section 811 funding by 50 percent at a time when HHS has been working so hard to promote independence and community integration for people with disabilities through the President's New Freedom Initiative?

Answer. The Department will continue to support the President's New Freedom Initiative by supporting and fully funding the 40,000 units that are supported by Section 811 funds.

Question. How will HUD ensure that low-income people with disabilities continue to have access to affordable housing in light of the fact that rental subsides alone are not sufficient because rental units are not available in most communities?

Answer. The Department will continue to support the 200,000 units that are occupied by persons with disabilities in various HUD programs. As you know, this includes 40,000 units that are supported by the Section 811 program. These units are located in many communities throughout the United States.

OPERATING FUND NEGOTIATED RULE

Question. The cost of implementing the recommendations of the Operating Fund rule negotiated between HUD and stakeholders was nearly $4 billion in 2003 dollars. In addition, agencies will incur transition costs for the conversion to property-based rather than agency-wide accounting and management required by the rule. Your budget requests just $3.4 billion for the operating fund for fiscal year 2006. Your department arrived at a negotiated agreement with stakeholders on this rule in June. Did funding needs of the negotiated rule figure into your budget request?

Answer. The issue of "transition costs" was discussed during negotiated rule-making but was not agreed to in the final Agreement. Hence, the fiscal year 2006 Budget request does not include any funding for transition costs. However, that PHAs currently have approximately $2.8 billion in operating reserves that they can use for transition costs.

Question. As I understand it, the Operating Fund proposed rule recently sent to Congress is materially different than the rule negotiated with public housing stakeholders last June.

Isn't changing the terms of the rule after you have arrived at a negotiated position a fundamental breach of this agreement?

Answer. Consistent with requirements under Executive Order 12866 entitled "Regulatory Planning and Review" and other rulemaking authorities, the negotiated rule underwent further HUD and Executive Branch reviews prior to publication. These changes were necessary in order to incorporate changes reflective of budget and policy priorities.

Question. The Department released data regarding the impact of the previously-negotiated rule on individual agencies. When do you plan to release agency-level data regarding the impact of you proposed rule? I think this would be key to a productive comment period on the proposed rule.

Answer. Impacts of the proposed rule on PHAs were presented to the various public housing trade associations and other representatives and posted on REAC's Operating Subsidy web-site: http://www.hud.gov/offices/pih.

QUESTIONS SUBMITTED BY SENATOR RICHARD J. DURBIN

Question. The President's budget proposes a 5 percent cut in fiscal year 2006 funding despite the acknowledgment that two new jurisdictions will become eligible for formula funding, bringing the total number of jurisdictions eligible for formula funding to 125. The proposed 2006 funding levels of $268 million would return HOPWA to a funding level between the 2001 ($257.4 million) and 2002 ($277.4 million) when there were only 103 and 107 jurisdictions, respectively. This means that the current HOPWA program must support more grantees with less money than ever before. Why is the Department withdrawing necessary funds while increasing eligible jurisdictions?

Answer. The Department's fiscal year 2006 Budget request of $268 million for the Housing Opportunities for Persons with AIDS (HOPWA) program will provide continued housing support for the most vulnerable individuals and their families living with HIV/AIDS. The funding request is approximately at the same level as recent program expenditure patterns (the most recent 3-year average was $274 million for all HOPWA grantees). HUD estimates that HOPWA housing subsidies and support in community residences and through direct rental assistance will enable over 67,000 households to reduce their risks of homelessness and improve their access to healthcare and other support. In addition, HOPWA grantees have shown good success in leveraging other resources to operate these housing programs by committing State, local, and private resources to their community efforts. On a technical note, the qualification of new formula recipients has a minimum effect on formula distributions. This is because they qualify for the smallest allocations, (generally around $350,000) and because the newly qualifying cities are in metropolitan areas that are likely to have been included in a grant to the State in a prior fiscal year. This latter change would have no net fiscal impact but would change the entity responsible for managing these grant activities. The correct number of HOPWA formula eligible communities in fiscal year 2006 will be 122. This number is being updated based on the use of AIDS surveillance data recently obtained from the Centers for Disease Control and Prevention (CDC). HUD has determined that the number of formula recipients in 2006 will only increase by one additional recipient (Palm Bay, Florida) as this metropolitan area meets the statutory eligibility requirements with a population of more than 500,000 persons and a cumulative number of cases of AIDS of greater than 1,500 cases of AIDS. Further, this area had previously been included in formula funding to the State of Florida, and as such, no significant net effect will occur, as the amount of funds allocated to the State will be proportionately smaller. Also, in fiscal year 2005, one newly designated recipient (Lakeland, Florida) made use of the authority provided in a new administrative provision to the HOPWA appropriations act that with the agreement of their State, allows the

State to continue to serve as the grantee for managing the HOPWA program in their metropolitan area. The required data from CDC involves the use of cumulative cases of AIDS in making these determinations, which includes a significant number of persons who have died due to AIDS. In 1999, HUD recommended an updated formula based on a CDC estimate of persons living with AIDS adjusted for area housing costs. The need to update the formula was further identified in the recent PART review for this program and a more accurate distribution could be based on a CDC report for persons living with AIDS and area housing costs.

Question. HUD is in the process of foreclosing on Lawndale Restoration, 1,240 project-based Section 8 apartments in Chicago's Lawndale Community. In the past, project-based vouchers would have been maintained after foreclosure. However, HUD is not offering that possibility, and is instead offering tenants Housing Choice Vouchers. If all qualifying tenants receive Housing Choice Vouchers, tenants of Lawndale Restoration will comprise a group that is 25 percent of the tenants who have been relocated from the Chicago Housing Authority during the past 5 years under its Plan for Transformation.

HUD is not offering other more flexible approaches that take into consideration whether project-based assistance, Housing Choice Vouchers or a combination of the two would be more appropriate rental assistance for this property. Why?

Answer. Over the last several years, the Department has not offered a project-based Section 8 contract after foreclosure. The Department believes that residents want flexibility, and the option to relocate if they so choose. The housing choice voucher gives residents that ability. In the case of the Lawndale project, the Department is aware of residents that have indicated their desire to relocate and there are some residents who want to remain at the project.

Although the Department will be issuing vouchers to eligible residents, no resident will be required to leave the project if they desire to stay. If a resident who desires to move from the development is unable to find other housing, they will always have their current housing available to them. If a resident decides to move permanently from the complex, it is because they desire to do so and not because of the foreclosure action.

Question. Some studies have indicated that 15 percent of voucher holders in Chicago are unable to sign a lease within 6 months that they have to find an apartment. Given the saturation in Chicago, explain how an additional thousand families from Lawndale Restoration will impact the housing market in Chicago?

Answer. The Department engaged a contractor to perform a market study in Chicago last year. The purpose of the study was to determine whether the rental market in Chicago could absorb the number of families projected to be relocated from public housing to private sector housing (assisted by the Housing Choice Voucher program) as a result of redevelopment activity at the Chicago Housing Authority. The market study concluded that there is an ample supply of vacant affordable private sector housing to absorb the families projected to be housed in private sector housing. The market study estimated that there would be 40,000 affordable vacant units in the local rental market annually. Based on the market study, the Department believes that the private market can absorb the families that would be impacted by the Lawndale restoration.

Question. Will these families be able to find decent housing in Chicago?

Answer. The Department engaged a contractor to perform a market study in Chicago last year. The purpose of the study was to determine whether the rental market in Chicago could absorb the number of families projected to be relocated from public housing to private sector housing (assisted by the Housing Choice Voucher Program) as a result of redevelopment activity at the Chicago Housing Authority. The market study concluded that there is an ample supply of vacant affordable private sector housing to absorb the families projected to be housed in private sector housing. The market study estimated that there would be 40,000 affordable vacant units in the local rental market annually. Based on the market study, the Department believes that the private market can absorb the families that would be impacted by the Lawndale restoration.

Question. Beyond the Housing Choice Vouchers, will HUD assist these families in finding housing? If so, how?

Answer. The Department has already provided relocation assistance (including the costs to move, transportation to find alternate housing, housing counseling, etc.) to the 180 residents who were required to move from three of the buildings currently being demolished. HUD is also providing the same relocation assistance to 35 residents of another building in the complex that has severe structural problems.

For the remaining buildings, the Department is not requiring the residents to relocate and therefore there will be no other assistance provided except for the housing choice voucher. The purchasers of the buildings will be required to provide relocation assistance while they make the necessary repairs to the buildings if the residents have to be relocated during construction. If a resident decides to move permanently from the complex, it is because they desire to do so and not because of governmental action and no government relocation assistance to those residents will be provided.

Question. On March 10, 2005, I sent a letter to HUD requesting that the Department reconsider HUD's decision to deny the Kankakee County Housing Authority funding for its entire voucher allotment. Please update me on the status of this request.

Answer. The Senator's request on behalf of the Kankakee County Housing Authority (KCHA) concerned HUD's denial of a request from that agency that HUD adjust the leasing figures used to calculate KCHA's calendar year 2005 voucher program renewal funding. As background, in December 2004, HUD provided to each Housing Authority (HA) the leasing and cost information, based on each HA's prior submissions, that HUD intended to use as the basis for calculating each HA's calendar year 2005 funding for voucher program renewals. Each HA was given the opportunity to request an adjustment of any data that was not accurate or that qualified for adjustment under the terms of the fiscal year 2005 Appropriations Act. KCHA responded to that information and requested that HUD adjust its leasing numbers to include a number of vouchers that had been provided to KCHA in a tenant protection action in August, 2001, but which were not yet under lease during the period HUD was required to use to calculate calendar year 2005 funding. KCHA's request was denied because the vouchers provided to KCHA in 2001 had been in their inventory for a sufficient period of time that they should have been under lease by the time period used to calculate the calendar year 2005 funding, which was May through July of 2004. The fiscal year 2005 Appropriations Act provided that HUD make necessary adjustments for costs related to first time renewals of tenant protection vouchers. At the time of KCHA's request, the vouchers in question had been renewed three times; as a result, KCHA was not eligible for an adjustment to their leasing numbers.

SUBCOMMITTEE RECESS

Senator MURRAY. Well, thank you very much, Senator Leahy. And I agree with you and appreciate your words today.

This subcommittee will stand in recess until Thursday, April 21, when we will take the testimony from OMB Director Bolten. And I can assure you we will be talking about the HUD budget among other things.

[Whereupon, at 11:05 a.m., Thursday, April 14, the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

THURSDAY, APRIL 21, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:34 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond, (chairman) presiding.

Present: Senators Bond, Bennett, Stevens, Murray, and Kohl.

EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

STATEMENT OF JOSHUA B. BOLTEN, DIRECTOR

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning. The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies will come to order.

We welcome Josh Bolten, Director, Office of Management and Budget. I look forward to your views, Director Bolten, on the President's overall budget request for 2006, as well as budget issues related to OMB's own needs.

The President's budget request for 2006 calls for some $840 billion in overall discretionary budget authority, including $419 billion for the Department of Defense and $32 billion for Homeland Security. For DOD, this would be an increase of $19 billion, or 4.8 percent, over 2005. For Homeland Security, this would be an increase of $1 billion, or 3.1 percent, over 2005. Even with significant increases in security-related spending, the overall 2006 budget request would hold overall spending to a 2.1 percent growth, just below the rate of inflation.

Consequently, the budget proposes that overall non-security discretionary spending would be reduced from the 2005 level by $3 billion, or 0.7 percent, for a total of $389 billion. Moreover, on non-defense discretionary spending, the budget proposes more than 150 reductions and eliminations in Federal programs to save $20 billion in budget authority in this coming fiscal year alone.

I support the President's goal of cutting the deficit in half by 2008. However, reducing the deficit solely on the back of domestic discretionary spending is very troubling and, I believe, an ill-conceived strategy that could have disastrous results for many important, congressionally supported, as well as popularly supported domestic programs. To be clear, discretionary spending should be reduced where appropriate. We should not, however, reduce those programs solely to meet arbitrary deficit reduction numbers, especially when many of these programs are important to the health, safety, and quality of life of the citizens of our Nation.

More importantly, mandatory spending must be reduced to achieve any true spending reform and deficit reduction. While I support the President's efforts to reform Social Security in order to avoid bankrupting the future of our children and our children's children, I am concerned that the budget proposes total mandatory spending of $1.6 trillion in 2006, an increase of $107 billion, or 7 percent, over fiscal year 2005. Mandatory spending currently accounts for some 63 percent of total Federal spending and by 2010 will grow to $2.1 trillion which would represent 68 percent of total spending. This is a total annual growth rate of some 6.3 percent, which towers over any savings expected to be achieved from domestic discretionary spending cuts.

However, we are not here to discuss reforming mandatory programs, no matter how important. We are here to discuss the President's proposed budget for domestic discretionary spending, especially those programs within the jurisdiction of the Transportation, Treasury, and HUD Appropriations Subcommittee, or the THUD committee, as it is called.

The House and Senate Appropriations and Budget Committees and OMB share responsibility for recommending a budget to Congress and the President that will ensure the continued effective running of the United States Government for each fiscal year. However, at the end of the day, we as appropriators must present to Congress and then the President a bill that is financially sound, responsible, and capable of maintaining the efficient running of government.

As part of this process, OMB has an obligation to propose funding recommendations that are consistent with budget and program realities. The administration's budget should not be based on flawed data and budget assumptions and should not include recommendations that violate Congress' Budget and Impoundment Control Act of 1974.

Unfortunately, I believe this budget request contains a number of flawed budget assumptions, as well as a number of ill-considered budget and policy recommendations. In many cases, Mr. Bolten, I believe you and the President have been ill-served by your staff, and it is especially problematic in a year of tight budget allocations.

As you may know, I had the distinct honor previously of serving as chair of the VA/HUD Appropriations Subcommittee and now as the chair of this subcommittee. This has allowed me to develop some familiarity with $170 billion of domestic discretionary spending, or 50 percent of the President's budget for domestic discretionary spending. I will focus my comments and questions today and for the record primarily on programs of which I have a personal knowledge and interest. Nevertheless, I understand that my concerns with the fiscal year 2006 budget are similar to the concerns my colleagues are wrestling with in other appropriations subcommittees.

First, let me express my sincere disappointment that the administration has proposed to eliminate the HUD Community Development Block Grant program, along with 17 other programs, and replace these with a block grant program in Commerce called Strengthening America's Communities Initiative.

The administration proposes to fund this initiative only at $3.7 billion, which is an overall reduction for all these programs of almost $2 billion, or some 34 percent, from the 2005 level.

The proposed elimination and related reduction of funding for CDBG, as well as many of these other programs is, in my view, a tragedy. Communities across the Nation rely on CDBG to fund critical housing and community development programs, and without these funds, many local programs will falter and fail.

Equally important, CDBG is a critical component of HUD's mission. CDBG helps to make HUD's housing mission successful. That is why they call it Housing and Urban Development. Without CDBG, it is the Department of Housing, and if your proposals go forward to block grant everything, housing would probably wind up as an office in the Secretary of Commerce's office that hands out block grant monies. As history tells us, successful community development relies on a comprehensive approach to housing and community development.

Now, CDBG is not perfect. CDBG funds are not always used well or effectively. However, HUD, OMB, and select CDBG interest groups recently ratified a consensus document to address weaknesses in the CDBG program by creating an outcome measurement system to establish new benchmarks and better oversight. Since this document is designed to address OMB's concerns, I am puzzled by the administration's proposal to dismantle a program that has been redesigned to become more effective and successful as required by the administration.

I have some more practical concerns, however. Even if we were to pass a new Commerce block grant this year—and I will have to say, talking with my colleagues, I find a minimum amount of high enthusiasm in the Congress for that—if you were successful to replace CDBG with a block grant, how is it possible for the Commerce Department to implement the program for 2006, including the issuing of regulations, the hiring and training of staff, and the education of communities in how these funds must be used? What happens to communities with existing projects that rely on CDBG funding, especially those projects with section 108 loan guarantees where the guarantees rely on a flow of future CDBG funding?

I will also have additional questions with regard to the proposed consolidation of the Community Development Financial Institutions program, the Bank Enterprise Act program, and the Section 4 Capacity Building LISC/Enterprise program into the new proposed Commerce block grant. None of these activities would fit into a block grant scheme, and I think the Nation would be a loser for it.

Another major funding area that OMB has not adequately supported—and we have talked about this before—is basic scientific research, primarily the physical sciences, which is mainly funded through the National Science Foundation. I no longer have responsibility in my committee for that, but let me reemphasize that NSF should play a critical role in the economic, scientific, and intellectual growth of the Nation. Our country's future resides in our ability to lead the world in science and technology, especially in the global marketplace. NSF should be one of our primary tools in meeting the goals of the 21st century by pushing the boundaries of scientific research and technology. This work of NSF will significantly build our economy and speed innovation.

The lack of support of NSF and the physical sciences and the growing funding disparity between the life sciences and the physical sciences is jeopardizing our Nation's ability to lead the world in scientific innovation. We are jeopardizing the work of the National Institutes of Health because we are undermining the physical sciences which provide the underpinning for medical technological advances. Inadequate funding for NSF hurts our economy and the creation of good jobs which would help address the outcry of outsourcing jobs to other countries. The bottom line is that by underfunding NSF, we are shooting ourselves and our future generations in the foot.

I know that this is not in this committee, but I believe that this is of such major concern that it ought to be addressed at the top policy levels in the administration. We have proposed and I have heard general plaudits for the goal of doubling the funding of NSF in 5 years, or a 14.7 percent increase annually, and I think the entire scientific community and anybody who looks at it would agree.

But let us go back to the THUD committee. I am really puzzled and concerned over the administration's proposal to rescind $2.5 billion from HUD's Housing Certificate Fund. As you know, we have spent several years reforming the Section 8 tenant-based voucher program to limit the growing costs, and we have required public housing authorities to implement a more responsible budget-based planning and funding system for the program. As a responsible part of these reforms, much of the funds that have been available normally for rescission from within HUD over the last few years are no longer available. In point of fact, when the HUD Secretary, Alphonso Jackson, came before us, we asked him to identify any account or source of funds at this time which could support a $2.5 billion rescission from within HUD. He was unable to do so, and I can understand his problem. But this is a question which needs concrete answers before we draft this bill and try to impose cuts in an area where nobody knows that rescissions can be made.

To be blunt, everyone's expectation is that OMB and HUD will have a system for evaluating and verifying where rescission funds will come from with a reasonable level of certainty. In particular, I expect OMB to provide an assessment of where these rescissions will come from and the methodology that OMB and HUD used in determining the amount of the rescission.

In addition, the administration is seeking to eliminate HOPE VI, as well as rescind the HOPE VI fiscal year 2005 funding of $143 million. As you may know—you may not know, but I am here to advise you—I set the stage for HOPE VI by including a demonstration project in the 1990 National Affordable Housing Act that allowed the demolition and replacement of Pruitt-Igoe Public Housing in St. Louis with vouchers and new housing. This approach has revolutionized the way we reformed obsolete public housing by allowing for the demolition of obsolete housing and the creation of mixed income private and public housing. This program has resulted in leveraging new private investment and the revitalization of entire communities. If anybody has any doubts about it, I would invite them to come to St. Louis or the many other communities where HOPE VI has been extremely successful.

I am concerned today also with the administration's penchant for rescinding 2005 funding programs that were supported by Congress and enacted by the President. There are other examples throughout the budget, including within this subcommittee. For example, the administration proposes a rescission of $74 million appropriated in 2005 for the Maritime Administration for the national defense tank vessel construction program. The rescission would eliminate the program. Both rescission requests raise possible violations of the Congressional Budget and Impoundment Control Act, as well as significant costs to the subcommittee, depending on our actions. If we do not rescind these funds from the enacted 2005 appropriations, the subcommittee will have to make up some $212 million that must come from offsets or cuts in other programs. If the rescissions do go forward, we think that there are other significant liabilities that will be incurred by the Federal Government, and it is an open question where those funds will come from.

Another substantial concern in the 2006 budget is Amtrak funding. I have not been a cheerleader for Amtrak. I supported it as Governor. But as the people at OMB should know, there are many of my colleagues and supporters that will seek to backfill this funding shortfall. I think you can count probably 55 or 60 votes on the Senate floor. That means we will have to cut other programs. These are program cuts and offsets that the administration has been unable or unwilling to identify. To be honest, I find the proposal for the Amtrak budget not responsible. I support the administration's efforts to initiate long overdue and fundamental reform of Amtrak's failed business model, but it is obvious that the $360 million the administration is proposing to support the dismantling of Amtrak is totally inadequate and could throw the entire passenger train industry into chaos, with bankruptcy and untold problems throughout the system, and for rail transportation generally. Clearly, whatever approach Congress takes, the funding for Amtrak will be far greater than proposed and will have to come from somewhere.

I also support the Airport Improvement Program which provides Federal grants to airports for projects to enhance safety, capacity, security, and environmental concerns. Yet, the 2006 budget requests $3 billion for AIP, a reduction of nearly $500 million from the 2005 enacted level, and a $600 million reduction from the amount authorized for 2006. This is a popular and important program that has broad support. The proposed funding will impact the funding available for primary and non-primary airports. Adequate funding is especially important in view of rising fuel costs.

Another area of concern to me is the Federal Government's ability or lack thereof to procure and manage information technology systems. To be clear, this is a problem that has existed for many years through both Democratic and Republican administrations. The Federal Government spends over $60 billion on IT projects, but it appears that a large portion of these funds are not managed effectively. For example, the Internal Revenue Service's Business Systems Modernization has been fraught with cost overruns, missed deliverables, and is currently designated as high risk by the Government Accountability Office. I could go down a list of problematic IT systems, but that would require another hearing. I think it is imperative—and this is where I have a constructive suggestion for OMB—to do a better job protecting the taxpayers' interest in procuring and overseeing its multi-billion dollar portfolio. Perhaps OMB could develop a cadre of experts to assist individual agencies in the IT arena by helping to establish IT requirements, helping to negotiate IT contracts, and helping to ensure that contractors meet all the requirements, benchmarks, and time lines. I look forward to working with you on IT procurement and management and any plans the agency may have to address this issue.

I do not think it is too much to ask the Federal Government to live within a budget. I did so as Governor of Missouri, and I believe in responsible spending. In conclusion, however, I do not believe that we should have to live within a budget that is based on flawed assumptions and is fiscally questionable, especially when proposed budget shortfalls must be offset from other programs and activities that the administration was unable to identify or propose. How can we make the budget work if OMB cannot?

PREPARED STATEMENT

Mr. Director, I would like to work with you in particular on the Government's IT issues. We also need your help and assistance in developing a budget and an appropriations plan that will allow our subcommittee to produce a responsible bill.

I look forward to working with you on these issues, and I now turn to my ranking member, Senator Murray. Senator.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, Housing and Urban Development and Related Agencies will come to order. We welcome Josh Bolten, Director, Office of Management and Budget (OMB). I look forward to your views on the President's overall budget request for fiscal year 2006 as well as budget issues related to OMB's own needs.

The President's budget request for fiscal year 2006 calls for some $840.3 billion in overall discretionary budget authority, including some $419.3 billion for the Department of Defense and $32 billion for Homeland Security. For DOD, this would be an increase of $19 billion or 4.8 percent over fiscal year 2005. For Homeland Security, this would be an increase of $1 billion or 3.1 percent over fiscal year 2005. Even with significant increases in security-related spending, the overall fiscal year 2006 budget request would hold overall spending to a 2.1 percent growth, just below the rate of inflation.

Consequently, the budget proposes that overall non-security discretionary spending would be reduced from the fiscal year 2005 level by some $3 billion or 0.7 percent for a total of $389 billion. Moreover, as to non-defense discretionary spending, the budget proposes more than 150 reductions and eliminations in Federal programs which would save some $20 billion in budget authority in fiscal year 2006 alone.

I support the President's goal of cutting the deficit in half by fiscal year 2008. However, reducing the deficit almost solely on the back of domestic discretionary spending is very troubling and, I believe, an ill-conceived strategy that could have disastrous results for many important, congressionally-supported domestic programs. To be clear, discretionary spending should be reduced where appropriate. We should not, however, reduce these programs solely for sake of deficit reduction, especially when many of these programs are important to the health, safety and quality of life of our Nation's citizens.

More importantly, mandatory spending must be reduced to achieve any true spending reform and deficit reduction. And while I support the President's efforts to reform Social Security in order to avoid bankrupting the future of our children and children's children, I remain very concerned that the budget proposes total mandatory spending of $1.6 trillion in fiscal year 2006, an increase of $107 billion or 7 percent over fiscal year 2005. Mandatory spending currently accounts for some 63 percent of total Federal spending. By fiscal year 2010, mandatory spending will grow to $2.1 trillion and will represent some 68 percent of total spending. This is a total annual growth rate of some 6.3 percent which towers over any savings expected to be achieved from domestic, discretionary spending.

However, we are not here to discuss reforming mandatory programs, no matter how important. We are here to discuss the President's proposed budget for domestic, discretionary spending for fiscal year 2006, especially those programs within the jurisdiction of the Transportation/Treasury Appropriations Subcommittee.

The House and Senate Appropriations and Budget Committees and OMB share responsible for recommending a budget to the Congress and the President that will ensure the continued effective running of the United States Government for each fiscal year. However, at the end of the day, we, as appropriators, MUST present to the Congress and then the President a bill that is financially sound, responsible and capable of maintaining the efficient running of the government.

As part of this process, OMB has an obligation to propose funding recommendations that are consistent with budget and program realities. The administration's budget request should not be based on flawed data and budget assumptions, and should not include recommendations that are a violation of the Congressional Budget and Impoundment Control Act of 1974.

Unfortunately, I believe this budget request contains a number of flawed budget assumptions as well as a number of ill-considered budget and policy recommendations. In many cases, Mr. Bolten, I believe that you and the President have been poorly served by your staff. This is especially problematic in a year of tight budget allocations.

As you know, I have had the distinct honor of serving as the former chair of both the VA/HUD Appropriations Subcommittee and now as the chair of the Transportation/Treasury Appropriations Subcommittee. This has allowed me to develop familiarity with some $170 billion of domestic discretionary spending or some 50 percent or more of the President's budget for domestic, discretionary spending. As a result, I will focus my comments and questions today and for the record primarily on programs of which I have a personal knowledge and interest. Nevertheless, I understand that my concerns with the fiscal year 2006 budget are similar to the concerns my colleagues are wrestling with in other appropriations subcommittees.

First, I am very disappointed that the administration has proposed to eliminate the HUD Community Development Block Grant (CDBG) program along with some 17 other programs and replace these programs with a new block grant in the Department of Commerce called the Strengthening America's Communities initiative. The administration also is proposing to fund this new initiative at $3.7 billion which is an overall reduction for all these programs of almost $2 billion or some 34.2 percent from the fiscal year 2005 level.

The proposed elimination and related reduction of funding for CDBG as well as many of these other programs is a tragedy. Communities across the Nation rely on CDBG to fund critical housing and community development programs. Without these funds, many local programs will falter and even fail. Equally important, CDBG is a critical component of HUD's mission; CDBG helps to make HUD's housing mission successful. Moreover, the use of CDBG consolidated plans helps to ensure that communities tie together CDBG, housing funds and other Federal and State resources into a comprehensive approach to local housing and community development needs.

Without CDBG, HUD's mission will be reduced to almost solely housing. As history tells us, successful community development relies on a comprehensive approach to housing and community development.

CDBG is not a perfect program and CDBG funds are not always used well or effectively. However, HUD, OMB and select CDBG interested groups recently ratified a consensus document to address weaknesses in the CDBG program by creating an Outcome Measurement System to establish new benchmarks and better oversight. Since this document is designed to address OMB's concerns, I am puzzled by the administration's efforts to dismantle a program that has been redesigned to become more effective and successful according to administration requirements.

I have more practical concerns, however. Even if we pass a new Commerce Block grant this year to replace CDBG, how is it possible for the Commerce Department to implement the program for fiscal year 2006, including the issuing of regulations, the hiring and training of staff, and the education of communities in how these funds must be used? What happens to communities with existing projects that rely on CDBG funding, especially those projects with section 108 loan guarantees where the guarantees rely on a flow of future CDBG funding?

I also will have additional questions with regard to the proposed consolidation of the Community Development Financial Institutions program, the Bank Enterprise Act program and the Section 4 Capacity Building "LISC/Enterprise" program into the new proposed commerce block grant. None of these activities easily fit into a block grant scheme.

Another major funding area that OMB has not adequately supported is basic scientific research—primarily, the physical sciences—which is mainly funded through the National Science Foundation. NSF plays a critical role in the economic, scientific and intellectual growth of this Nation. Our country's future resides in our ability to lead the world in science and technology, especially in the global marketplace. NSF is one of our primary tools in meeting the global challenges of the 21st Century by pushing the boundaries of scientific research and technology. This work will grow our economy and speed innovation, improving the quality of life for all people.

However, the lack of support for NSF and the physical sciences and the growing funding disparity between the life sciences and the physical sciences is jeopardizing our Nation's ability to lead the world in scientific innovation. Further, we are jeopardizing the work of the National Institutes of Health because we are undermining the physical sciences, which provide the underpinning for medical technological advances. Inadequate funding for NSF also hurts our economy and the creation of good jobs, which would help address the outcry of outsourcing jobs to other countries. The bottom-line is that by underfunding NSF, we are shooting ourselves and our future generations in the foot. I hope we can get NSF back on the path of doubling the budget as I have strongly advocated.

I also am very puzzled and concerned over the administration's proposal to rescind some $2.5 billion from HUD's Housing Certificate Fund. As you know, we have spent several years reforming the section 8 tenant-based voucher program to limit the growing costs and require PHAs to implement a more responsible budget-based planning and funding system for the voucher program. As a responsible part of these reforms, much of the funds that have been available normally for rescission from within HUD over the last few years are no longer available. In point of fact, HUD's Secretary, Alphonso Jackson, was unable to identify any account or source of funds at this time which could support a $2.5 billion rescission from within HUD. This is a question which needs concrete answers before we draft this bill. To be blunt, everyone's expectation is that OMB and HUD have a system for evaluating and verifying where rescission funds will come from with a reasonable level of certainty. In particular, I expect OMB to be able to provide an assessment of where these rescissions will come from and the methodology that OMB and HUD used in determining the amount of the rescission.

In addition, the administration is seeking to eliminate HOPE VI as well as rescind the HOPE VI fiscal year 2005 funding of $143 million. As you may know, I set the stage for HOPE VI by including a demonstration project in the 1990 National Affordable Housing Act that allowed the demolition and replacement of Pruitt-Igoe Public Housing in St. Louis with vouchers and new housing. This approach revolutionized the way we reformed obsolete public housing by allowing for the demolition of this obsolete housing and the creation of mixed income private and public housing. This program has resulted in leveraging new private investment and the revitalization of entire communities.

While I am opposed to the elimination of the HOPE VI program, I am more concerned today with the administration's penchant for rescinding fiscal year 2005 funding from programs that were supported by the Congress and enacted by the President. There are other examples throughout the budget, including within the Transportation/Treasury Appropriations Subcommittee. For example, the administration also proposes a rescission of $74 million appropriated in fiscal year 2005 for the Maritime Administration for the National Defense Tank Vessel Construction program. This rescission would eliminate this program. Both rescission requests raise possible violations of the Congressional Budget and Impoundment Control Act as well as significant costs to the subcommittee depending on our actions. If we do not rescind these funds from these fiscal year 2005 enacted appropriations, the subcommittee will have to make up some $212 million that must come from offsets or cuts in other programs.

Another area of substantial concern in the fiscal year 2006 budget is Amtrak funding. I am not a fan of Amtrak but it appears, as OMB knows, that many of my colleagues are supporters and will seek to backfill this funding shortfall. This means we will have to cut other programs, and these are programs cuts and offsets that that the administration has been unable or unwilling to identify. I also find the Amtrak budget incredibly irresponsible. While I support the administration's efforts to initiate long overdue and fundamental reform of Amtrak's failed business model, it is obvious that the $360 million that the administration is proposing to support the dismantling of Amtrak is totally inadequate and could throw the entire passenger train industry into chaos. Clearly, whatever approach the Congress takes, the funding for Amtrak will be far greater than proposed and will have to come from somewhere.

I also support the Airport Improvement Program which provides Federal grants to airports for projects to enhance airport safety, capacity, security, and environmental concerns. Yet, the fiscal year 2006 budget requests $3.0 billion for AIP, a reduction of nearly $500 million from fiscal year 2005 enacted level and a $600 million reduction from the amount authorized for fiscal year 2006. This is a popular and important program that has broad support and the proposed funding will impact the funding available for primary and non-primary airports.

Another area of concern to me is the Federal Government's ability, or lack thereof, to procure and manage information technology systems. To be clear, this is a problem that has existed for many years through both Democratic and Republican administrations. The Federal Government spends over $60 billion on IT projects but it appears that a large portion of those funds are not managed effectively. For example, the Internal Revenue Service's "Business Systems Modernization" has been fraught with cost overruns and missed deliverables and is currently designated as a "high risk" area by the Government Accountability Office. I could go down a laundry list of problematic IT systems but that would require another hearing. I believe it is imperative that the Federal Government, led by OMB, must do a better job of protecting the taxpayer's interest in procuring and overseeing its multibillion dollar portfolio. Perhaps, OMB could develop a cadre of experts that assist individual agencies in the IT arena by helping to establish agency IT requirements, helping to negotiate the IT contract, and helping to ensure the contractor meets all requirements, benchmarks and timelines. I look forward to hearing OMB's efforts in IT procurement and management and any plans the agency may have in addressing this serious issue.

I don't think it is too much to ask the Federal Government to live within a budget. I did so as governor of Missouri and I believe in responsible spending. However, I do not believe that we should have to live within a budget that is based on flawed assumptions and is fiscally questionable, especially when proposed budget shortfalls must be offset from other programs and activities—programs and activities that the administration was unable to identify or propose. How are we expected to make the budget work if OMB cannot?

Mr. Bolten, I would like to work with you in particular on the government's IT issues. However, we also need your help and assistance in developing a budget that allows our subcommittee to develop a responsible bill. I look forward to working with you on all these issues.

I now turn to my Ranking Member, Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Thank you very much, Mr. Chairman. I join with you in welcoming OMB Director Bolten here to our subcommittee this morning.

It has been at least 3 years since the OMB Director has appeared before the subcommittee, so I am pleased that Director Bolten could be with us to discuss the budget request for his own office, as well as the larger budget request of the President for the coming fiscal year.

Mr. Chairman, in addition to serving on the Appropriations Committee, I serve on the Budget Committee. Chairman Bond used to serve on the Budget Committee, but he has moved on to bigger and better things wisely.

You did not need to hear what he just said.

Over the past several weeks, the Budget Committee has been busy drafting a budget and moving it through committee markup and passing it to the Senate floor. I voted against that budget both in committee and on the floor because I believe it did not reflect the right priorities for our county, and it did not strike the right balance between taxes, deficit reduction, and the very real needs that are facing our communities.

I actually have to say that participating in the budget debate over the past couple weeks has reminded me of a very lengthy and painful visit to the dentist's office, and the Muzak in the dentist's office played nothing but a repeating loop of that song we all know well, "Don't Worry, Be Happy."

Don't worry about the drastic cuts, the unidentified rescissions, the user fees, and the problems we are pushing down the road. Don't worry about what is actually in the budget. We will deal with it later. It is kind of don't worry, be happy.

Well, frankly, I am very worried because I can see what is going to happen to some of our country's most critical needs. We are setting ourselves up for a train wreck.

The budget resolution that was presented in the committee accepted the President's proposed funding figure for non-defense, non-homeland security discretionary spending. It was a real cut below last year's level. During debate on the budget, many amendments were offered to restore funding cuts that were proposed in the President's budget. We had amendments to restore funding for Amtrak, the Community Development Block Grant program, first responders, cops on the street, vocational education, and others. Almost all of those amendments were rejected, but still many Senators were telling us don't worry, be happy because when Congress gets around to the appropriations process later in the year, we are not going to enact those cuts anyway.

Well, that does not make the problem go away. In fact, it actually makes it worse.

For example, the Senate failed to adopt an amendment to restore $1.4 billion in spending so Amtrak could maintain rail service next year. Even though that amendment failed, I have heard a number of my colleagues in the Senate say, don't worry, be happy, we will find enough money in the appropriations process to keep Amtrak alive anyway.

Similarly, an amendment was offered to restore funding for the Community Development Block Grant program. While that amendment failed, an amendment was later adopted that said we will somehow find the funding to restore the CDBG program through cuts in unidentified programs. Again, it is don't worry about what is actually in the budget, be happy.

As the budget resolution now moves toward conference, I am having a very hard time convincing some of my colleagues to understand the math does not add up. If we are going to adopt a ceiling for domestic discretionary spending that comes close to the

President's number, we are either going to have to accept many of the budget cuts or we are going to have to impose severe cuts in other programs.

Amtrak and CDBG are just two of the President's proposals under this subcommittee's jurisdiction. The President's budget proposes an unallocated rescission of $2.5 billion to be derived from any program within the Department of Housing and Urban Development. The budget does not tell us where that $2.5 billion would come from.

And last week, HUD Secretary Jackson would not provide a guarantee to the subcommittee that those severe cuts would not come at the expense of programs serving the poor or even the homeless. Again, it is don't worry about the budget cuts, don't worry about the impact on the poor and homeless, just be happy.

Similarly, within the subcommittee's jurisdiction, the President is proposing a large number of new user fees, fees that some say are just new taxes. These are fees that are not going to be adopted by the authorizing committees and therefore will require discretionary appropriations the President has not requested. In fact, if the past is any guide, it is not clear that the administration will ever get around to even submitting their user fee proposals to the authorizing committees.

When I add together all of these funding holes, I see a shortfall of between $5 billion and $6 billion just for programs under the jurisdiction of this subcommittee.

So I am one Senator who cannot buy into the "don't worry, be happy" attitude of some of my colleagues, and frankly, I am very worried. This subcommittee is facing a very tough road ahead and it will have a painful impact on our communities.

Absent some recognition on the part of the conferees on the budget resolution of the very real holes in the President's budget proposal, I believe that some of my colleagues will be facing a very rude awakening when we get to the appropriations process later this summer.

I would implore my colleagues to stop listening to the music and instead focus on the impossible choices we are setting ourselves up for if we stick to the President's proposed ceiling for domestic discretionary spending.

Mr. Bolten, I also want to question you today about the President's dramatic cuts to the Hanford nuclear waste cleanup. The President's cuts may violate the Federal Government's legal obligations under the Tri-Party Agreement, and I am not going to remain quiet while this administration walks away from its responsibility to the people of the Tri-Cities in my State.

I also want you to know that I am very concerned about the President's budget proposals relating to the Bonneville Power Administration. The White House plan will force higher electricity rates on Northwest residents and on our businesses. I know I do not need to remind you, Mr. Bolten, our region is still really feeling the effects of the Enron manipulation of the market at the same time we are experiencing extremely high gas prices. We have had enough pain when it comes to energy, and we do not need a White House plan that puts energy traders above Northwest citizens and businesses.

Another White House proposal for BPA would cripple our ability to invest in our transmission and generation systems, which will leave our entire region vulnerable to blackouts and higher energy costs.

PREPARED STATEMENT

So, Mr. Bolten, those are some of the things I want to explore with you during this hearing.

Mr. Chairman, thank you so much for holding this, and I look forward to the discussion.

[The statement follows:]

PREPARED STATEMENT OF SENATOR PATTY MURRAY

I want to welcome OMB Director Bolten to the subcommittee this morning. It's been at least 3 years since the OMB Director has appeared before the subcommittee, so I'm pleased that Director Bolten could be with us to discuss the budget request for his own office, as well as the larger budget request of the President for the coming fiscal year.

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Almost all of these amendments were rejected, but still many Senators are telling us: "Don't worry. Be happy," because when Congress gets around to the Appropriations process later in the year, we aren't going to enact those cuts anyway.

Well that doesn't make the problem go away. In fact, it makes it worse.

For example, the Senate failed to adopt an amendment to restore $1.4 billion in spending so that Amtrak could maintain rail service next year. Even though that amendment failed, I have heard a number of my colleagues in the Senate say, "Don't worry. Be happy."; we will find enough money through the Appropriations process to keep Amtrak alive anyway.

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As the Budget Resolution moves toward conference, I am having a very hard time getting my colleagues to understand that the math just doesn't add up. If we are going to adopt a ceiling for domestic discretionary spending that comes close to the President's number, we are either going to have to accept many of his budget cuts, or we are going to have to impose severe cuts in other programs.

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These are fees that are not going to be adopted by the authorizing committees and therefore, will require discretionary appropriations that the President has not requested.

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I would implore my colleagues to stop listening to the music and instead focus on the impossible choices that we are setting ourselves up for if we stick to the President's proposed ceiling for domestic discretionary spending.

HANFORD NUCLEAR CLEANUP

Mr. Bolten, I also want to question you about the President's dramatic cuts to the Hanford nuclear waste clean up. The President's cuts may violate the Federal Government's legal obligations under the Tri-Party agreement. I am not going to remain quiet while this administration walks away from its responsibility to the people of the Tri-Cities.

BPA

I also continue to be concerned by the President's budget proposals relating to the Bonneville Power Administration. The White House plan will force higher electricity rates on Northwest residents and businesses. I don't need to remind you, Mr. Bolten, that our region is still feeling the painful effects of Enron's manipulation of the market at the same time we're experiencing record gas prices. We've had enough pain when it comes to energy. We don't need a White House plan that puts energy traders above Northwest citizens and businesses.

Another White House proposal for BPA would cripple our ability to invest in our transmission and generation systems, leaving our entire region vulnerable to blackouts and higher energy costs. Those are some of the things I want to explore with you during this hearing.

PREPARED STATEMENT

Senator BOND. Thank you very much, Senator Murray. Senator Cochran has submitted a statement which will be included in the record as well.

[The statement follows:]

PREPARED STATEMENT OF SENATOR THAD COCHRAN

Mr. Director, thank you for being here today to discuss the President's budget request. It is a pleasure to work with you as we move forward through the appropriation process.

The President's plan to cut the Federal deficit in half over the next 5 years is laudable and we will work with you to achieve this goal, and I am hopeful that the Senate and the House will agree soon upon a budget resolution that will be the framework for our work for the remainder of the year.

We appreciate your leadership in defining priorities and thank you for the good work that you do as Director of the Office of Management and Budget.

STATEMENT OF JOSHUA B. BOLTEN

Senator BOND. With that introduction, Director Bolten, we would be happy to have your views.

Mr. BOLTEN. Thank you, Mr. Chairman and Senator Murray. Thank you for your warm welcome.

I am, indeed, pleased to be here this morning to discuss the President's 2006 budget request for the Office of Management and Budget and also discuss the broader budget issues that each of you raised in your opening statements.

I would like to begin with a brief review of the President's overall 2006 budget request. The 2006 budget funds efforts to defend the homeland from attack. We are transforming our military and supporting our troops, as they fight and win the global war on terror. We are helping to spread freedom throughout the world. We are promoting high standards in our schools, among many other priorities reflected in the President's budget.

Those policies, especially tax relief, have helped create millions of new jobs, a rebound in business investment, and record home ownership rates. In order to keep our economy strong and achieve the President's goal of cutting the deficit in half by 2009, as you mentioned, Mr. Chairman, we need to continue the President's pro-growth policies and, importantly for this discussion, exercise even greater spending restraint than we have in recent years.

During the first term, the President committed to spend what was needed on the war on terror and to protect the homeland, and he committed to enforce spending restraint elsewhere. Because of this focus, deficits are below what they otherwise would have been. With continuation of the President's pro-growth economic policies and responsible spending restraint now, we will remain on track to cut the deficit in half by 2009 to a level that is well below the 40-year historical average deficit of 2.3 percent of GDP.

The administration proposes to tighten spending further this year by limiting the growth in overall discretionary spending, even after significant increases in defense and homeland security, to 2.1 percent. Mr. Chairman, you highlighted that in your opening remarks, and you did note that that is less than the projected rate of inflation, I believe. If you did not note it, I note it now. So, Senator Murray, your comments, as well, are on target, which is to say that in those non-security areas, the President is proposing a spending level that is below inflation—so a real cut.

In non-security discretionary accounts, the President's proposal would cut spending by nearly 1 percent, 0.7 percent, as you pointed out, Mr. Chairman. That is the tightest such restraint proposed since the Reagan administration.

The budget also proposes more than 150 reductions and eliminations in non-defense discretionary programs, saving about $20 billion in 2006, and an additional set of reforms in mandatory programs, saving about $137 billion over the next 10 years. So, Mr. Chairman, we are not focusing our efforts exclusively on the discretionary side of the budget. We also believe that it is important to begin the process of digging in on the mandatory side.

To ensure the Federal Government spends taxpayer dollars most effectively, the administration continues to implement the President's Management Agenda (PMA). The PMA helps individual agencies and programs focus on and produce results. It promotes this goal through several key components: strategic management of human capital, competitive sourcing, improved performance and reporting standards, integration of budget policy with performance measures, and finally, Mr. Chairman, the one that you highlighted in your opening statement: electronic government, e-government, initiatives, and how we spend our IT money.

OMB has successfully designed and implemented the Program Assessment Rating Tool, or PART, to help agencies measure the success of their programs, focus efforts to improve program performance, and set budget policy accordingly.

Consistent with the President's overall 2006 budget proposal, the Office of Management and Budget has itself submitted a disciplined request. OMB's total budget request amounts to about $75 million, the same as was appropriated for the agency in the 2005 budget process.

To achieve this spending restraint, OMB is pursuing cost savings wherever possible. As in the past, OMB is achieving cost savings largely through reductions in staffing. We are principally an agency of people and that is the only place we can really go to find the savings. Last year, OMB was appropriated $1.6 million less than the President's budget request. In addition, OMB, like other agencies, absorbed a pay raise of 3.7 percent. To accommodate these lower funding levels, we have reduced OMB staff from 527 positions in fiscal year 2001 to 510 positions in 2004 to 490 positions anticipated in 2005 and 2006.

With these lower levels of resources and staffing, we believe OMB can continue to deliver high-quality performance and fulfill our many important core responsibilities. Our best known of these responsibilities is the preparation of the President's annual budget. In addition, our responsibilities include oversight of other budgetary matters, management issues, the administration's legislative proposals, regulatory reforms, procurement policies, and other important subjects. We assure that all such proposals are consistent with the relevant statutes and presidential objectives. In meeting these responsibilities, OMB is prepared to work within the constraints of a tight budgetary environment.

I look forward to working with the Congress and with this committee in particular to develop a final budget that is consistent with our goals of spending discipline and focusing on priorities.

PREPARED STATEMENT

Mr. Chairman, that concludes my prepared statement. I know you and Senator Murray have raised a number of issues in your opening statements. I would be happy to respond to any of them in questions.

[The statement follows:]

PREPARED STATEMENT OF JOSHUA B. BOLTEN

Mr. Chairman, Senator Murray, members of the subcommittee, I am pleased to be here this morning to discuss the President's fiscal year 2006 budget request for the Office of Management and Budget (OMB).

WINNING THE WAR ON TERROR, PROTECTING THE HOMELAND AND STRENGTHENING THE ECONOMY

I would like to begin with a brief review of the President's overall fiscal year 2006 budget. The 2006 budget funds efforts to defend the homeland from attack. We are transforming our military and supporting our troops as they fight and win the Global War on Terror. We are helping to spread freedom throughout the world. We are promoting high standards in our schools. The President's policies in this budget, especially tax relief, have helped create millions of new jobs, a rebound in business investment, and record homeownership rates. In order to keep our economy strong, and achieve the President's goal of cutting the deficit in half by 2009, we need to continue the President's pro-growth policies and exercise even greater spending restraint.

During the first term the President committed to spend what was needed to win the War on Terror and protect the homeland—and he committed to enforce spending restraint elsewhere. Because of this focus, deficits are below what they otherwise would have been. With continuation of the President's pro-growth economic policies and responsible spending restraint, we will remain on track to cut the deficit in half by 2009, to a level that is well below the 40-year historical average deficit of 2.3 percent of GDP.

The administration proposes to tighten spending further this year by limiting the growth in overall discretionary spending, even after significant increases in defense and homeland security, to 2.1 percent—less than the projected rate of inflation. In other words, under the President's 2006 budget, overall discretionary spending will see a reduction in real terms. In non-security discretionary accounts, the President proposes to cut spending by nearly 1 percent—the tightest such restraint proposed since the Reagan Administration.

The budget also proposes more than 150 reductions and eliminations in non-defense discretionary programs, saving about $20 billion in 2006, and an additional set of reforms in mandatory programs, saving about $137 billion over the next 10 years.

DELIVERING RESULTS

To ensure the Federal Government spends taxpayer dollars most effectively, the administration continues to implement the President's Management Agenda (PMA). The PMA helps individual agencies and programs focus on and produce results, and promotes this goal through several key components: strategic management of human capital; competitive sourcing; improved financial performance and reporting standards; electronic government (e-gov) initiatives; and integration of budget policy with performance measures.

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OMB'S BUDGET

Consistent with the President's overall fiscal year 2006 budget proposal, the Office of Management and Budget has submitted a disciplined request. OMB's total budget request amounts to $75.1 million—the same as was appropriated for the agency in the 2005 budget process.

To achieve this spending restraint, OMB is pursuing cost savings wherever possible. As in the past, OMB is achieving cost savings largely through reductions in staffing. Last year, OMB was appropriated $1.6 million less than the President's budgetary request. In addition, OMB—like other agencies—absorbed a pay raise of 3.7 percent. To accommodate lower funding levels, we have reduced OMB staff from 527 positions in fiscal year 2001, to 510 positions in 2004, to the 490 positions anticipated for 2005 and 2006.

With these lower levels of resources and staffing, we believe OMB can continue to deliver high-quality performance and fulfill our many important core responsibilities. Our best known of these responsibilities is the preparation of the President's annual budget. In addition, our responsibilities include oversight of budgetary matters, management issues, the administration's legislative proposals, regulatory reforms, procurement policies and other important subjects. We assure that all such proposals are consistent with relevant statutes and Presidential objectives. In meeting these responsibilities, OMB is prepared to work within the constraints of a tight budgetary environment.

I look forward to working with the Congress to develop a final budget that is consistent with our goals of spending discipline and focusing on priorities.

Senator BOND. Thank you very much, Mr. Director. We look forward to working within that constrained budget for OMB, but I would like to go back to some of the questions I raised in my opening statement.

Please give me your rationale for eliminating CDBG. You just went through a drill with the interested parties to figure out how to make CDBG work better. It has had tremendous impact in many communities, a favorable impact. The joint HUD/OMB Grantee Outcome Measurement Working Group came up with these. We have got communities with existing projects relying on CDBG funding, especially with section 108 loan guarantees. Why did you decide to cut off this program?

COMMUNITY DEVELOPMENT BLOCK GRANT

Mr. BOLTEN. Mr. Chairman, the judgment about the consolidation of these programs, not their total elimination, but the consolidation of these programs into one single place had a lot to do with how we best target our resources. The administration's judgment about how to rationalize the many economic development programs that exist today in government was focused on trying to make sure that we make the best use of the limited resources we have available. We are, indeed, proposing reducing those resources overall, but also targeting those resources on the areas most in need.

Right now, through the CDBG program and the CSBG program, we have a lot of money going out to the States and localities largely on a formula basis with the Federal Government not really able to tell what it is getting for its money. It has become almost an entitlement, if you will, on the State revenue sharing side of the ledger.

What we are trying to do with this proposal is make sure that we are applying the money that we do have most effectively to meet economic development goals. Right now a lot of CDBG money and CDBG money goes toward worthy goals, many of them duplicated in other Federal programs. What we would like to see this money do is not simply support a variety of local safety nets that are provided for those most in need in our country, but ensure that what we are doing with the money is promoting economic development in the community that will make the social safety net less necessary.

Senator BOND. Community development, from my experience, is significantly different than general economic development, what the Commerce Department does. That is why they set up the Department of Housing and Urban Development. From my personal experience, I can tell you that there is a very vital role for communities to play in the community development which develops strong communities in relation to housing.

Essentially you are saying you do not want a Housing and Urban Development Department. You do not want that function. I would think that you would have a proposal to continue the reforms that you have worked out with respect to CDBG to make sure that that program works, unless you honestly believe that community development is not a worthwhile goal. Are you saying that?

Mr. BOLTEN. No, sir, Mr. Chairman. The administration does strongly believe in community development as a worthwhile goal. The question is what to do with our available Federal dollars. As

Secretary Jackson testified before you, he said that he thought the CDBG formula approach has become less targeted than it ought to be on those communities with real development needs. The consolidation of all these programs in the Commerce Department, which has the best experience with creating public/private partnerships to promote economic development, is the approach that the administration has chosen to try to target those needs.

A lot of communities, we believe under the proposal we have put before you, will actually end up with more money than they do under the existing formulas. What we are trying to do is make sure that those communities most in need and those most likely to make good use of Federal dollars in promoting an environment where there are jobs, where there is housing, that is where we are trying to put the money, and that was the purpose of the proposal that the President put before you.

Senator BOND. I just think that is flat wrong.

Let me ask you about the practical problems. HUD staff has experience and expertise, local relationships. How do you expect the Commerce program to implement the program in 2006? You have left the salaries and expenses in CDBG for administering the program. Do you expect to take the CDBG staff into Commerce? How are the communities which use section 108 loan guarantees going to be made whole? These are some real practical problems I see.

Mr. BOLTEN. There are some important practical problems, Mr. Chairman. It has been our contemplation to move some of, at least, the core staff over to the Commerce Department. Should the Congress in its wisdom decide to support the President's proposal, I can assure you, we will work very closely with you and other interested members to make sure that the transition is smooth and not disadvantageous to any of the programs involved.

Senator BOND. Thank you, Director.

Senator Murray.

AMTRAK

Senator MURRAY. Mr. Bolten, for some time now, I have been trying to figure out who really speaks for the administration when it comes to your budget and policies for Amtrak. As you know, your budget requests zero for Amtrak, and the President's budget states explicitly—and I want to read it. It says, "With no subsidies, Amtrak would quickly enter bankruptcy which would likely lead to the elimination of inefficient operations and the reorganization of the railroad through bankruptcy procedures. Ultimately, a more rational passenger rail system would emerge."

Now, I have heard it on good authority that your administration's stated expectation to put Amtrak into bankruptcy was not crafted by anyone at the Department of Transportation but was, rather, crafted in your office. Secretary Mineta has been crossing the country making speeches and telling the press that it is not the administration's goal to put Amtrak into bankruptcy.

Can you tell me this morning, is this language in the President's budget correct, or is Secretary Mineta correct?

Mr. BOLTEN. Well, I think, Senator Murray, they are both correct. All of our proposals, are prepared in close coordination between the relevant agencies and OMB. It is not the objective of the administration to put Amtrak into bankruptcy, but having failed for several years now to achieve the kinds of necessary reforms in the Amtrak system, we felt that at this point we have no alternative but to propose a budget that may, indeed, have that effect in order to get the kind of action and reform that we need.

I thought Secretary Mineta put it very well in a New York Times op-ed that he published about 2 months ago. He said, "there are some who have suggested that our reforms are aimed at killing Amtrak. Not true. If we wanted to kill Amtrak, we would not have to lift a finger. We cannot save intercity passenger rail service by burying our heads in the sand and simply shoveling more money into a system that cannot help but fail."

Senator MURRAY. Well, can you answer me, does the administration want to reorganize Amtrak in bankruptcy or keep it out of bankruptcy? Which one?

Mr. BOLTEN. We would actually be happier to do it without a bankruptcy, but our proposals to do it in that fashion have so far——

Senator MURRAY. So you intend to have it in bankruptcy to reorganize it.

Mr. BOLTEN. We believe it needs to be reorganized one way or the other. If bankruptcy is the only option, then we believe that if we are to be responsible with the taxpayers' dollars, that is the only way to do it.

Senator MURRAY. Earlier last month, Secretary Mineta had an interview with National Public Radio on the administration's plan for Amtrak, and the NPR reporter pointed out that the President's budget requests zero for Amtrak, and then he asked, what is the real figure that the administration is willing to spend on Amtrak? Secretary Mineta answered, probably in the area of about $1.5 billion to $2 billion, and then he went on to point out that Amtrak was woefully behind in maintaining tunnels and other infrastructure under its control.

Do you concur with Secretary Mineta's remarks that the administration is willing to spend between $1.5 billion and $2 billion on Amtrak next year?

Mr. BOLTEN. I do not want to put a specific figure on it at this point, but the administration is, indeed, prepared to spend more money on Amtrak in the future if we get a rationalized system that does, as Secretary Mineta was suggesting in his remark, suggest on making sure that the infrastructure is in place for the continuing effective operation of those portions of Amtrak that can be commercially competitive. But what that requires is a complete reorganization and restructuring of Amtrak so that we do focus our resources on those portions that can, in fact, be commercially competitive. That is a lot less than what is currently out there and which has been persistently subsidized with taxpayer dollars without any prospect realistically at this point of ultimately achieving what was the original objective of Amtrak, which was putting this rail system on a commercially sound basis.

Senator MURRAY. Well, earlier this year, I was very critical of Amtrak's board of directors. For the first time, that board to failed to articulate a budget request to Congress at the beginning of the year as it is called to do in the Rail Passenger Service Act. It appeared to me that since every one of the Amtrak board members are now Bush appointees, they did not want to articulate a budget that was different from the President's.

Today, however, in the Russell Senate Office Building across the street from us, the Amtrak board is revealing its own reform plan for the railroad to the Senate Commerce Committee. The Amtrak board chairman is testifying that the board is requesting the Appropriations Committee provide $1.82 billion for the railroad for next year. That is more than a 50 percent increase over the current level of funding. The board will argue that reforming Amtrak costs money and that the railroad simply cannot survive on its current level of spending.

In fact, the DOT Inspector General is going to testify this morning as well that simply maintaining the current Amtrak system will require an increase of between $200 million and $300 million above the current funding level.

Mr. Bolten, now that the board of directors, made up entirely of the President's appointees, has articulated a funding request to Congress, is OMB prepared to submit to us a funding request to Congress for Amtrak?

Mr. BOLTEN. Senator Murray, we have submitted the President's funding request for Amtrak to the committee.

Senator MURRAY. For zero.

Mr. BOLTEN. We have included about $300 million for the maintenance of some intercity rail in that category.

While I have not had a chance to review what the board is presenting, I am told that they do have some important steps forward in reform. We obviously do not agree with them on the amount of money they want to put in, but there are enormous anomalies in this system that need, I think at this point, urgently to be corrected——

Senator MURRAY. So you will not endorse the $1.2 billion that they are asking for?

Mr. BOLTEN. No, I will not, Senator.

Senator MURRAY. Well, our committee is going to mark up the appropriations bill likely in July. Can we expect you to submit a budget request for Amtrak by the July 4th recess?

Mr. BOLTEN. Senator, you have our request before you.

Senator MURRAY. Which is zero.

Mr. BOLTEN. For those portions of Amtrak not related to intercity rail, yes.

Senator MURRAY. Well, that is going to make it very difficult, Mr. Chairman.

Senator BOND. Thank you, Senator Murray. That is the question I was prepared to ask. When are we going to see a responsible proposal for reform from the administration? This proposal to push Amtrak into bankruptcy could cause tremendous disruption. They have mortgaged Penn Station. This is a disaster. I would be willing to work with you on a responsible reform program, but to zero it out, the costs are going to be significant. The Acela trains are out of operation now. That is 20 percent of the revenue. We have got a disaster on our hands, and throwing $364 million at intercity service, when you have the tremendous costs that the bankruptcy of Amtrak is going to cause, without any responsible plan for reform, just is not credible.

I hope that with the Commerce Committee and the administration's recommendations, we will get some kind of realistic proposal prior to our marking up in July because I do not know what we can do with the request that you presented. It is designed to fail. So anyhow, you made your point, but I tell you that this is a disaster that is going to focus right on OMB and the person who controls it.

Let me move to other block grant issues. The Capacity Building LISC/Enterprise program and CDFI are very important. The Bank Enterprise Act gets banks into underserved areas where there are no traditional financial institutions. LISC provides significant funds to provide nationwide leadership for developing and training existing nonprofits. This gives them an opportunity to compete for block grant funds.

Why are you backing away from these programs and why do you think it is time to cut off funding for these elements that are essential in underserved areas?

Mr. BOLTEN. Mr. Chairman, I am not in a good position to speak to all of the individual details of those, but I know that the judgment of those who put this program together was that we could best serve all of those needs through one consolidated program. I believe a lot of those needs and desires can still be met through the consolidated program we have proposed at the Commerce Department. I would like to give you more information, if I may, for the record.

[The information follows:]

STRENGTHENING AMERICA'S COMMUNITIES

The President's Budget supports the Federal Government's role in economic and community development. The current Federal approach is not optimally designed to achieve results for our communities. During 2004, the administration reviewed the effectiveness and structure of Federal economic and community development efforts and found several weaknesses in the current design of these programs. The Strengthening America's Communities Initiative (SACI) proposes to consolidate 18 programs into a unified grant program. The new program, within the Department of Commerce, will clarify the purpose of Federal development assistance, simplify the grant process, target funds to those communities most in need of assistance, and hold grantees accountable for results in exchange for flexible use of the funds.

While some individual programs or projects within our communities have been successful, the delivery of such resources is often duplicative and overly complex. The administration believes there is a better way. If one were starting from scratch, no one would design a Federal assistance system that has 18 grant programs spread across five cabinet agencies. The administration believes local flexibility is more effective than Federal control. Economic and community development activities such as those provided by the LISC/Enterprise and CDFI programs, which you mentioned, will remain eligible activities under SACI. In exchange for this flexibility, SACI will include accountability measures that require communities to demonstrate progress toward locally-selected goals for development. The administration also believes that eligibility and funding criteria should target communities that are most in need of assistance.

We look forward to continuing to work with the Congress to determine ways to improve the Federal approach to economic and community development to ensure that taxpayer resources are spent not on wealthy communities, but on the distressed. In the end, these investments should generate measurable results for low-income persons and economically distressed areas.

Senator BOND. Well, I do not see how that is going to work.

This is a good one: where are you going to get the $2.5 billion from the housing certificate fund, Section 8? I assume that you have some rationale. Where are these rescissions going to come from? Where is that money?

Mr. BOLTEN. Mr. Chairman, the figure we proposed for rescissions is, I believe, consistent with the historical range of rescissions that have been available each year.

Senator BOND. That is before we reformed the program. Mr. Director, we reformed the program because there were these problems. We reformed it so that we would not have these huge rescissions. And now you are assuming that the program operates as it has in the past, but we worked with HUD and reformed the program. And I do not know where you are going to find them. Historically they were there. Now they are not there.

Mr. BOLTEN. Well, we believe, Senator, that they are still there, that there still will be substantial unobligated balances. Whether the exact figure ends up being $2.5 billion or not may be open to discussion, but we believe that even with the reforms in place, there will be substantial balances available——

Senator BOND. Well, I will be most anxious, and I am sure by July 1 you and HUD will be able to tell us where that money is.

Mr. BOLTEN. I expect we will know quite a bit more by July.

Senator BOND. If you would give us the methodology for the record. I would like to know how you are coming up with it because I do not believe it is there.

[The information follows:]

HUD RESCISSION

Each year, since 1998, large rescissions have been taken from this account—an average of $2 billion per year. These funds represent recoveries of amounts previously appropriated and obligated that are in excess of current needs.

[In millions of dollars]

Fiscal Year	BA (Pre-Rescission)	Rescission
Fiscal year 2001	13,941	(1,947)
Fiscal year 2002	15,641	(1,589)
Fiscal year 2003	17,112	(1,600)
Fiscal year 2004	19,257	(2,844)
Fiscal year 2005	20,064	(1,557)
Fiscal year 2006 proposed	20,917	(2,500)

As is the case each year, HUD may have a general idea ahead of time, but they will not determine which funds from which accounts will be used to satisfy the rescission until June or July of 2006.

While the estimate of excess funds available for rescission may change, there is every reason to believe based on past experience that sufficient funds will be available for rescission.

In addition, the final appropriations language has been sufficiently broad, and the President's Budget requests similar language again for fiscal year 2006, to enable the Department to look to other sources of funds to rescind within the Department should there be insufficient funds within this account. In 2003, for example, Congress enacted a rescission of $1.6 billion which was satisfied with $1.17 billion in unobligated balances in the Section 8 account and $426 million in unobligated balances from other accounts.

AIP PROGRAM

Senator BOND. Let me ask you, before I turn it over, about the AIP program. This cuts the entitlement for primary airports to be cut in half. The Alaska airport supplemental is reduced by 50 percent. Why did you decide to cut this program?

Mr. BOLTEN. Mr. Chairman, let me give you a response on that for the record.

[The information follows:]

AK AIRPORT (AIP PROGRAM)

The 2006 Budget provides $3.0 billion for the Airport Improvement Program (AIP). These resources are sufficient to fund construction of all planned new runways and tarmacs, and remain high compared to historical levels (as recently as fiscal year 2000, the AIP program was funded at $1.9 billion). The Budget also includes language that should alleviate your concerns about the entitlement for primary airports and the Alaska airport supplemental. Under the approach included in the Budget, the basic structure of the entitlement formulas are preserved with airports experiencing very modest reductions (less than 10 percent) in entitlement amounts. The Alaska supplemental would fare even better, with no loss of funding.

Senator BOND. All right.

I see that Senator Bennett has joined us, but I will go on to Senator Murray for the next question, and then turn to Senator Bennett.

Senator BENNETT. Thank you.

Senator MURRAY. Thank you, Mr. Chairman. Let me just echo the chairman's remarks. I look forward to seeing the list from you and Secretary Jackson on where those rescissions are going to be before our markup. I simply do not see how we can do that without your request in.

But I want to go back to one thing on Amtrak before I move on. The $360 million that you were talking about in the budget is by law just for mass transit systems—I know you understand that—operating over Amtrak property. It is not for Amtrak trains. So the issue we are concerned about is what the board is testifying before Commerce today and those needs.

Let me ask you one other question on Amtrak. It is my understanding that the brake problems that have been discovered with the Acela trains that we are hearing so much about is not going to be reparable very quickly. In fact, the Acela trains may stay parked, we hear now, for some months, and Amtrak may lose as much as $60 million in net revenue as a result. That additional $60 million loss may eat up almost every dollar of working cash that the railroad can generate prior to the beginning of next fiscal year. I wanted to find out if your agency was monitoring that situation and the revenue impact on Amtrak.

Mr. BOLTEN. We are monitoring it. We do know that they have some working capital available carried over. I had heard even a slightly larger figure than $60 million was possible. I know they are carrying over some working capital in that range, but Senator, we will keep an eye on that situation.

Senator MURRAY. It is my understanding Secretary Mineta is saying he does not want to put Amtrak into bankruptcy. So is it possible that you are considering a supplemental appropriation to deal with this dramatic loss of revenue?

Mr. BOLTEN. We are not considering one at this time, but we are monitoring the situation.

HANFORD SITE

Senator MURRAY. Okay. I appreciate that.

I wanted to turn to a different topic for a minute and ask you, while you are here, about the budget for the cleanup of Hanford nuclear reservation. You may know that in the past month we have had over 1,200 workers at Hanford who have received their layoff notice, and some of those are attributable to seismic issues at the waste treatment plant. Others are attributable to the fact that funding shortfalls are expected in fiscal year 2006.

This year the budget you sent over cuts funding for environmental management programs by $548 million nationwide. Hanford alone makes up $297 million, about 54 percent of that cut in funding. And we want to know why in my State you are proposing cuts that are falling so disproportionately on Hanford compared to other sites in the Nation?

Mr. BOLTEN. Senator, let me come back to you with a more detailed response, but my recollection about that situation was that that was a judgment about how much could reasonably be spent in the coming year, that there has been, I believe, over the several recent years an acceleration in spending on the Hanford cleanup, and that the folks who have worked with the spending flow on this believe that this was a reasonable amount to be spending in this year and still keep us on track to getting the cleanup done on time.

[The information follows:]

HANFORD

The budget requests funding to meet the administration's commitments for cleanup at nuclear sites, recognizing that uncertainties can limit cleanup activities. The President's request for fiscal year 2006 for Hanford is $1.8 billion, a 20 percent increase above the fiscal year 2001 enacted level. At Hanford, there are legal uncertainties associated with tank closures brought on by Washington State Initiative 297 and related lawsuits, which have introduced uncertainties in the areas of waste importation, permitting, and waste retrieval and disposal activities. Additionally, since the State of Washington was not included in section 3116 of the Ronald W. Reagan National Defense Authorization Act for fiscal year 2005, which resolved radioactive waste classification issues in Idaho and South Carolina, the administration is evaluating how to proceed.

The 2006 budget request takes into account these legal uncertainties. It also reflects completed work associated with the waste tanks, including removing liquids from the single-shell tanks.

Senator MURRAY. Well, I do not understand how the Federal Government is going to meet its legal requirements under the Tri-Party Agreement with funding cuts of that size. I assume you are aware of the Tri-Party Agreement.

Mr. BOLTEN. I am.

Senator MURRAY. The DOE's contract for a waste treatment plant calls for Bechtel to receive $690 million each year, and that steady multi-year stream of $690 million per year was chosen to avoid a situation where there would be huge year-to-year swings in the funding that is required to complete the plant. But for fiscal year 2006, the administration wants to provide $64 million less than the contracted amount. So the President's budget really appears to be guaranteeing a delay in the start of the waste treatment plant, and that is in violation of the Tri-Party Agreement.

Can you guarantee me that the administration will request funding above the $690 million level in future years so we avoid a delay of the waste treatment plant and keep its word with the Tri-Party Agreement?

Mr. BOLTEN. I am not in a position to guarantee you what specific funding levels will be in any particular year, but I would like to come back to you and show you and your staff the spending stream that the Department of Energy has proposed to ensure that we do get the Hanford site cleaned up within the scheduled——

Senator MURRAY. Okay. Well, I would very much like to meet with you and go through that because I do not see how on earth we are going to meet the legal requirements of the Tri-Party Agreement with these funding deficits. So I would appreciate that.

Senator BOND. Thank you, Senator Murray.

Now we turn to Senator Bennett. Since we have had a couple of rounds, if you would like to take two rounds, we will give you the opportunity to explore your areas of interest with the Director.

Senator BENNETT. Thank you very much, Mr. Chairman.

Mr. Director, you know, but we acknowledge, you have one of the toughest jobs in Washington, and it is always easy to be a politician when there is a surplus because you can meet everybody's needs and be a hero. When you are fighting a deficit, it is always difficult, and to use the label of an old movie, you become Dr. No. That is a tough position to be in. I sympathize with you.

You have been around town long enough to know that you are being set up when I make those kinds of kind comments in advance of where I am going.

Mr. BOLTEN. Senator, you missed the earlier part of the hearing in which Senators Bond and Murray where kind enough to skip those comments.

They moved directly to what follows.

STRENGTHENING AMERICA'S COMMUNITIES INITIATIVES

Senator BENNETT. They moved directly to it. All right.

I am chairman of the Agriculture Appropriations Subcommittee. The President's budget requests no funds at all for the Rural Business Opportunity grant program, Rural Business Enterprise grant program, Rural Empowerment Zones, and Enterprise Community grant program, all of which are administered by the Rural Development at USDA.

The budget does propose a newer and smaller community development grant program to combine these programs with others to be administered by the Department of Commerce. I wonder what expertise the Department of Commerce has with respect to rural community development that causes you to take this out of USDA and put it in Commerce because the pressure, obviously, is on me to find those funds, to take care of it in agriculture. Have you proposed an increase in Commerce to make up for the fact that this money is all taken away from USDA, or am I getting into the weeds and something you are not personally familiar with?

Mr. BOLTEN. No, sir. I am not intimately familiar with the individual programs, but overall we have proposed a consolidation of many programs, about 18 programs, spread across at different agencies, including the Agriculture Department, but primarily from HUD, into the Commerce Department. One of the reasons why we have chosen to implement a consolidation in the Commerce Department is that that is where there is, we believe, the best expertise on economic development overall, whether it be rural or urban, and also that it is an agency that is accustomed to promoting public/private partnerships, which we believe are part of the answer toward achieving economic development in areas that have lagged so far.

Senator BENNETT. All right. I suppose you are not the person for me to ask this, but before I can be comfortable in straight-arming everybody who has typically come to the Agriculture Subcommittee for this kind of support, I think I need to have some reassurance from the Department of Commerce that they do know what they are doing and they are not just going to cut this off willy-nilly and say, okay, you are out because we have consolidated and then we are going to take what money we have and it is less money overall and give it to the programs we are familiar with, and because rural America is the stepchild, we are just going to say you are out and injured.

You are not the one to direct the Commerce Department to come talk to me, but I think I will use your answer as a reason to say to them, you ought to be talking to our subcommittee and telling us what you are going to be doing in these areas because cutting them out entirely from the President's budget, without the kind of explanation you have given us here, has caused great angst, as I am sure you can understand.

Mr. BOLTEN. Senator, I think it is a legitimate question and I will take the opportunity to ask Secretary Gutierrez to be sure that you are fully briefed on how they would intend to deal with the situation, in which we acknowledge we are consolidating programs with less money available, but what we will be trying to do is target Federal monies where it is, (A), likely to be most effective and, (B), to areas of the most need.

CDBG FUNDING

Senator BENNETT. That leads us to what I assume may have been raised before I got here. This is CDBG money with respect to HUD. Can you tell us in what way CDBG has been considered ineffective? I understand that word has been used to describe it. If I am covering ground that has already been covered——

Senator BOND. We have asked the question and have not gotten any answers.

Senator BENNETT. There is no such thing as repetition in the Senate.

So I would like to hear your rationale.

Mr. BOLTEN. Senator, the question has not been asked in quite that way.

I believe the formal rating of the CDBG program from our assessment system was "results not demonstrated" because what goes on with a lot of the CDBG money is that it goes out by formula to localities, and the Federal Government then has no particular way to track what happens to it and, most important, what sort of results are being achieved with the Federal money. It has become essentially a Federal revenue sharing program.

What we are trying to do with the President's proposal of consolidating these various programs, including CDBG, into the Commerce Department is ensure that we focus our resources where we believe they can be most effective, where the Federal Government can track results, and insist on accountability for the use of the money rather than just sprinkling around funds to what, in many cases I am sure, are laudable goals but not necessarily the top Federal priority nor in a way that permits the Federal Government to tell the taxpayers how the money is being spent.

Senator BENNETT. Again, that sounds very logical, and once again, there is great angst on the part of people involved in the program—they are not only laudable, but in many cases absolutely essential, particularly in housing—that somehow the Commerce Department is not the place where they feel comfortable going with their concerns.

I am perfectly willing to support something that says just because inertia has kept it one place, does not mean it needs to stay here. I know how damaging inertia can be. I tell people the problem with inertia is not inertia at rest, which is the accusation that is usually made about civil servants. It is inertia at motion, that a body in motion tends to stay in motion and in the same direction, long after the direction ceased to make sense. So I am very sympathetic with the general position you have just outlined.

But that having been said, there are a lot of folks who are very, very concerned that the Commerce Department has no sympathy or no understanding or no expertise with which to deal with housing problems.

I am as anxious to make sure that we get our financial house in order in a macro sense as anybody, but I see the specifics of the people who are living on the edge and literally from year to year in terms of their Section 8 funds, their affordable housing. It is frustrating that we cannot give them any sense of permanence. And these are not people who are living well by your standards or mine. They are living very much on the edge, and every year the Congress has to rescue the housing funds that tell them you can stay in your home for 1 more year before this program is going to be challenged again and show up in the budget thing. And they show up in my office in Salt Lake with "am I going to be able to keep my house? And if I cannot, I have no idea where I am going." These are people in their 70's and 80's who are hanging on, as I say, from month to month. Every year I say, well, I will talk to Chairman Bond, and every year Chairman Bond comes through. So I am a hero in Utah because of the work he does here.

What reassurance can we give these people in this kind of situation that Commerce has the expertise, has the understanding, has the concern that these programs represent?

Mr. BOLTEN. Well, first of all, I think the kinds of concerns you identified should be addressed through the housing programs that are specifically directed toward that. But beyond that——

Senator BENNETT. Yes, but they need the money and the money gets chopped off every year or cut back every year. And we have to restore it in this committee.

Mr. BOLTEN. But I believe that is an issue separate from the CDBG issue where the money is going out to community development organizations. I will ask Secretary Gutierrez to address it with you when he speaks about the agriculture side, but I think Secretary Gutierrez can give good comfort about how they would handle the community development needs that are intended to be addressed by CDBG.

Senator BOND. Thank you very much.

Senator BENNETT. Thank you, Mr. Chairman.

Senator BOND. Senator Stevens.

ESSENTIAL AIR SERVICE

Senator STEVENS. Thank you very much.

Mr. Director, it is nice to be with you today.

I too have some problems, but each of them requires a little recitation of history. The first is Essential Air Service. When we decided that we were going to terminate the old Civil Aeronautics Board, which directed that every place that wanted air service would get it, and it got it at a substantial cost to the Federal Government indirectly, we created this program to assure that the small areas, which would lose air service because they were not economical, would have at least a minimum amount of service.

In my State, as you know, 78 percent of the travel between cities is by air because there are no roads. Congress made a decision a long time ago not to build roads, particularly after about one-third of our State was withdrawn for wild and scenic rivers and parks and wildlife refuges, et cetera. It would be very difficult to get through them, and the roads would have to go around those things.

This has been a very meaningful program in my State and, as a matter of fact, is the only lifeline for many people who live in the villages, of which we have 231 now. The difficulty is this. We also tied together the Postal Service delivery of mail to those places by creating the bypass mail system which requires that the postal cargo go to hubs and from those hubs, they fly out the mail to villages. We tie the two together so we have passenger seats and cargo going at least three times a week to these villages. That is their total lifeline.

Some of them were supported for many years by riverboats or boats that went up and down the coast, which as you know, is half the coastline of the United States. There was one boat that went up one time and came back called the North Star.

Now, it looks like it is an expensive program, but if you do away with it, the costs are going to be extremely higher. We still have the responsibility to deal with those places, and most of the travel through that area is somehow or other federally supported anyway through BIA, the Indian Health Service, and others. Unless you want to buy some airplanes and fly BIA around or fly the Indian Health Service around, the cheapest way to do it is through combining both the mail and cargo and passenger service. It cannot work unless you have the Essential Air Service contribution.

Now, you have a proposal that requires matching funds and the assistance depends upon the distance to the nearest large or medium airport. Well, we are, as you know, one-fifth the size of the

United States. Some of those villages are 500 miles from the nearest real airport and a couple of them even further than that.

I would urge you to look at this. I understand your concept of having in some areas, where they have a capability of contributing local matching funds, that it might be possible. But in areas such as ours where the principal beneficiaries of these are the native villages, the application of your new principle will just increase Federal costs. You will be chartering airplanes if you do not buy them. I would urge you to take a look at that.

Only about 35 of the communities actually benefit from the program but they are communities that are tied into the bypass mail system too. There is a joint subsidy to maintaining this traffic. And I will not ask for an answer to that because I just think you ought to take a look at it and study it.

Mr. BOLTEN. We will take a look at that.

EDA

Senator STEVENS. Now, next is the EDA. As the State that is coming into the 21st century after everybody else, we just came on board with EDA in recent years. It really does not even have an office in the State. It came to us from either San Francisco or Seattle, and those people came up at fishing time and they looked around and put a few bucks around the place, but they really did not plan how to bring these communities into the 21st century.

Some time ago, I negotiated with the Department and we agreed to an obligation that they would put $15 million in funding for development projects for Alaska over a period of years. This is the last year of that. But we got that deal because we showed them that we had been totally left out. Either we are going to have some economic development that helps these people come into the private sector and be contributors, or they are going to continue to be one of the faucets we have to turn on and off in terms of Federal assistance forever.

Again, I urge you to take a look at the problem of elimination of the EDA in terms of our area. It is just unfair. Hawaii and Alaska became a State in 1959. A lot of the Federal officials did not even discover us until 1969, and that is when a brash, young lawyer came to the Senate.

Senator BOND. They have been paying attention ever since.

Senator STEVENS. They have been paying a little bit of attention, but it took them 20 years to wake up.

RURAL COMMUNITY ADVANCED PROGRAM (RCAP)

Thirdly, the elimination of the rural community advanced programs, the RCAP, within the agriculture bill. Here again, we have two monstrous areas that are capable of agriculture production. We finally have one agriculture county station in Alaska. We have one and they get limited assistance. But we have been using the rural community development grants and some of these others to reach out to the villages and provide them with basic sanitation, basic clean water, and basic concepts of maintaining health. The result: we have reduced the cost to the Indian Health Service. We have increased the performance of these children in school. And now, along comes the concept that this is going to be done away with.

There is one in particular, the high cost energy grant. We have places that are paying $5 a gallon for fuel. They are paying 28 cents probably in the rest of the States. We have been trying to construct local power plants using local fuels to try and see if they can get away from buying and having fuel transported. All that is transported in there is at government expense. So again, by eliminating this program, we are eliminating the inching that we are doing, inching away from total Federal dependency on their lives.

I would like for you to sit down and talk to some of your people sometime.

By the way, most people do not know it, but some of the outer islands of Hawaii have problems very similar to ours. That is why the four of us are with each other all the time because we have similar problems. Actually Hawaii is larger than Alaska, if you fill in the water in between the islands. You know what I mean?

They have problems out there in the periphery that are as bad as ours along the coasts and in the interior and up along the Arctic coast.

Those two offshore States need this program. We need a way to try to find a way to discuss it with your people because, not meaning to be offensive, but your recommendations are one-size-fits-all.

Senator BOND. Mr. Director, I would suggest that this is an opportunity for you to schedule a meeting with Senator Stevens, Senator Murkowski, Senator Inouye, Senator Akaka. I think it would be a very informative session for you. I wish I could be a fly on the wall to watch, but I would urge you to have that.

Senator Kohl.

Senator STEVENS. Just so you know, Josh is a close friend, as a matter of fact, and I hesitate to make these suggestions to him in public. I probably could have made them in private, but I want them on the record anyway, Josh.

Senator BOND. As they say in the business, harsh letter to follow.

Mr. BOLTEN. I always look forward to an opportunity to engage with Chairman Stevens.

Senator BOND. Director Bolten is a good friend. You ought to see how we treat our enemies.

Senator Kohl.

MANUFACTURING EXTENSION PARTNERSHIP (MEP)

Senator KOHL. Thank you, Mr. Chairman. Mr. Bolten, over the past several years, the administration has attempted to slash funding for the Manufacturing Extension Partnership program, which is a program that helps small and mid-sized American manufacturers to modernize in order to compete in the global marketplace. MEP has a proven track record I think that you are aware of. They have consistently demonstrated their ability to create jobs and improve profits of these companies. I have visited many of them around my own State, but there are indications that are very clear that they replicate this kind of success all over the country. I do not understand why that program, which has been so successful, is really a program that, for the most part, the administration has indicated they want to terminate.

The funding for the program has been just at over $100 million over the last several years. It is also funded at the State and local levels. It is also paid for, in small part, by those companies that use it. So it is a good program and it is not a really expensive Federal program, but it does have good dividend returns.

Maybe you could make a comment on it. We are still trying, as you know, in this budget this year to restore the funding. It was cut down to something like $39 million or $38 million, which spread across 50 States really is not sufficient. We want to get that restored to where it was, $112 million. Can we hope that you will support this effort, which is relatively modest, but I think it is significant in terms of protecting manufacturing jobs in this country and growing that part of our economy?

Mr. BOLTEN. Senator, the MEP program is one that I have had a number of very strong anecdotal reports about, about success stories there. In many respects, it is the kind of program in an unconstrained budget environment you might like to continue. But the program was originally intended, as it was originally set up, ultimately to be self-sustaining through fees paid by those that take advantage of its services. The administration would still like to move it to that basis.

It was funded this past year, I believe, at just over $100 million. The year before that, the Congress funded at about $40 million, which is the request that the administration is making this year. We are not proposing total termination this year. We have proposed a substantially reduced funding level in part because of the many strains that you have seen exhibited even here at just this one hearing, the many strains in the budget, where we need to set priorities and allocate our Federal dollars, our taxpayer dollars, where we think they can make the most good and where they are the most needed.

The MEP program has good anecdotes, produces some good results, but I think it is also a program that can meet the needs of its constituency hopefully ultimately on a self-sustaining basis, which is why we have proposed that for this year, it be cut back to the level that it was funded at year-before-last.

Senator KOHL. Well, ultimately it is a judgment and you all submit a budget that represents your best judgments, and I do respect that. As you know, you can be right and you can be wrong. I have given a lot of attention to the program, and I am utterly convinced as a businessman that it really returns dividends for the money that is spent, and that the money that we are spending at the Federal level is relatively modest. To signal that the government is going to get out of that business and either it will be self-sustaining or funded at the State and local level or it will go out, which is what that judgment means, I do not think is the correct decision to be making. I wish I could convince you that the program really deserves to be supported at its modest levels and not jettisoned. I will just continue to work on that and I hope that we can have some success.

The anecdotal evidence that you point to is really more than anecdotal. There is solid evidence that the program is effective and works. Solid evidence. It is not just anecdotal. So in that light and considering the fact that we are working so hard to maintain our job base in that part of our economy, I guess I do not fully understand why you all decide that you want to basically get to a termination of Federal support for that program, except that you are saying—and I have heard this from others who have preceded you in defending your decision—that is just our decision. You say we have heard evidence that it works. We have heard evidence that it is a good program. Nevertheless, we want to get to the point where we defund it. And it is the manufacturing sector. I do not quite understand.

Mr. BOLTEN. Well, Senator, it is really a question of priorities, that we believe that this program can be self-sustaining, that it does get resources from States and localities, that our Federal dollars are better spent on other priorities.

One of the priorities of this administration is, indeed, to make sure that our manufacturing sector, especially those involved in exports, remains strong. Secretary Gutierrez I know is devoting a lot of time and energy to that, and he has a new Assistant Secretary who focuses on those issues.

One of the important initiatives that we are undertaking right now at OMB is we have taken in a review of regulations that are regarded by the manufacturing community as impeding their competitiveness, especially internationally, and we are reviewing those for ways in which we can, without undermining other health and safety objectives and environmental objectives, free up our manufacturing community to be more effective and competitive. We hope to get your support in that undertaking as well.

Senator KOHL. I thank you, and Mr. Chairman, I thank you.

PART PROGRAM

Senator BOND. Thank you very much, Senator Kohl.

Mr. Bolten, I commend you for your emphasis on the PART program. I think it is very important that you determine what programs are effective. I note that the National Science Foundation, which I said earlier is extremely important in our ability to lead the world in science and technology, has the future of the U.S. job market and economy in its responsibility. We are seeing India, China, and Japan quickly outpacing the United States with developing scientists and engineers and the skills that go along with them. And the Program Assessment Rating Tool, the PART, has found NSF to have one of the strongest report cards. Parenthetically I would note that OMB has one of the weakest report cards.

Could you explain to me why you have chosen, when you are supposedly establishing priorities, not to put any priority on this institution which holds the future growth and development of our country in its grasp?

Mr. BOLTEN. Mr. Chairman, let me begin by associating myself with the remarks that you made in your opening statement about the importance of the physical sciences to our economy, to the future competitiveness of our economy. What we did in this budget was we did increase NSF funding by 2.4 percent overall.

Senator BOND. Whoopee.

Mr. BOLTEN. I note, Mr. Chairman, that you said whoopee to that.

Senator BOND. We will strike that from the record.

Mr. BOLTEN. I would like to request that it remain in the record, because in the current budget context, whoopee for 2.4 percent is actually appropriate. We are in a budget context where we are cutting the non-security elements by a real 1 percent, a nominal 1 percent, a real cut larger than that, when you factor in inflation. So when we are growing an agency by a substantial part of the budget by 2.4 percent, I think in this context that is an expression of support.

In an unconstrained budgetary environment, would we like to see more money going into those programs that PART so well as NSF does? I personally would. I appreciate your comments about the PART system and how we are trying to use it to inform budgetary decisions so that we focus our dollars on programs that are working. NSF appears to be working. And I would like to see us in a situation where we are able to give them the resources they need going forward.

FEDERAL IT PROGRAM

Senator BOND. I am from the Show Me State, Mr. Director, and I would like to see that in the budget recommendations and not just in our discussions.

I mentioned the Federal IT programs. I am sorry we are missing the OMB hearing in the Committee on Government Reform on the House side on whether OMB is properly managing the $65 billion in IT spending. The committee says OMB did not develop a single aggregate list identifying projects and the weakness. OMB has not developed a structured, consistent process for deciding how to follow up on corrective actions that it has asked agencies to take. And the GAO is going to be giving a report.

Can you give us a brief idea of what you expect to do in this IT area? It is a significant challenge. What do you intend to do on it?

Mr. BOLTEN. Thank you, Mr. Chairman. I have not had a chance to review, I think it is, a GAO report that is being discussed over on the House side. I will review it and we will take its recommendations seriously and factor them into our process going forward.

I will say that this administration has put a great deal of focus on the management of IT, which is a huge part of our budget, as you mentioned in your remarks, and one that has been seriously challenged for many years. It is not a problem that can be fixed overnight.

But the President felt that it was an important enough part of good management of the government that he made it one of the five areas that we rate in our President's Management Agenda. We use those scorecards now, the ones that you referenced in your previous question. We use those scorecards to keep track of how agencies are doing and we try very hard to instill in the agencies both an appreciation of the importance of good management of IT, which to most managers seems like a very technical thing that somebody else ought to take care of, No. 1, and No. 2, that they need to do that with a focus on results so that we do not have fiascoes like we have had at several agencies.

Senator BOND. We will look forward to working with you on that.

I was going to ask you a question on highway funding. I think $284 billion is not adequate for our highway needs, but I can assure you that we are looking forward to giving you a highway bill that does not increase the deficit but maybe does a little better job in meeting our basic infrastructure needs.

I would ask my last question. We are drastically cutting many programs that are important to the quality of life of Americans to our economic future on the discretionary side. We are seeing mandatory spending going up $107 billion in 2006. I would ask you the rhetorical question, are you going to do something about limiting the explosive costs of mandatory spending, and when can we see some real results?

Mr. BOLTEN. Absolutely, Mr. Chairman, and the mandatory problem is one that dwarfs the challenges we face in our discretionary budget. It has three major components in entitlement spending: Social Security, Medicare, and Medicaid. On the last, the President has put forward proposals included in his budget and now, I know, being debated in the context of the budget resolution, to begin to get control of some of the explosive cost growth in the Medicaid program. We have put forward, I think, some very responsible proposals that just begin to ensure that we are spending our dollars there responsibly. There has been a great outcry about the supposed cuts the administration has proposed in Medicaid. What is actually going on is that instead of the current trajectory on auto pilot of Medicaid spending increasing out over the next 10 years at 7.4 percent growth, the administration is proposing that that growth be reduced to 7.2 percent. Obviously, there is a lot more that needs to be done.

Medicare, which is the biggest part of the problem, is an issue with a wide variety of elements that contribute to the problem. The biggest one is overall health care costs. I know the time is expired, so I will not go into any detail on initiatives to control health care costs. But that is crucial. At some point I believe we will also need to take another look at the Medicare system, which you have just legislated on, to ensure that we are getting the taxpayers value.

The third element is Social Security. The President, as you know, has an initiative——

Senator BOND. I know the President has made a recommendation. I look forward to supporting plans there, and I hope you will do something. When we thought we were getting a $400 billion Medicare increase, that was wrong by almost double. That is really disappointing.

That is my final question. I will turn to Senator Murray for such questions as she may wish to ask.

Senator MURRAY. I have a couple other areas, Mr. Chairman, so I appreciate that. One of them is regarding air passengers.

In the Homeland Security budget, the administration proposed to increase the security fee paid by passengers by 120 percent next year from $2.50 to $5.50 per segment. As you probably are well aware, the airlines are complaining bitterly, and I think correctly, that this is a $1.5 billion tax increase which further undermines their ability to recover economically.

In Secretary Mineta's formal testimony before us, he justified a half billion dollar cut in airport investments by arguing that several airports are not yet charging the full allowable passenger facility charge that they are allowed under law. Secretary Mineta's testimony implied that the proper way to invest in airports is through another $350 million in fees instead of from appropriations from the Airport and Airway Trust Fund.

So in addition to all these other problems, as you well know, the price of oil between $50 and $60 a barrel is not helping either.

I am curious whether the administration has any sympathy for the airlines, first of all, and the challenges that they are facing with this, and really why, if you understood that you were giving us a double whammy with two proposals, one to increase the airport facility fees by $350 million and also requiring $1.5 billion in higher fees at the same time.

Mr. BOLTEN. Senator, we recognize that the airline industry is challenged, as is the rail industry, as are our highways, as are virtually all modes of transportation especially by high oil prices. But we also know that we have a responsibility to be prudent with the taxpayers' dollar.

Now, the increase in the fees that you referenced, I think it is, from about $3 per segment up to about $5 a segment is what we are talking about, an authorized increase in the fee that goes on an airline ticket. What we are trying to do is bring us closer to making it possible for those fees to fully fund the cost of the airport screening that has now been implemented since 9/11.

The Federal Government has to pay those costs, or the taxpayer has to pay those costs. The question is who is going to bear it. We have two choices. We can try to impose that cost on those who are using the airline services or we can impose them on the general taxpayer. I believe that given that choice, the former answer is almost always the right answer, that you want those who are taking advantage of a service to bear the cost.

Senator MURRAY. Well, it is except if you will recall, when the airlines went down after September 11, the economic impact was devastating. We certainly felt it in my end of the world. So I think we have to be very careful what kind of economic impact we put on the airlines.

Mr. BOLTEN. That is understood.

Senator MURRAY. I wanted to bring up another topic with you that I am deeply concerned about. I have served on this Appropriations Committee for 13 years, and throughout that time I have had the pleasure of working on a bipartisan basis with several different chairmen, including Senator Shelby and Senator Bond. I believe that despite my policy differences with the administration, I have always been very careful to leave my door open to any member of the administration to talk about policies of importance to my State or to the country. I have worked closely with the Bush administration on trade and commerce issues and port security, and those are all important to me.

I say that because I have been really disappointed to learn over the past few weeks that the Executive Office of the President has been promoting a funding proposal that they want included in the pending supplemental that is before us right now. But as far as I can tell, this proposal has only been floated to majority members of the subcommittee and the majority staff. I wanted to ask you if you believe that the Executive Office of the President has the responsibility to come to Congress and justify its budget like every other agency in the Government.

Mr. BOLTEN. I believe we do, yes.

EXOP/OFFICE OF POLICY DEVELOPMENT

Senator MURRAY. Well, I do too and I believe that partisan differences should never enter into the considerations of this subcommittee when it comes to the financial needs of the Executive Office.

So I want to know if you can tell me why the administration is floating a proposal to eliminate the Office of Policy Development in the White House and merge it with the larger White House salaries and expenses account, and really more importantly, why has this proposal not been formally transmitted as a budget amendment through OMB.

Mr. BOLTEN. Senator, I cannot tell you why it has exactly been approached this way. I know we would be happy to engage with you on the proposal, and I am happy to discuss it with you. Probably this hearing is not——

Senator MURRAY. Can you just tell us why none of the minority staff on the Appropriations Committee has been talked to about this?

Mr. BOLTEN. I do not know who has been contacted and who has not been contacted.

Senator MURRAY. I can tell you that none of them have. We just know about it.

Mr. BOLTEN. Well, as I say, we would be happy to engage with you on the issue. It is something with which I have a little bit of familiarity and I know it would be an important and very useful piece of flexibility for the management of the White House in a situation where in the last 2005 budget the Office of Policy Development was drastically cut. I think that to enable the chief of staff in the White House to properly manage the White House resources—I think what they are suggesting is simply an ability to merge some of the accounts to make it easier to deal with that kind of situation.

Senator MURRAY. I think you may remember that during the Transportation/Treasury conference last year we adopted reprogramming guidelines for the Executive Office of the President which were most generous and most flexible. It is just disconcerting that this proposal is being floated on a plain white piece of paper to Republican members only. I just would suggest to you that you work with all of us on this committee and we would appreciate that consideration.

Mr. BOLTEN. We would be happy to engage with you, Senator, and I will make sure that does happen.

Senator MURRAY. I know my time is up and I know the chairman is ready to go.

BONNEVILLE POWER ADMINISTRATION (BPA)

I would just say I do have a question on Bonneville Power Administration. I think it is a topic you and I have gone through a number of times. We are very concerned about the President's proposals for power marketing administrations to go to market-based rates. Congress has spoken on that. I think you know that that is not going to fly on this end of the road.

But the other one is the proposal in the budget that would limit BPA's use of third party financing. I am not sure if you are closely familiar with it, but it is by accounting financing arrangements against BPA's borrowing authority limits. I wanted to ask you if you think BPA's investments and using third party financing are liabilities of the U.S. Treasury or they are liabilities of the Northwest ratepayers.

Mr. BOLTEN. Senator, if I may, I would like to respond on this issue in general to you for the record, with the chairman's permission.

[The information follows:]

BONNEVILLE POWER ADMINISTRATION (BPA)

BPA currently pays its obligations using power revenues from its ratepayers. Therefore, its liabilities accrue immediately to its ratepayers. Given that BPA is a wholly-Federal entity within the Department of Energy, the administration is committed to ensuring that BPA has the resources necessary to honor its liabilities.

The legislation the administration transmitted on June 1, 2005 to count BPA and TVA debt-like transactions against their debt caps is intended to accurately reflect these agencies' liabilities for the benefit of their ratepayers and other stakeholders, including taxpayers. Third party financing in which the non-Federal partner bears substantial risk would not be counted toward their debt caps, and this is the kind of partnering the administration has urged these agencies to explore. In addition, the Budget proposes to increase BPA's debt cap by $200 million, which exceeds the amount of third-party financing BPA informed us it would like to pursue over the next 5 years, so our proposal should not have any programmatic effect on BPA's operations.

ADDITIONAL COMMITTEE QUESTIONS

Senator BOND. Okay. I really appreciate that because it has extreme consequences, and we have entered into a number of agreements believing that it is Northwest ratepayers, and if there is a difference of opinion, we need to know that.

Senator MURRAY. Thank you, Mr. Chairman. I appreciate it.

Senator BOND. Thank you very much, Senator Murray.

[The following questions were not asked at the hearing, but were submitted to the Office for response subsequent to the hearing:]

QUESTIONS SUBMITTED BY SENATOR PATTY MURRAY

IMPACT OF HUD'S UNALLOCATED RESCISSION OF $2.5 BILLION

Question. Mr. Bolten, last week, our subcommittee held a hearing with HUD Secretary Alphonso Jackson. Your administration has singled out the Department of Housing and Urban Development for the largest cuts of any major Federal agency. I find this to be particularly tragic given the agency's mission to house the poor and seek to redevelop the Nation's most troubled communities.

Your budget for HUD seeks authority to rescind $2.5 billion in unobligated balances from any program within HUD. In response to my questions, Secretary Jackson could not commit to me that this rescission would not come at the expense of existing levels of funding to house the poor. He could not even guarantee that this funding cut would not come at the expense of programs serving the homeless. It was clear that this proposal to impose a $2.5 billion rescission against the agency was not something that was concocted at HUD.

Mr. Bolten, since this proposal appears to have been developed and supported at your agency, can you guarantee me that if we adopt your proposal to rescind $2.5 billion from any program at HUD, that these funds will not work a hardship on any of the low-income communities that are served by HUD? Can you provide me with a guarantee that this rescission will not end up coming at the expense of programs serving the disabled, or the homeless, or people living with HIV/AIDS?

Secretary Jackson told us that he would be trying to develop a list as to where this $2.5 billion would come from over the course of the next several weeks. Can you guarantee us that we are going to get this list prior to the time that this subcommittee marks up?

Answer. While the estimate of excess funds available for rescission may change, there is every reason to believe, based on past experience that a large recovery will occur. Each year, since 1998, large amounts have been available for rescission from the Section 8 account—an average of $2 billion in rescissions per year. These funds proposed for rescission in the fiscal year 2006 budget represent recoveries of amounts in the Section 8 programs or other HUD programs previously appropriated and obligated that are in excess of current needs.

The President's 2006 Budget does allow the Department to look to other sources of funds within the Department should there be insufficient funds within this account. However, this would not affect new funds in any program account. The funds proposed for rescission will not be needed to meet current obligations.

In 2003, for example, Congress enacted a rescission of $1.6 billion which was satisfied with $1.174 billion in unobligated balances in the Section 8 account and $426 million in unobligated balances from other accounts including the Flexible Subsidy account ($306 million) and small amounts from seven other accounts, with no programmatic effects.

As is the case each year, HUD may have a general idea ahead of time, but will not determine which funds from which accounts will be used to satisfy the rescission until June or July of 2006. While the estimate of excess funds available for rescission may change, based on past experience sufficient funds will be available within the Section 8 programs.

PART—PROGRAM ASSESSMENT RATING TOOL

Question. Mr. Bolten, I understand that your Program Assessment Rating Tool—or "PART" is the administration's tool to rate the effectiveness of Federal programs and help inform your budget decisions. As I review the President's Budget, it appears that several programs are slated for funding cuts despite receiving a positive PART rating. For example, the airport grant program and the Fair Housing Assistance Program are rated "moderately effective", yet their budgets are cut. The Education Department's college prep program—"GEAR-UP"—is rated as "adequate." Yet your budget is proposing that all funding for that program be eliminated.

It appears that, for all the effort and expense that the agencies and OMB are going through to execute the PART process, it is not informing your budget decisions. Why not?

Why would an agency have an incentive to improve a program and achieve a better PART score if OMB is just going to turn around and cut or eliminate the program anyway?

Answer. As the administration prepared its list of proposed major reforms and budget savings, we were guided by three major criteria:

- —Does the program meet the Nation's priorities? The budget increases funding to strengthen our Armed Forces, improve our homeland defenses, promote economic opportunity, and foster compassion.
- —Does the program meet the President's principles for appropriate use of taxpayer resources? If an appropriate Federal role could not be identified in a program's mission, the budget generally proposes to reduce or eliminate its funding.
- —Does the program produce the intended results? The Bush Administration is measuring the effectiveness of the government's programs—and the results are helping us make budgeting decisions.

Just as a low PART rating does not automatically result in a funding decrease, a high PART rating does not automatically result in a funding increase. A PART assessment is an important factor, but not the only factor, in funding decisions. For example, while the GEAR UP program was rated "adequate," it is among a number of narrow-purpose programs proposed for consolidation into the High School Intervention program. Activities supported by the GEAR UP program would be allowable under the new program if they can lead to improved student achievement.

The administration wants all Federal programs to work better. Because agencies are committed to improving their programs, they have defined specific steps that address PART findings for all programs, even highly rated ones or those proposed for termination.

NEW PRIVACY AND CIVIL LIBERTIES OVERSIGHT BOARD

Question. As the Nation goes to new and greater lengths to fight terrorism, there is a simultaneous and growing concern over the protection of the civil liberties of our citizens. The Intelligence Bill that the President signed into law in December sought to address this issue by creating a Board that would be responsible for ensuring that privacy and civil liberty concerns are appropriately considered in all Executive Branch policies and practices across the entire Federal Government. My subcommittee colleague, Senator Durbin, was instrumental in authorizing the provision in law that requires the establishment of the new Privacy and Civil Liberties Oversight Board. That Board is to be composed of five members and staff to support it. Yet, the Executive Office of the President is only requesting $750,000 to support two FTEs for the new Board.

How effective can this Board be with only two FTEs?

How did you decide, with a Federal workforce of 4.1 million military and civilian Federal employees, that the protection of civil liberties only requires two employees?

What are your long-term staffing plans for the Board?

The legislation that created this Board is the same legislation that created the National Director of Intelligence, and his nomination is currently pending in the Senate. Where are the nominees for this Board? When should we expect to see nominations submitted to the Senate?

Answer. The President is committed to protecting the legal rights of all Americans, including freedoms, civil liberties, and information privacy guaranteed by Federal law, in the effective performance of national security and homeland security functions. In his Executive Order of August 27, 2004, the President created a Presidential board of senior agency officials to advance this commitment and to advise him on new and ongoing efforts to safeguard these legal rights. The Privacy and Civil Liberties Board subsequently established by the Intelligence Reform and Terrorism Prevention Act of 2004 (Act) will build on this important effort.

The administration's proposal for funding the Privacy and Civil Liberties Board established by the Act envisions a Board whose members carry out their functions for the government on a part-time basis, with a full-time Executive Director. In addition, the Act authorizes the use of agency detailees on a non-reimbursable basis. A Board composed of part-time members was envisioned by the Act—which authorized the Chair of the Board to serve on either a full-or part-time basis, but specified that remaining Board members would serve part-time. Thus, with part-time members, the equivalent number of FTEs for the board is two.

This arrangement will help ensure that the Board is staffed with people with the right type of expertise because it permits members to be appointed who will not have to leave their jobs in order to carry out this important function. In addition, if the administration draws on the staff of various agencies, the Board's activities would be augmented without adding to the cost of its function, promoting efficiencies within a tight budget climate. Agency staff would carry out the day-to-day activities and research for the Board, while leaving the results of that research, and advising and counseling on development and implementation of policy, to Board members.

Finally, the funding level in the administration's proposal is very similar to that provided historically for the President's Foreign Intelligence Advisory Board, which operates with a modest budget and whose members serve without compensation.

The administration believes that this arrangement will be most beneficial to the Federal Government—drawing on the right type of expertise, and promoting efficient use of existing government resources. Once the Board is up and running, its progress and performance will be examined to determine whether this model continues to be appropriate.

On June 10, 2005, the President announced his intent to nominate Carol E. Dinkins to be the Chairman of the Board, and Alan Charles Raul to be the Vice Chairman. Additionally, the President appointed Lanny J. Davis, Theodore B. Olson and Francis X. Taylor as members of the Board.

A RECORD NUMBER OF FEES?

Question. Your budget this year includes a very large number of new user fees. It can be argued that, with the exception of National Defense, there are designated "users" for just about every government service. For example, the government could require that the cost of wheat subsidies only be paid by people that buy bread and cereal. The government could require that only small businesses pay the costs of the Small Business Administration.

How does this administration decide which services should be paid for through general revenues versus user fees? Does the administration concede that there is any limit to the number of new user fees you should propose?

Many have criticized the administration's user fee proposals as just more taxes. Would you agree that there should be some relationship between the fees that are charged and actual cost of providing the government service?

I am concerned about one area new user fees; namely, the fees you want to impose on small wineries in Washington State. In one small agency alone in this bill—the Alcohol, Tobacco Tax and Trade Bureau—five new or increased fees are being proposed equaling 31 percent of the TTB fiscal year 2006 budget request. I am told that there is no relationship between the actual services the wineries receive from TTB and the fees you now want to impose.

How did you decide that an industry that already pays nearly $550 million in Federal excise taxes needs to pay new fees?

Why is there no correlation between the fees you want to propose and the services these wineries receive?

Answer. In general, the administration uses Circular A–25 on User Charges, to develop its user fee proposals. Circular A–25 provides as a general policy that user charges should be designed to recover the full cost of Federal activities that provide special benefits beyond those received by the general public. Under current law, the Federal Government already recovers the full cost for the activities of agencies such as the Federal Energy Regulatory Commission, the Securities Exchange Commission, and the Patent and Trademark Office.

In the case of the Alcohol and Tobacco Tax and Trade Bureau (TTB), the proposed user fees reflect the agency's best current estimates of the charges necessary to transfer full costs to the direct beneficiaries of the agency's services and to limit use of those services when not required. The services provided by TTB ultimately protect the public against misleading labels, adulterated alcohol, protect against dishonest persons entering the alcohol business, and promote fair competition among industry members. TTB's regulatory efforts provide value to the industry and the industry should pay for the benefits it receives from these efforts.

For small wineries, at least four of the following five user fees would apply depending on the activity:

—*New Permit Applications*.—$500 minimum fee. Applies to all wineries, as well as other businesses. TTB must review and investigate the qualifications of the applicant, including the applicant's criminal background and whether he or she is likely to operate in conformity with Federal law.

—*Certificates of Label Approval/Certificates of Exemption*.—$100 minimum fee for paper filing, $50 minimum fee for electronic filing. Applies to all alcohol beverage products. A key feature of the user fee proposal is to encourage businesses to file their applications electronically.

—*Formula Review with No Laboratory Analysis*.—$200 minimum fee. Wineries must submit formulas only if product evaluation is required by regulation (e.g., for flavored wine). Formula review is necessary to ensure the proper labeling classification of products.

—*Formula Review with Laboratory Analysis*.—$600 minimum fee. If a winery wants a label approved without the sulfite declaration, a lab analysis and report is required, which would be covered by the proposed user fee. However, the lab analysis need not be conducted by the TTB lab.

—*American Viticultural Area Petitions*.—$3,000 minimum fee. This fee applies only on petitions that wineries choose to submit for recognition of new viticultural areas, and covers the cost of reviewing the petition and submitting it for formal rulemaking.

COMPETITIVE SOURCING—DISABLED AND HEALTH CARE

Question. In 2001, President Bush announced his New Freedom Initiative, which involves "tearing down the remaining barriers to equality" that face Americans with disabilities. At the time, he noted that the unemployment rate for Americans with disabilities is about 70 percent. The President says he cares about the disabled, but the disabled can lose their Federal jobs if those jobs are subjected to competitive sourcing.

In February of this year, OMB reportedly prepared draft guidance for the 2005 competitive sourcing inventories. This draft guidance was never released. It advised agencies that, as part of the competitive sourcing process, they could "set aside FTEs for the employment of physically- and/or mentally-challenged individuals."

Why wasn't this memo finalized and sent out to all Federal agencies? Is it possible that certain disabled individuals have already lost their Federal job as a result of OMB's failure to disseminate this guidance?

The administration has stated numerous times that they are concerned about the number of Americans that are without health insurance. Yet, your competitive sourcing rules penalize Federal employees that want to compete to keep their jobs because they have a responsible employer that provides health insurance. The cost of their Federal health insurance often works to their disadvantage when they compete against private vendors that do not offer it.

Is this policy consistent with the administration's stated concern for the uninsured? Why aren't you requiring all contractors to provide insurance commensurate with the Federal benefits? Why aren't you at least requiring all contractors to provide some minimal level of health insurance?

Currently, the DOD Appropriations Bill requires you to ignore the added costs of Federal health insurance when conducting a competition between private vendors and Federal employees that are trying to keep their jobs at DOD.

Do you believe it makes sense to have this policy only for competitions within the Defense Department but not the other Federal agencies? Why?

Answer. On May 23, 2005, OMB issued government-wide guidance to help agencies prepare their inventories of commercial inventories (see OMB Memorandum M–05–12, available on www.omb.gov). The guidance includes an example of the rationale an agency could use to justify exempting positions held by individuals with disabilities from competition. The example explains that an agency may set aside positions for the larger governmental purpose of providing gainful employment for those individuals who, as a result of their disability, have limited employment options in the private sector. The guidance, which addresses a wide range of issues to improve the accuracy and overall quality of inventories, was subject to a lengthy agency review and comment process. The sample rationale described in the final guidance reflects a best practice that is already being used by agencies to exempt individuals with disabilities from competition—i.e., the guidance neither creates a new requirement nor allows for an exclusion that had formerly been prohibited.

We do not believe that Federal employees are disadvantaged in public-private competitions. Just as we would not penalize a private entity specifically if they offered better health benefits to their employees than the Federal entity, neither do we penalize Federal agencies that offer health benefits that a private competitor does not offer. In fact, Federal employees are generally given a 10 percent price advantage over their private sector counterparts. For work to be converted from public to private sector performance, a contractor must propose to perform at a cost which is at least 10 percent lower than that proposed by the in-house offeror. Federal employees have performed well in public-private competitions. They have been selected as the best value provider to perform work representing approximately 90 percent of the positions competed in fiscal years 2003 and 2004 and, thanks to competition, they have developed more efficient and cost-effective methods to serve our taxpayers.

The administration believes that Section 8014 of the fiscal year 2005 Defense Appropriations Act unnecessarily subjects private sector bidders to intrusive data requirements concerning the provision of health benefits to their employees. While well intentioned, this provision ultimately undermines the efficiencies in private health plans and provides another disincentive for the private sector to participate in DOD's competitions. Further, by discouraging private sector interest in competitive sourcing, this provision places at risk significant savings—estimated to be $6 billion from fiscal year 2001 to 2006—generated by the Competitive Sourcing initiative of the President's Management Agenda. Small business participation in competitions will be severely undermined since this provision makes it particularly burdensome to assemble competitive offers.

COMPETITIVE SOURCING

Question. Director Bolten, in your answers to post-confirmation hearing questions, you told the Congress, "If confirmed, I will ask the Administrator for Federal Procurement to recommend ways to improve opportunities for federal employees to compete for new work and for work currently performed by contractors." Please provide the committee with a list of those recommendations and please identify specific instances in specific agencies in which Federal employees have been allowed to compete for new work and contractor work.

Please provide a list of specific instances in which OMB has given credit to agencies towards the achievement of the goals included in their "competitive sourcing" plans for using alternatives to public-private competition for the generation of efficiencies in the delivery of services.

The Administrator of the Office of Federal Procurement Policy, in his responses to pre-confirmation hearing questions last year, said that he, "would encourage in-house service providers to develop most efficient organizations as a matter of routine, including for streamlined competitions." Why has OMB strenuously opposed any legislation that would ensure that in-house service providers are always allowed to develop most efficient organizations as part of any public-private competitions?

Further, the Administrator of the Office of Federal Procurement Policy, in his responses to pre-confirmation hearing questions said that he, "would not object to removing the five-year recompetition provision from the Circular and relying on agencies to determine appropriate performance periods based on the nature and risk associated with the services to be provided." Has this change been made? If not, why?

According to a May 30, 2003, posting on GovExec.com, "In a late April interview with Government Executive, Angela Styles, the director of the Office of Federal Procurement Policy, said curbing direct conversions was part of OMB's effort to prove that competitive sourcing is about competition, and not shifting contracts to private firms. 'People have criticized us for this being an outsourcing initiative and I've been trying to tell them that it's really not, that what we want is competition and the best value for the taxpayer at the lowest cost. I think this adds a little more meat to what we're saying,' Styles said. On Wednesday, an OMB official said the idea of banning direct conversions was 'presented to OMB by federal employee organizations and their members, and we listened to them. Direct conversions for under 10 [full-time equivalent] employees are now a thing of the past. We believe that fiscal responsibility demands that decisions be made by facts, and the new streamlined approach requires knowledge of the costs and agency accountability.'" However, the Administrator of the Office of Federal Procurement Policy, in an article posted on GovExec.com on January 14, 2005, said he was considering allowing agencies to shift work to contractors without competition, a practice known as direct conversion. Please indicate why OMB's thinking may have changed, providing any relevant research, and provide an update as to OMB's intentions with regard to its support for reviving the practice of direct conversion.

Answer. The OFPP Administrator has reviewed the A–76 Circular's provisions for Federal employee performance of new work and contracted work and concluded that these provisions are fair and reasonable. The circular permits agencies to consider in-sourcing or performing new work by demonstrating through competition that this action will achieve the best value for the taxpayer.

Agencies that have developed highly efficient internal operations and have the capacity to handle common support functions for multiple agencies will soon have the opportunity to compete for this work from other agencies, beginning with financial management and human resources, as part of OMB's efforts to reduce duplication in lines of business through cost-effective migration and consolidation. If a private sector source wins a competition, the government providers will have another opportunity to compete when the work comes up for recompetition.

Regarding alternatives for public-private competition, agencies are always encouraged to find efficiencies and better ways to perform their mission. However, credit in the competitive sourcing scorecard is directly tied to those management efforts involving the use of competition since the initiative focuses on how well agencies use competition as a management tool to reduce costs, increase efficiencies, and eliminate waste.

OMB recognizes that public-private competition is just one of a number of management tools, and not all commercial activities are suitable for competition (e.g., perhaps because there is no private sector interest in the work or the activity is core to the mission and potential conversions to the private sector would subject the mission to undue risk). OFPP will continue to work with agencies' Competitive Sourcing Officials (CSOs) on guidance to determine how agencies might develop "high performing organizations" where competition isn't appropriate.

OMB has opposed calling for the development of most efficient organizations (MEOs) because they have typically has been coupled with objectionable provisions, such as requirements that agencies choose the cheapest provider rather than the one that offers the best value to the taxpayer. In addition, statutory language is unnecessary because Circular A–76 already provides a strong foundation for the development of MEOs: the Circular requires MEOs for all standard competitions and encourages MEOs for all streamlined competitions. Fiscal year 2004 data from the agencies shows a trend towards greater use of standard competitions and streamlined competitions with MEOs.

With regard to the 5-year recompetition provision in Circular A–76, a change has been made. In April 2004, OMB issued a memorandum to advise agency heads that the 5-year performance limitation no longer applies. The memorandum vests agencies with the discretion to determine an appropriate performance period considering the nature and risk of the service.

Generally, we will expect agencies to continue using public-private competitions that take cost into careful consideration when deciding whether work should be converted from public to private sector performance. At the same time, there may be cases where direct conversions of small numbers of positions may make sense (e.g., clearly commercial, non-core work) where such conversions may help the agency expeditiously redirect its workforce to mission critical activities that are not suitable for private sector performance.

SUBCOMMITTEE RECESS

Senator BOND. Thank you, Director Bolten. It has certainly been an interesting exercise. We appreciate your coming before us. We have many things that we look forward to working with you on.

This hearing is recessed.

[Whereupon, at 11:15 a.m., Thursday, April 21, the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

TUESDAY, APRIL 26, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:34 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Murray, Byrd, and Dorgan.

DEPARTMENT OF THE TREASURY

OFFICE OF THE SECRETARY

STATEMENT OF JOHN W. SNOW, SECRETARY

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning. The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD, and Related Agencies will come to order. Thus far, this new subcommittee has met to discuss the fiscal year 2006 budgets of the Departments of Transportation and Housing and Urban Development, as well as the IRS.

This morning we meet to discuss budgetary and policy matters related to the third and final Department under the subcommittee's jurisdiction, the Department of the Treasury. I'm pleased to welcome Secretary John Snow before this subcommittee and look forward to hearing your perspective on the accomplishments and challenges facing one of the Nation's oldest Cabinet Departments.

The President has set out an ambitious economic agenda for his second term, including reforming the Social Security system, overhauling the tax code, and halving the deficit. The Treasury needs to take charge of all these issues. In particular, Secretary Snow, you have a very important and high profile leadership role in promoting and explaining the administration's Social Security reform plan to the Nation.

I think we all agree that reform of Social Security is critical to the future economic well-being of our Nation. Nevertheless, while I understand your involvement with the 60 stops in 60 days tour, I'm concerned that taking a criss-crossing tour of the country while most senior level positions in the Treasury are vacant has left a void of leadership at the Department.

This may not only undermine effective management of the Department, it also diminishes the role of the Treasury in formulating policy and stewardship of economic and financial systems. Furthermore, Treasury is often left without a notable representative during interagency meetings, thereby risking losing its core responsibilities and authorities to other agencies.

The list of vacant positions reads like a social register of Federal economic policy. It includes a Deputy Secretary, two Under Secretaries, six Assistant Secretaries, and a number of other key positions. More than one-third of Treasury's main jobs are either vacant or filled by acting appointees. I am especially discouraged that in most cases, to our knowledge, no potential nominee is even in the pipeline. Someday there could be a financial crisis that requires Treasury's immediate expertise, and right now I'm not sure who would answer the call.

You've got a lot of fish to fry, Mr. Secretary, and I know you can fry those fish well. But when you're cooking that many fish, you've got to have some help. And I hope that we can do more than just cross our fingers that you won't be called on to be in three places at once without the Deputy and the Under Secretaries and Assistant Secretaries.

At its peak, the Treasury was the second largest law enforcement Department of the Federal Government. But since the Homeland Security Act, most of Treasury's law enforcement bureaus and capabilities have been transferred. Now, as Treasury reestablishes its enforcement capabilities and reasserts its proper role as the leader of government's efforts to fight terrorist financing, I'm troubled by the implementation of the statute establishing the Office of Terrorism and Financial Intelligence, or TFI, and the realignment of resources from Office of Foreign Assets Control to TFI, and more specifically, to the Office of Intelligence and Analysis, OIA, within TFI.

The principal reason Congress established TFI is to assure aggressive policy formulation, planning, and coordination over the Treasury's efforts to thwart terrorist financing, and enforcement of money laundering and other financial crimes. It appears that the office is becoming instead an operational unit at Treasury that replicates the capabilities of the Financial Crimes Enforcement Network Bureau, or FinCEN, and OFAC.

The decision to transfer 23 analysts from OFAC's foreign terrorist division to OIA, which will assume responsibility for that function, is evidence of the desire to form TFI into an operational unit. I think that's a questionable move. It's wasteful to reproduce capabilities that already exist, and it perhaps weakens the enforcement of the Nation's economic sanctions program and the Bank Secrecy Act, the very foundation of Treasury's efforts to counter terrorism financing.

More important, the Congress established the Office of Intelligence and Analysis at Treasury to empower the Department to be the leader of the Federal Government's effort in combating terrorist financing. At a time when Treasury needs to take bold actions, Treasury instead has not yet submitted a nominee to lead the office and has staffed the office with detailees, has failed to build a unique, organic intelligence capability, and has been mired in internal resource realignments. I don't believe that's acceptable.

Another major area of concern for me is information security. It was really disturbing to read a recent report issued by the GAO that found that the lack of major security controls jeopardized the taxpayer and law enforcement data collected and processed by two Treasury bureaus: IRS and FinCEN. GAO's April 15 report, titled "Information Security: Internal Revenue Service Needs to Remedy Serious Weaknesses Over Taxpayer and Bank Secrecy Act Data," found that sensitive taxpayer and law enforcement data is at risk of unauthorized use, possibly without detection.

While IRS has made some progress in correcting 32 of 53 previously reported information security weaknesses, GAO identified 30 new weaknesses. To me, it sounds like while locks were being installed on the front door, the windows and the back door were left open. And with some 7,400 possible users with access to the data, I believe the risk is extremely high and is potentially disastrous.

With the recent media stories on identify theft and breaches of personal information by private data collection agencies, the Department must make information security a priority immediately. I urge you, Mr. Secretary, to personally oversee this area because of the extreme consequences of the problem. Our ability to collect taxes and fight terrorism and crime are jeopardized by the lack of security controls.

What bothers me most is that IRS and FinCEN data may already have been compromised, and are being used or plan to be used for criminal use, and we may not even know the information has been misappropriated. I hope it's not too late and you can provide me and the committee your personal commitment that you will resolve this issue quickly.

Last year, this committee added $5 million for FinCEN to develop the first phase of its BSA Direct project, an IT system that will enable FinCEN to become the repository for Bank Secrecy Act data. Considering the risk of unauthorized disclosure, modification, or destruction of the data stored at the Detroit Computing Center, as noted by GAO and years of audit work by TIGTA, I hope you'll give us your commitment to this project and we'll charge FinCEN rather than the IRS with collecting and storing Bank Secrecy Act data. This would streamline administration of the Bank Secrecy Act at FinCEN, thereby making one bureau at Treasury clearly responsible and accountable to you for enforcement of the Act.

Mr. Secretary, let me also raise concerns with the 2006 budget request. The administration is proposing to eliminate the Community Development Financial Institutions program, CDFI, and the Bank Enterprise Act, which were funded at $31.4 million and $11.4 million respectively in 2005. These programs, in my view, in my experience in other committees, have been very important in expanding the availability of financial services in rural and urban areas that are underserved by financial institutions.

Instead, the administration is proposing that both programs be eligible for funding through the Strengthening America's Communities initiative, an administration-proposed block grant program that is designed to be administered by the Commerce Department. Both programs work very well, but more importantly, it's hard to envision any State or community awarding scarce block grant funds to financial institutions, no matter how well they serve financially underserved areas.

As I've stated in other hearings, I just do not believe that that transfer of these important programs to the new block grant makes any sense.

Another bad idea is the budget request to establish new user fees of $28 million at the Alcohol and Tobacco Tax and Trade Bureau. I appreciate that, unlike other areas of the budget request, these proposed user fees do not dig funding holes for the subcommittee, and that the budget includes funding to cover any shortfall in the revenue from these fees. I am imposed—I am opposed nevertheless to the proposed fees, because they disproportionately impact small businesses, especially those involved in the legal distribution of alcohol and tobacco products.

Congress just suspended collection of the special occupational tax for alcohol and tobacco because of its burden on small businesses. And I believe it would be ill-advised and ill-timed to levy another tax through this user fee proposal on the same small businesses. I understand that these user fees have been proposed previously, but have been killed within the administration. I think that was a good idea, and I would not be at all surprised if these user fees meet the same fate in Congress this year.

Finally, I have concerns about the IRS Business Systems Modernization (BSM) program, which I discussed previously with the IRS Commissioner. Replacement of antiquated computer systems to perform basic tax administration is critical for improving the level of service that taxpayers justifiably expect, and for closing the tax gap.

Sadly, virtually every procurement activity in BSM is behind schedule, over budget, and when the contractor provides software and hardware to the IRS, it does not meet the performance requirements. After spending nearly $2 billion, the IRS will be able to process the most basic 1040–EZ returns during this tax filing season. There are few calculations on the 1040–EZ form, and the IRS and the contractor are a long way from being able to process complex returns and schedules filed by most Americans.

I am curious to hear your views, Mr. Secretary, as someone who's had a career in the private sector, on whether the IRS and American taxpayers have received our money's worth on BSM.

In closing, as I've highlighted, there are some serious issues that need your immediate and full attention. I have the greatest faith in you personally, Mr. Secretary, with your intelligence, capability, and aggressiveness. I look forward to working with you. However, neither you nor I nor the Congress can do all this by ourselves, because of the scope and complexity of the problems.

I strongly urge you to get your senior positions filled in the Department. Otherwise, it's going to be very difficult for you to ensure accountability and oversight of the Department. Until you do so, it will be difficult at best to assure me, this committee, and the public that the Treasury is performing its responsibilities and protecting its citizens.

PREPARED STATEMENT

I thank you for your appearance and look forward to working with you on these very challenging issues. And I now turn to my ranking member, Senator Murray, for her opening statement.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

Good morning, the Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD, and Related Agencies will come to order. Thus far this new subcommittee has met to discuss the fiscal year 2006 budgets of the Department of Transportation and the Department of Housing and Urban Development. This morning we meet to discuss budgetary and policy matters related to the third and final department under the subcommittee's jurisdiction, the Department of the Treasury. I am pleased to welcome Secretary John Snow before the subcommittee and look forward to hearing your perspective on the accomplishments and the challenges facing one of the Nation's oldest cabinet departments.

The President has set out an ambitious economic agenda for his second term, including reforming the Social Security system, overhauling the tax code, and halving the deficit. The Treasury needs to take charge of all these issues. In particular, Secretary Snow, you have a very important and high-profile leadership role in promoting and explaining the administration's Social Security reform plan to the Nation. And I think we all agree that the reform of Social Security is critical to the future economic well-being of our Nation.

Nevertheless, while I do not object to your involvement with the "60 Stops in 60 Days Tour," I am concerned that taking a crisscrossing tour of the country while most senior-level positions at the Treasury are vacant has left a void of leadership at the Department. This not only undermines effective management of the Department, it also diminishes the role of the Treasury in formulating policy and stewardship of economic and financial systems. Furthermore, Treasury is often left without a notable representative during interagency meetings, thereby risking losing its core responsibilities and authorities to other agencies. The list of vacant positions reads like a social register of Federal economic policy and includes the Deputy Secretary, two undersecretaries, six assistant secretaries, and a number of other key positions. More than one-third of Treasury's main jobs are either vacant or filled by acting appointees. I am especially discouraged that, in most cases, no potential nominee is even in the pipeline. Some day there could be a financial crisis that requires Treasury's immediate expertise, and right now, I'm not sure who would answer the call—we should do more than just cross our fingers.

At its peak, the Treasury was the second-largest law enforcement department of the Federal Government. Since the Homeland Security Act of 2002, most of Treasury's law enforcement bureaus and capabilities were transferred. Now, as Treasury reestablishes its enforcement capabilities and reasserts its proper role as the leader of government's efforts to fight terrorist financing, I am troubled by the implementation of the statute establishing the Office of Terrorism and Financial Intelligence (TFI) and by the realignment of resources from Office of Foreign Assets Control to TFI and, more specifically, to the Office of Intelligence and Analysis (OIA) within TFI.

The principle reason that Congress established TFI is to ensure aggressive policy formulation, planning, and coordination over the Treasury's efforts to thwart terrorist financing and enforcement of anti-money laundering and other financial crimes. It appears that the office is becoming instead an operational unit at Treasury that replicates the capabilities of the Financial Crimes Enforcement Network Bureau or "FinCEN" and OFAC. The decision to transfer 23 analysts from OFAC's foreign terrorist division to OIA, which will assume responsibility for that function, is evidence of the desire to form TFI into an operational unit. This is a highly questionable move. It is wasteful to reproduce capabilities that already exist, and it weakens the enforcement of the Nation's economic sanctions programs and the Bank Secrecy Act—the very foundation of Treasury's efforts to counter terrorists' financing. More importantly, the Congress established the Office of Intelligence and Analysis at Treasury to empower the Department to be the leader of the Federal Government's efforts in combating terrorist financing. At a time when Treasury needs to take bold actions, Treasury instead has not yet submitted a nominee to lead the office, has staffed the office with detailees, has failed to build a unique organic intelligence capability, and has been mired in internal resource realignments. Mr. Secretary, this is simply unacceptable.

Another major area of concern for me is information security. I was extremely disturbed to read a recent report issued by the Government Accountability Office that found that the lack of major security controls jeopardized taxpayer and law enforcement data collected and processed by two Treasury bureaus—the IRS and FinCEN. GAO's April 15, 2005 report titled "Information Security: Internal Revenue Service Needs to Remedy Serious Weaknesses over Taxpayer and Bank Secrecy Act Data" found that sensitive taxpayer and law enforcement data is at risk of unauthorized use—possibly without detection. While IRS has made some progress in correcting 32 of 53 previously reported information security weaknesses, GAO identified 39 new weaknesses. To me, it sounds like while locks were being installed on the front door, your windows and back door were open. And with some 7,400 possible users with access to these data, I believe the risk is extremely high and potentially disastrous.

With the recent media stories on identity theft and breaches of personal information by private data collection agencies, the Department must make information security a priority immediately. I strongly urge you, Mr. Secretary, to oversee personally this area because of the extreme consequences of this problem. Our ability to collect taxes and fight terrorism and crime are jeopardized by the lack of security controls. What bothers me the most is that IRS and FinCEN data may already have been compromised and are being used or planned to be used for criminal use, and you may not even know the information has been misappropriated. I hope it is not too late and you can provide me and this committee your personal commitment that you will quickly resolve this serious issue.

Last year, this committee added $5 million for FinCEN to develop the first phase of its "BSA Direct" project, an IT system that will enable FinCEN to become the repository for Bank Secrecy Act data. Considering the risk of unauthorized disclosure, modification, or destruction of the data stored at the Detroit Computing Center as noted by the GAO and years of audit work by TIGTA, I hope you will give us your commitment to this project and will charge FinCEN, rather than the IRS, with collecting and storing Bank Secrecy Act data. This would streamline administration of the Bank Secrecy Act at FinCEN, thereby making one bureau at Treasury clearly responsible and accountable to you for enforcement of that Act.

Mr. Secretary, let me also raise several concerns with the fiscal year 2006 budget request. The administration is proposing to eliminate the Community Development Financial Institutions program and the Bank Enterprise Act program which were funded at $31.4 million and $11.4 million in fiscal year 2005, respectively. These programs have been very important in expanding the availability of financial services in rural and urban areas that are underserved by financial institutions. Instead, the administration is proposing that both programs be eligible for funding through the Strengthening America's Communities initiative, an administration proposed block grant program that is designed to be administered by the Department of Commerce. Both programs work very well, but, more importantly, it is hard to envision any State or community awarding scarce block grant funds to financial institutions, no matter how well they serve financially underserved areas.

Another bad idea in the budget request is the proposal to establish new user fees at the Alcohol and Tobacco Tax and Trade Bureau. I appreciate that, unlike other areas of the budget request, these proposed user fees do not dig funding holes for the subcommittee and that the budget includes funding to cover any shortfall in revenue from these fees. I am opposed, nevertheless, to the proposed user fees because they disproportionately impact small businesses, especially those involved in the legal distribution of alcohol and tobacco products. Congress just suspended collection of the Special Occupational Tax for alcohol and tobacco because of its burden on small businesses, and I believe it would be ill-advised and ill-timed to levy another tax through this user fee proposal on the same small businesses.

I understand that these user fees been proposed previously, but have been killed within the administration. I would not be at all surprised if these user fees met the same fate in Congress this year.

Finally, I raise concerns with the IRS's Business Systems Modernization program, which I discussed in great detail with the IRS Commissioner earlier this year. Replacement of the antiquated computer systems to perform basic tax administration is critical for improving the level of service that taxpayers justifiably expect and for closing the tax gap. Sadly, virtually every procurement activity in BSM is behind schedule, over budget, and when the contractor provides software and hardware to the IRS, it does not meet the performance requirements. After spending nearly $2 billion, the IRS will be able to process the most basic 1040 EZ returns during this tax filing season. There are few calculations on the 1040 EZ form and the IRS and the contractor are is long way from being able to process the complex returns and schedules filed my most Americans.

Mr. Secretary, I am curious to hear your views, as Secretary and as someone who had a career in the private sector, on whether the IRS and American taxpayer has gotten its money's worth on BSM.

In closing, as I have highlighted, there are some serious issues that need your immediate and full attention. I have faith in you personally, Mr. Secretary. You are smart, capable and aggressive. I also look forward to working with you. However, neither you nor I nor the Congress can do all this by ourselves. Because of the scope and complexity of these problems, I strongly urge you to get your Department's senior positions filled. Otherwise, it will be difficult, if not impossible, for you to ensure accountability and oversight of the Department. Until you do so, it will be difficult at best to assure me, this committee, and the public that the Treasury is performing its responsibilities in protecting its citizens.

Thank you. I look forward to working with you on these very challenging issues and I now turn to my ranking member, Senator Murray, for her opening statement.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Thank you very much, Mr. Chairman. Secretary Snow, welcome back to the subcommittee.

Secretary SNOW. Thank you.

Senator MURRAY. Since your last appearance, we've expanded our jurisdiction just a bit on this subcommittee. But I want you to know that your Department does remain a priority and an area of deep concern.

I know you have been traveling around the country trying to drum up support for the President's effort to privatize Social Security, and, to me, breaking the promise of Social Security and putting millions of Americans at risk is wrong. I know that you and I are not going to reach agreement on that today. But I think we can both agree that this national conversation has shown many Americans just how important Social Security is.

Today, more Americans understand how important Social Security's guaranteed benefit is. More Americans know that Social Security helps not just the retired, but provides critical income for the disabled, for widows, and surviving children. And I think more Americans appreciate the stability and certainty of their Social Security checks as we've seen the stock market rise and fall like a roller coaster lately.

While I know we will have a chance to talk about Social Security and issues like the health of our economy and the strength of the dollar, I want to make sure that this subcommittee attends to its central responsibility, reviewing the President's budget for your Department and reviewing how your Department has spent the money Congress has appropriated.

So today I want to discuss what's in this budget, including the new initiatives the Secretary wants to launch, and I also want to talk about what's not in this budget, the things the Secretary wants to terminate and the user fees the administration wants to impose on American families and small businesses. I especially want to discuss the Department's continuing problems in managing major procurements.

While it comes to addressing the agency's physical and IT infrastructure, it's clear that Treasury needs to do a better job in how it spends the dollars it collects from taxpayers.

Let me start with what is in this budget request. The administration is requesting a boost of more than $446 million for tax law enforcement activities. However, this boost will not signal a new historic high in IRS enforcement activities, far from it. As the IRS Commissioner told this subcommittee recently, the agency's enforcement efforts have been allowed to wane in the last few years. I'm encouraged that the agency now wants to reverse that trend, and since the IRS fails to collect between $250 billion and $330 billion each year from tax cheats, I would say that this reversal could not happen soon enough.

While the agency is finally addressing something it's allowed to languish for years, the way it's addressing it does trouble me. The administration wants to pay for more enforcement by cutting direct service to taxpayers. The President's budget would cut services that are essential in helping citizens comply with our tax laws.

For example, your budget proposal would: close as many as one out of every four taxpayer assistance centers across the country; eliminate phone tax filing, which is used by more than 5 million individuals and businesses each year; shorten the number of phone hours that IRS personnel are available to answer taxpayers' questions; discontinue tax law assistance through the Internet; and cut outreach efforts to high-risk taxpayer groups.

I don't believe these cuts are merited if they will only heighten confusion and hassle for taxpayers, and perhaps even make the compliance problem worse.

Unfortunately, funding for these basic taxpayer service functions is not the only thing missing from this budget. I am very concerned about the Secretary's proposals to eliminate funding for many essential functions in the Alcohol and Tobacco Tax and Trade Bureau. Instead of continuing to provide appropriated funding, the Secretary would impose new taxes on industry to pay for these functions.

Let me give you one example of great importance to families in my home State. Over the past few years, the people in Washington State have built a world-renowned wine industry through hard work, research, and creativity. These vineyards are providing jobs for communities that have struggled. They're bringing tourists to many parts of my state and they're helping our economy.

Over the past decade, wine has become a $2.4 billion industry in my State. Production has doubled, and now wine grapes are the State's fourth-largest fruit crop. Today there are more than 300 wineries in my State, nearly double the number in 2000, and Washington's wine industry supports more than 11,000 related jobs. Mr. Chairman, I'd love to have you come and visit sometime.

Senator BOND. If you want to visit the Missouri wineries, we'll make a——

Senator MURRAY. Deal.

Road trip. Many of our wine producers are small, family-run vineyards, and they should be encouraged and supported for the progress they've built with their own hands. Instead, this administration wants to hit them with more taxes in the form of new user fees.

Mr. Secretary, I can tell you that your proposal to fund the Alcohol and Tobacco Tax and Trade Bureau with user fees is going to impose a tremendous hardship on our small family-owned vineyards. Forcing vineyards to pay a fee just to get their labels approved will hurt new entrants into this promising market. We should be encouraging their success instead of putting more barriers to their viability. This proposal is especially puzzling coming from an administration that claims to encourage entrepreneurship and reduced tax burdens.

Finally, Mr. Secretary, I want to raise my concerns regarding the Treasury Department's deeply troubled record in handling major procurements, especially IT services. We receive a continuing stream of reports from the GAO and the Inspector General regarding projects that are way behind schedule, cost more than they should, or are not adequately secure.

The Treasury Department has finally established its new human resource information system known as HR Connect. That system cost taxpayers $173 million. A similar system at the Coast Guard cost one-seventh of that amount. A similar system at the Agricultural Department cost less than one-tenth that amount.

The Department's renovation activities are also a concern. The initiative to repair and restore the Treasury building and its Annex have been badly mismanaged. The cost so far will soon top a quarter of a billion dollars, but for all that money, work on the Treasury building is still not complete, and the Treasury Annex has not yet been touched.

Other examples of Treasury's poor management of major projects abound. Just last week, we read in the paper about an employee tuition assistance program at the IRS. More than 60 percent of the funding has gone to overhead, and less than 40 percent went to actual tuition assistance. Treasury's efforts to procure a new secure communications system was recently slowed down because the agency failed to grant all the bidders access to relevant information. As a result, the GAO sustained a bid protest.

And speaking of the GAO, that agency informed us that despite the progress the IRS has made in correcting information security weaknesses, more than half of the deficiencies identified 3 years ago are not fixed. Let me say that again. It's been 3 years and half the improvements still have not been made.

And these are not minor issues. Some of the vulnerabilities that still exist include the opportunity for any employee at the IRS and elsewhere in the Treasury to have easy, unauthorized access to sensitive information, including filings under the Bank Secrecy Act. In terms of the largest amount of taxpayer dollars lost, we could hold several days of hearings on the Business Systems Modernization program at the IRS. It might take that long to compare what has been delivered under that program compared to what was originally promised.

Mr. Secretary, I recognize that you personally cannot stay on top of each and every one of these programs. But when I look at these persistent management problems at your agency, when I look at the tax dollars being wasted, when I look at the rapid turnover and high number of vacancies at your agency, I have to worry whether there's anyone at home minding the store.

I know we both agree taxpayers deserve better. I hope as we discuss some of these problems this morning you will be frank with us on how we can help you get some of these troubled programs under control.

Thank you, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF SENATOR PATTY MURRAY

Secretary Snow, I want to welcome you back to this subcommittee. Since your last appearance, we've expanded our jurisdiction a bit, but I want you to know that your Department remains a priority for us and an area of deep concern.

THE PRESIDENT'S SOCIAL SECURITY PROPOSAL

I know that you've been traveling around the country trying to drum up support for the President's proposal to privatize Social Security. To me, breaking the promise of Social Security and putting millions of Americans at risk is wrong. I know that you and I aren't going to reach an agreement on that today.

But I think we can both agree that this national conversation has shown many Americans just how important Social Security is. Today, more Americans understand how important Social Security's guaranteed benefit is. More Americans know that Social Security helps—not just the retired—but also provides critical income for the disabled, for widows and for surviving children. And I think more Americans appreciate the stability and certainty of their Social Security checks as we've seen the stock market rise and fall like a roller coaster lately.

While I know we'll have a chance to talk about Social Security and issues like the health of our economy and the strength of the dollar, I want to make sure this subcommittee attends to its central responsibility—reviewing the President's budget for your department and reviewing how your department has spent the money Congress has appropriated.

So today I want to discuss what's in this budget, including the new initiatives the Secretary wants to launch. I also want to talk about what's not in this budget—the things the Secretary wants to terminate and the user fees the administration wants to impose on American families and small businesses.

I especially want to discuss the Department's continuing problems in managing major procurements. When it comes to addressing the agency's physical and IT infrastructure, it's clear that Treasury needs to do a better job in how it spends the dollars it collects from taxpayers.

BOOSTING TAX LAW ENFORCEMENT

Let me start with what is in this budget request. The administration is requesting a boost of more than $446 million for tax law enforcement activities. However, this boost will not signal a new historic high in IRS enforcement activities—far from it. As the IRS Commissioner told this committee recently, the agency's enforcement efforts have been allowed to wane in the last few years. I'm encouraged that the agency now wants to reverse that trend. And since the IRS fails to collect between $250 billion to $330 billion each year from tax cheats, I would say that this reversal couldn't happen soon enough.

CUTTING SERVICES TO TAXPAYERS

While the agency is finally addressing something it's allowed to languish for years, the way it's addressing it troubles me. The administration wants to pay for more enforcement by cutting direct services to taxpayers. The President's budget would cut services that are essential in helping citizens comply with the tax laws. For example, your budget proposal would close as many as one out of every four Taxpayer Assistance Centers across the country; eliminate phone tax filing, which is used by more than 5 million individuals and businesses each year; shorten the number of phone hours that IRS personnel are available to answer taxpayers' questions; discontinue tax law assistance through the internet; and cut outreach efforts to high-risk taxpayer groups. I don't believe that these cuts are merited if they will only heighten confusion and hassle for taxpayers and, perhaps, even make the compliance problem worse.

IMPOSING NEW FEES ON WASHINGTON'S WINE INDUSTRY

Unfortunately, funding for these basic taxpayer service functions is not the only thing missing from this budget. I am very concerned about the Secretary's proposals to eliminate funding for many essential functions in the Alcohol and Tobacco Tax and Trade Bureau. Instead of continuing to provide appropriated funding, the Secretary would impose new taxes on industry to pay for these functions.

Let me give you one example of great importance to families in my State. Over the past few years, the people in Washington State have built a world-renowned wine industry through hard work, research, and creativity. These vineyards are providing jobs for communities that have struggled. They're bringing tourists to many parts of our State, and they are helping our economy.

Over the past decade, wine has become a $2.4 billion industry to my State. Production has doubled, and now wine grapes are the State's 4th largest fruit crop. Today there are more than 300 wineries throughout the State—nearly double the number in 2000. And Washington's wine industry supports more than 11,000 related jobs.

Many of our wine producers are small, family-run vineyards. They should be encouraged and supported for the progress they've built with their own hands. Instead, this administration wants to hit them with more taxes in the form of new user fees. Mr. Secretary, I can tell you that your proposal to fund the alcohol tax bureau with "user fees" is going to impose a hardship our small family-owned vineyards. Forcing vineyards to pay a fee just to get their labels approved will hurt new entrants into this promising market. We should be encouraging their success instead of putting up more barriers to their viability. This proposal is especially puzzling coming from an administration that claims to encourage entrepreneurship and reduced tax burdens.

MAJOR PROCUREMENT PROBLEMS

Finally, Mr. Secretary, I want to raise my concerns regarding the Treasury Department's deeply troubled record in handling major procurements, especially IT services. We receive a continuing stream of reports from the GAO and the Inspector General regarding projects that are way behind schedule, that cost more than they should, or that are not adequately secure.

The Treasury Department has finally established its new human resource information system—known as "HR Connect." That system cost taxpayers $173 million. A similar system at the Coast Guard cost one-seventh that amount. A similar system at the Agriculture Department cost less than one-tenth that amount.

The Department's renovation activities are also a concern. The initiative to repair and restore the Treasury Building and its Annex has been badly mismanaged. The cost so far will soon top $250 million. But for all that money work on the Treasury Building is still not complete, and the Treasury Annex has not yet been touched.

Other examples of Treasury's poor management of major projects abound. Just last week, we read in the paper about an employee tuition assistance program at the IRS. More than 60 percent of the funding has gone to overhead, and less than 40 percent went to actual tuition assistance.

Treasury's efforts to procure a new secure communications system was recently slowed down because the agency failed to grant all the bidders access to the relevant information. As a result, the GAO sustained a bid protest.

And, speaking of the GAO, that agency informed us that, despite the progress the IRS has made in correcting information security weaknesses, more than half of the deficiencies identified 3 years ago are still not fixed. It's been 3 years, and half the improvements still haven't been made. And these aren't minor issues. Some of the vulnerabilities that still exist include the opportunity for any employee at the IRS and elsewhere in Treasury to have easy, unauthorized access to sensitive information including filings under the Bank Secrecy Act.

In terms of the largest amount of taxpayer dollars lost, we could hold several days of hearings on the Business Systems Modernization program at the IRS. It might take that long to compare what has been delivered under that program compared to what was originally promised.

Mr. Secretary, I recognize that you personally cannot stay on top of each and every one of these programs. But when I look at these persistent management problems at your agency, when I look at taxpayer dollars being wasted, when I look at the rapid turnover and high number of vacancies at your agency, I have to worry whether there is anyone at home minding the store.

I know that we both agree that taxpayers deserve better. I hope that as we discuss some of these problems this morning you will be frank with us on how we can help you get some of these troubled programs under control.

Thank you, Mr. Chairman.

Senator BOND. Thank you very much, Senator Murray. Senator Byrd.

Senator BYRD. Mr. Chairman, I hope you're recuperating well.

Senator BOND. Just mean.

Senator BYRD. Mean? Why, you've been that way all the time.

You just broke your shoulder, you just hurt your shoulder a few days ago.

Senator BOND. That just gives me an excuse.

Senator BYRD. Does your wife accept that?

Senator BOND. I have—there is a mad orthopedic surgeon who did me in.

Senator BYRD. Okay. Well, now, are you calling on me for an opening statement or for questions?

Senator BOND. We would like to be enlightened by your opening statement. We have not heard the Secretary's initial statement.

Senator BYRD. Yes. Well, I don't believe I'll make an opening statement. I hope I can get out before 10:30 or 10:45 for another appointment. I do have some questions.

Senator BOND. Well, we will have 5-minute questions, and as always, we ask the Secretary to submit his full statement for the record and to give us the highlights that he thinks are most important, and then we'll go on the rapid-fire question.

Senator BYRD. May I then retract my statement that I don't want to make an opening statement? I'll be very brief.

Senator BOND. All right, sir.

STATEMENT OF SENATOR ROBERT C. BYRD

Senator BYRD. Mr. Secretary, good morning to you.

Secretary SNOW. Good morning, Senator.

Senator BYRD. You're one of my favorite Cabinet members.

Secretary SNOW. Thank you.

Senator BYRD. I submitted a number of questions for the record when you testified before the Senate Budget Committee last February. I received your responses yesterday. I was alarmed by the vague answers you provided to some very straightforward questions.

You have been traveling around the country, as has the President, touting a plan to change Social Security. But here we are nearing the midpoint in the congressional calendar. The Finance Committee is holding hearings today and reportedly is preparing to draft legislation soon. The public still does not know how much the President's plan will cost or how it will affect their benefits.

Now, as a child of that generation that's been talked about a good bit recently, I can remember when the old people down in Raleigh County, West Virginia, didn't have anything to help them when they became too old to work. The only place they had left to go was over the hill to the poorhouse. They could stand at the gates of their children's homes with their hats in their hands and beg to be taken in, but, oftentimes, the children were not able to help them.

I can remember when the Social Security check was referred to as the old-age pension check. It came to my wonderful mom and dad, who are in heaven today. These old people raised me. They were not my biological father and mother, but they raised me. They were honest; they were religious. They didn't wear their religion on their sleeves; they didn't make a big hoopty-doo about it. But they were truly, truly religious.

I can remember the first Social Security checks they got. My, what a beacon of hope those Social Security checks were. And so, I have a deep-rooted respect and gratification for Social Security. I'm very concerned about Social Security.

I won't ask any questions right now, but I thank you for your appearance. I always have had a tremendous respect for you, and I like you personally. I will have a few questions for you later. Thank you, Mr. Chairman. Thank you, Mrs. Murray.

Senator BOND. Thank you very much, Senator Byrd. I believe you have had some dealings with West Virginia in your prior occupation, and obviously they were very satisfactory, and we've all appreciated those.

Mr. Secretary.

STATEMENT OF SECRETARY JOHN W. SNOW

Secretary SNOW. Thank you very much, Mr. Chairman, Senator Murray, Senator Byrd. Yes, I've had many dealings with West Virginia and the esteemed senior Senator over a long, long time, and I admire him deeply.

Thank you for the chance to come up today and talk about the Treasury 2006 budget request. We're still hoping to get the 2005 reprogramming approval as well. And you asked me what might be helpful in the Department moving forward with some of these initiatives. That's one thing, Mr. Chairman, that would be helpful.

Because of the homeland security issues that arose after 9/11, the Treasury Department is a very different place today than the place it was at the beginning of this administration. A large number, as you know, of law enforcement functions, have been taken from the Department and located elsewhere, primarily in the Department of Homeland Security, but some in the Justice Department. And the restructuring of the Department probably represents the largest governmental restructuring of any agency in modern times, as we lost some 35,000 people who went off to other agencies.

As a result, the Department is a very different place today. Its mission is in some ways more coherent. We're focused primarily on economic matters and finance matters, economic policy, advice to the President on economic issues is a primary function. Another function is collecting the revenues, as you know, and that's the single biggest part of the Department in terms of people, about 100,000 out of the 110,000 or 115,000 people are in the tax collection, tax administration, tax enforcement set of activities.

The Department is also responsible for collecting the bills and being the paymaster for the country, and managing the finances, issuing the debt, and managing the overall financial condition of the country.

In terms of economic policy, the issue we're most directly involved in now, as has been said, is Social Security. I know we'll have a good discussion on that as we proceed. The President's objective there, I think, is simply to have this dialogue with the country, to lay out the issues, and engender a better understanding of what's at stake here.

And what's at stake is awfully important. I agree with Senator Byrd. This is a system that millions of Americans depend on. I think some 45 million Americans receive Social Security checks today, of which—and this is the important point—a very high percent depend on that for their entire subsistence. This is a noble initiative of the American government. It's one of the most important programs that government ever undertook. It's served our Nation well for seven decades, and we need to take steps to make sure it serves us well going forward. So preserving and protecting Social Security has to be the major focus of that initiative, and putting it on a sustainable course.

We're also engaged in efforts to rethink the code and make sure that the Internal Revenue system is administered well, is simpler, is less complex, less burdensome, and is fair and encourages good behavior on the part of businesses and taxpayers so the economy continues to grow. You know the President appointed a panel co-chaired by two of your former colleagues, former Senator Connie Mack of Florida and former Senator John Breaux, with a number of other very highly thought of and distinguished people.

We've asked the panel to report back to us by the end of July. I'm in continuous contact with the co-chairs, and they're making a lot of good progress. And I look forward to getting their report at the end of July and then working with them and sending forward recommendations to the President, which I hope will lead to legislative proposals later this year coming up to the Congress.

We're also focused on the deficits. The deficits are too large. The debt levels and the deficits are too large. We need to continue to find ways to rein them in and to pursue fiscally responsible policies. That's an issue I know is very much on the minds of the committee as you oversee our activities.

PREPARED STATEMENT

You have mentioned the vacancies. We can talk about that. There are too many vacancies at the Department today, I acknowledge that. I also acknowledge the need to do better in this information technology arena, both at FinCEN and at the IRS. And I look forward to working with the committee as we continue to focus on how to make sure that the Department carries on its activities in ways that follow your directions and well serve the taxpayers of America.

And with that, I thank you.

[The statement follows:]

PREPARED STATEMENT OF SECRETARY JOHN W. SNOW

Chairman Bond, Senator Murray, and members of the subcommittee, I appreciate the opportunity to appear before you today to discuss the President's fiscal year 2006 budget for the Department of the Treasury.

The Department's budget reflects the President's top priorities for fiscal year 2006: fighting the financial war on terror while ensuring America's economic strength, and demonstrating the fiscal responsibility necessary to reduce the deficit. The fiscal year 2006 request of $11.6 billion also supports Treasury's longer term core strategic missions: promoting national prosperity through economic growth and job creation; maintaining public trust and confidence in our economic and financial systems; and ensuring the Treasury organization has the workforce, technology, and business practices to meet the Nation's needs effectively and efficiently. This budget request focuses on the President's belief that the budget be fair while holding the government accountable. It adheres to the principle that "taxpayer dollars must be spent wisely, or not at all."

Mr. Chairman, we provided the committee with a detailed breakdown and justification for President's fiscal year 2006 budget request for Treasury. I would like to take the opportunity today to point out some highlights of our request and then I'd be happy to take any questions you may have.

STRENGTHEN NATIONAL SECURITY

Treasury's budget reinforces the President's commitment to combating terrorist financing and safeguarding the U.S. financial system. Since September 11, we have leveraged the relationships, resources, and expertise that we have acquired over the past several years in combating money laundering to address terrorist financing and protecting our financial systems. Our efforts in both attacking terrorist financing and protecting the financial system are complementary and are effecting the changes required to protect the integrity of our financial systems by identifying, disrupting and dismantling sources, flows, and uses of tainted capital within those systems. To support these efforts, the President requests $351.3 million for fiscal year 2006.

The Office of Terrorism and Financial Intelligence (TFI) leads Treasury's efforts to sever the lines of financial support to international terrorists and serves as a critical component of the administration's overall effort to keep America safe from terrorist plots. The establishment of TFI unifies leadership for the functions of the Office of Intelligence Analysis (OIA), the Office of Terrorist Financing and Financial Crimes (TFFC), the Financial Crimes Enforcement Network (FinCEN), the Office of Foreign Assets Control (OFAC), and the Treasury Executive Office for Asset Forfeiture (TEOAF). The objectives of unifying this leadership are better coordination of Treasury's array of economic tools against terrorist and national security threats. To safeguard financial systems both at home and abroad, TFI draws upon a range of capabilities that cut across various categories, including financial sanctions, financial regulation and supervision, international initiatives, private sector outreach, and law enforcement support. TFI consolidates the policy, enforcement, regulatory, international, and analytical functions of the Treasury and adds to them critical intelligence components. OIA provides focused and operable intelligence in support of the Department's mission and policies. TFI's enforcement responsibilities are executed by the TFFC, OFAC, and FinCEN. Finally, TFI provides policy guidance for the IRS-Criminal Investigation Division (IRS–CI) in their anti-money laundering, terrorist financing, and financial crimes cases.

Since September 2001, the United States and its allies have designated 399 terrorist related entities and frozen over $147 million in terrorist assets. TFI has designated and frozen the assets of prominent terrorist financiers and organizations, including Adel Batterjee, a Saudi financier of al Qaida, and the Islamic African Relief Agency, a corrupt global charity that supported Usama bin Laden and HAMAS. Thanks to collaborative efforts by TFI and other agencies, the United States has facilitated the finding and freezing of nearly $6 billion in Iraqi assets outside of Iraq, the return of over $2.7 billion of those funds, and the recovery of more than $1 billion in cash inside Iraq.

Treasury's fiscal year 2006 request includes increases for resources to enhance Treasury's analytical capability so that senior officials have access to actionable financial intelligence. The request also supports TFI creating a 21st century information technology infrastructure to assist in the global fight against terror.

The Financial Crimes Enforcement Network has a major role in supporting TFI's enforcement responsibilities. The President's request includes $73.6 million for FinCEN to support its mission to safeguard the financial system from abuses of financial crime, including terrorist financing, money laundering and other illicit activity. This increase will provide FinCEN with the funding needed to enhance its outreach efforts to financial institutions newly covered by Bank Secrecy Act regulations and strengthen examination and enforcement activities; strengthen analytical support services; and expand FinCEN's support to other international financial intelligence units to facilitate information exchange.

The IRS–CI also plays a key role in investigating financial crimes. The request supports the unique skills and expertise of IRS–CI agents in investigating tax fraud and financial crimes not only to support tax compliance, but also benefit the war on terror and our efforts to root out financial crimes. These agents apply their training, skills, and expertise to support the national effort to combat terrorism and participate in the Joint Terrorism Task Force and other similar interagency efforts focused on disrupting and dismantling terrorist financing.

In addition, the Office of Critical Infrastructure Protection and Compliance Policy leads our efforts to safeguard the financial infrastructure. This Office works closely with other Federal agencies and the private sector to safeguard our infrastructure. That is essential, given that the majority of the critical financial infrastructure of the United States is owned and operated by the private sector.

Finally, an essential aspect of ensuring our national security is to secure fragile states and foster sustainable development in the world's poorest nations. The Office of International Affairs uses bilateral diplomacy and its role as steward of the international financial institutions, including the World Bank and International Monetary Fund—to create the economic growth that will reduce conflict and the conditions that favor terrorism in the developing world.

ENSURE FINANCIAL SECURITY

Treasury's strategic goal to manage the U.S. Government's finances effectively is the largest part of the President's fiscal year 2006 request for the Department. The budget request of $11 billion—the majority of which is for the Internal Revenue Service—underscores our commitment to provide quality service to taxpayers and enforce America's tax laws in a balanced manner. The request includes a 7.8 percent increase in enforcement funding over fiscal year 2005. The increase will provide additional resources to examine more tax returns, collect past due taxes and investigate cases of tax evasion.

It is important that these enforcement investments be fully funded, therefore the administration proposes to employ a budget enforcement mechanism used commonly in the 1990's for spending items that contribute to increased revenues or reductions in improper payments. Under the proposal, an adjustment for IRS enforcement would be made by the Budget Committees to the section 302(a) allocation to the Appropriations Committees found in the concurrent resolution on the budget. In addition, the administration will also seek to establish statutory spending limits, as defined by section 251 of the Balanced Budget and Emergency Deficit Control Act of 1985, and to adjust them for this purpose. To ensure full funding of the program and inflationary cost increases, either of these adjustments would only be permissible if the Congress funded the base level for IRS enforcement at $6.4 billion and restricted the use of the funds. The maximum allowable adjustment to the 302(a) allocation and/or the statutory spending limit would be $446 million for fiscal year 2006, bringing the total enforcement level in the IRS to $6.9 billion. This entire amount is included in the overall discretionary spending total sought by the administration and is fully accounted for in the budget.

The proposed fiscal year 2006 budget makes a strong commitment to a sound system of tax administration. The IRS collects $2 trillion annually; however, billions continue to go uncollected every year. The increase in enforcement funding will be used to bolster audit coverage of corporations and high-income individuals who try to evade taxes as well as to expand collection and criminal investigation efforts. These investments will pay for themselves several times over.

The President's request also provides $199 million to continue efforts to modernize the tax system through investments in IRS's Business Systems Modernization (BSM). The modernization program is providing real business benefits to taxpayers and IRS employees by delivering several modernized systems. For example, the Service implemented the Integrated Financial System that replaces its administrative accounting system. BSM funding allowed IRS to fully deploy online e-Services functionality for tax practitioners and other third parties, such as banks and brokerage firms allowing improved and faster interactions for transactions such as the application for e-filing, requests for Preparer Tax Information Number and Secure Electronic Return Originator applications, among many other products. The IRS also deployed Modernized e-File, which provides e-filing for the first time to large corporations and tax-exempt organizations. Replacing the outdated legacy system, the Customer Account Data Engine, which began processing the simplest 1040 EZ returns in July of last year, is a modern database that will eventually house tax information for more than 200 million tax returns per year.

The IRS also administers a refundable tax credit for the cost of health insurance for both qualified individual and family members. The request provides $20.2 million to continue implementation and operation of the Health Insurance Tax Credit Program. The annual cost of this program is reduced by over $15 million due to IRS's active program oversight and cost-cutting initiatives.

The Alcohol and Tobacco Tax and Trade Bureau (TTB) is responsible for the regulation of the alcohol and tobacco industries, and the collection of $14.7 billion annually in alcohol, tobacco, firearms, and ammunition excise taxes at a cost of $1 for every $368 collected. Our fiscal year 2006 request includes $91.1 million for TTB. The budget proposes to establish user fees to cover a portion of the costs of TTB's regulatory functions under its Protect the Public line-of-business.

The budget also includes a $236.2 million request for the Financial Management Service (FMS), which administers the government's payments and collections systems. In fiscal year 2004, FMS issued more than 940 million non-Defense payments, 705 million electronic payments and 235 million paper checks, FMS annually issues more than 940 million non-Defense payments valued at $1.5 trillion. The Budget provides funding for FMS's electronic initiatives, such as: Pay.gov, which is a Government-wide web portal to collect non-tax revenue electronically; Paper Check Conversion, which converts checks into electronic debits thereby moving funds more quickly; and Stored Value Cards, which directly support military operations overseas. The fiscal year 2006 request also includes legislative proposals to improve and enhance opportunities to collect delinquent debt through FMS's debt collection program.

The Bureau of the Public Debt (BPD) continues its management and improvement of Federal borrowing and debt accounting processes. The budget requests $179.9 million in direct appropriations for BPD which includes $3 million in user fees. The funding will allow BPD to continue improving the efficiency of the securities services to customers by expanding TreasuryDirect, an investment system that will enable Treasury customers to manage their investment accounts online.

The functions of the United States Mint and the Bureau of Engraving and Printing (BEP) are vital to the health of our Nation's economy. These two agencies fulfill the Treasury Department's responsibility of meeting global demand for the world's most accepted coins and currency. The United States Mint also continues to manufacture and market popular numismatic products, while BEP also continues to develop new designs of next generation currency to guard against counterfeiting.

PROMOTE ECONOMIC OPPORTUNITY

The Treasury Department works to ensure that U.S. and world economies perform at full economic potential. To reach this potential, the economy must increase its rate of growth and create new, high quality jobs for all Americans. The legal and regulatory framework must also support this growth by providing an environment where businesses and individuals can grow and prosper without the burdens and costs of unnecessary rules and regulations.

Our budget requests $1.6 billion to support these strategic goals. The request includes funds for policy offices that guide domestic economic development, tax programs, financial institutions and other fiscal matters. These policies are essential as Treasury works to simplify the U.S. tax code and create a legal and regulatory framework that allows the Nation's businesses to thrive.

Treasury's international programs and three Treasury bureaus, the Community Development Financial Institutions Fund, the Office of the Comptroller of Currency and the Office of Thrift Supervision play diverse roles in fostering economic growth and prosperity. From serving as the President's principal economic advisor to maintaining the health of the national banking and thrift system, the Treasury has a significant influence on creating the conditions for a robust economy. Through the Office of International Affairs, the Treasury also pursues diplomacy to create the conditions for global growth, which creates economic opportunity at home and overseas, by a range of actions, including the reduction of undue barriers to trade and investment and the establishment of stability in the international financial system.

Treasury's international assistance programs request of $1.5 billion for fiscal year 2006 is part of the Foreign Operations, Export Financing, and Related Program Appropriations Act. These programs include multilateral development banks (MDBs), debt reduction, and technical assistance—all critical instruments to promote the administration's international economic agenda. MDBs promote global economic growth and poverty reduction, and help create stronger markets for U.S. goods and services. Debt reduction helps poor countries move to a sustainable level of debt and remove debt overhang that inhibits growth. Our technical assistance programs help countries institute the sound budget and financial systems needed for economic growth.

MANAGE FOR RESULTS

The President requests $211.8 million to protect the integrity and effectively manage the resources of the Department of Treasury, and ensure that it remains a world class organization. Included in this request is $16.7 million to fund the Department's Office of Inspector General (OIG) and augment audit and investigative capabilities.

This portion of the budget also includes $133.3 million for the Inspector General for Tax Administration (TIGTA) and its efforts to oversee the Nation's tax administration. TIGTA continues to play a significant role in providing independent oversight, which promotes efficiency and integrity in the IRS's ability to collect $2 trillion annually. TIGTA aggressively combats any identified attempts to disrupt and/or interfere with tax administration. The Nation's voluntary tax compliance system is supported and protected by TIGTA agents who participate in the Joint Terrorism Task Force and proactively seek to identify individuals or groups who pose a threat to effective tax administration. Critical information is shared with the IRS and allows the leaders of the IRS to make effective business decisions, which promote efficient tax administration and support IRS employee safety.

The proposed budget request includes $7.9 million in new funding to provide for an improved technology infrastructure, essential for keeping pace with the Department's needs to enhance productivity, improve communication, interact effectively with the world-wide financial community, and meet other management needs. Funding will be used to improve the Department's information technology infrastructure to ensure the effectiveness of the Department in managing Federal finances and combating financial crimes and terrorist financing. The request also ensures that the Department will continue its major facilities projects and services for the Main Treasury and Treasury Annex buildings to ensure the safety and health of occupants and perform structural repairs and improvements. Additional funds will allow Treasury to complete the project during fiscal year 2006 and reoccupy the restored office space.

THE PRESIDENT'S MANAGEMENT AGENDA

Treasury has focused its management initiatives around the goals of the President's Management Agenda (PMA). Under guidance from the PMA, the Treasury has grasped tangible results in managing the Nation's finances, taking advantage of new opportunities and opposing threats. The Department is committed to defining desired results for each area and managing to achieve them, at acceptable cost levels.

In fiscal year 2004, Treasury achieved significant milestones in implementing the President's Management Agenda, improving three of our five status scores for the PMA over the prior year.

Treasury managed for results as we implemented a new performance appraisal system for our Senior Executive Service that links managers' performance assessments to accomplishing the Department's top priorities. We are also focusing on recruiting and retaining a world-class workforce, and have started implementing a new Human Capital Strategic Plan. This plan is the Department's roadmap for molding a workforce of engaged, highly competent, and business-aligned employees.

The Department is making good progress on using competition to improve efficiency. This past year, we completed five public-private competitions, and as a result, expect savings of $200 million over the next 5 years. Our efficiency initiatives have received national recognition, winning the President's Quality Award for Management Innovation at the IRS for our Area Distribution Center competition.

Treasury continues to be a leader in making financial information available in a timely manner through a 3-day close of its books at the end of each month, and for the fifth consecutive year we received a clean audit opinion. The Department continues to work at securing our information systems. Our systems are more secure now than at any other time, with 86 percent certified and accredited as secure at the end of 2004.

CONCLUSION

Mr. Chairman, I look forward to working with you, members of the committee, and your staff to maximize Treasury's resources in the best interest of the American people and our country as we move into fiscal year 2006. We have hard work ahead of us and I am hopeful that together we can work to make the Treasury a model for management and service to the American people, and continue to generate economic growth, increase the number of jobs for our citizens, and keep our financial systems strong and secure.

Thank you again for the opportunity to present the Treasury Department's budget today. I would be pleased to answer your questions.

TREASURY DEPARTMENT VACANCIES

Senator BOND. Thank you very much, Mr. Secretary. We're talking about unfilled vacancies. The—I'm particularly troubled at key management positions, Deputy Secretary, Assistant Secretary for Management, Chief Financial Officer remain unfilled.

How do you hold a staff accountable, how can you operate it when key people that should be in your organization are not there? What are the plans to get these positions filled?

Secretary SNOW. Well, Mr. Chairman, the work of the Department is getting done, but it sure would be desirable and helpful to have those vacancies filled. Several of those vacancies are standing in the nomination process awaiting hearings. More are awaiting clearance through the White House process. And I'm in continuous touch with the White House Personnel Office and Office of the Chief Counsel——

Senator BOND. Please give them our best wishes, would you?

Secretary SNOW [continuing]. And urging them to move this process along. But in terms of the work of the Department, though, while it would greatly help us to have these people in place, the Department has a terrific group of hardworking civil servants and a good work of political people, small but able, and the work is getting done. It's a lot of overtime though for us these days.

Senator BOND. But, Mr. Secretary, I mentioned the GAO reports that security weaknesses place sensitive taxpayer and Bank Secrecy Act information at risk, and TIGTA has also identified numerous problems with IRS information security. You, under the Federal Information and Security Management Act, are responsible for providing information security, and are you alarmed by the GAO's findings? And how and when are you going to resolve these problems?

Secretary SNOW. Senator, this is a serious issue and we take it seriously. We are committed to the information security of the systems we have at the Department, and pledge to you this will be a priority.

I talked to the Acting Deputy Secretary this morning about it and the Chief of Staff, and we're all going to make every effort to close the gap. We know there's a gap here. We're also going to work closely with the Department's Inspector General, Harry Damelin, a position that was recently filled, I'm delighted to say, and with Russell George of TIGTA, the Inspector General for the IRS, both of whom are aware of these issues and will be very helpful in bringing them to closure. We recognize we have some distance to go here.

TERRORIST FINANCING

Senator BOND. I—again, I'm concerned, as I mentioned earlier, about your work on terrorist financing. We created the Office of Intelligence and Analysis, but Treasury, it appears to us, has not stepped up to the plate. This seems to support the conclusions that OIA will merely become an operational unit, not adding any value or, even worse, assuming the role of the Treasury's current assets at OFAC and FinCEN.

What will the roughly 25 analysts transferred from OFAC to OIA be doing that is different from what they were doing at OFAC? And how will this transfer impact the OFAC? And I'd just ask the general question, shouldn't the OIA serve the policy makers at Treasury and leave the operations to operational units? That's my concern.

Secretary SNOW. Right. Mr. Chairman, this is an issue that we spent a lot of time on thinking through and trying to get right. And the very able Under Secretary who is responsible for this whole collection of activities, anti-money laundering, terrorist finance, protecting the financial system against money laundering and terrorist finance, and leading the financial war on terror, came to the conclusion as he looked at his organization that the best way to fulfill the responsibilities, the critically important responsibility he has, is to take the intelligence function and concentrate it under the new Assistant Secretary for Intelligence and Analysis.

As he's told me, these people, these—I think it's 23 analysts who were in OFAC—even if there had been no resource constraints on the Department, are the very people you would want at the center of the intelligence-gathering activities to strengthen our ability to carry on these functions. And OFAC will be able to have full access to the intelligence that's gathered.

His view, and I share it, is that our function will be strengthened by putting the intelligence under a very capable Assistant Secretary for Intelligence and Analysis, and then led by a person whose full-time job is intelligence.

Senator BOND. Thank you, Mr. Secretary. I'll have further questions on that, but now I'll turn to Senator Murray.

Senator MURRAY. Mr. Chairman, with your permission, I want to yield to Senator Byrd. He has a time commitment.

SOCIAL SECURITY

Senator BYRD. I thank you, Mr. Chairman. I thank you, Senator Murray. Mr. Secretary, I only have 5 minutes. I have several questions. I'll try to ask only five. I hope we can limit them to 1 minute each.

Mr. Secretary, Mr. Bush told workers in his State of the Union address that, with regard to personal accounts, your money will grow over time at a greater rate than anything the current system can deliver. Question No. 1: However, the stock market has ups and downs. If workers retire when the stock market is down, they're in deep trouble. They can't wait for the market to recover. What guarantee would the administration support to ensure a minimum benefit from an individual account?

Secretary SNOW. Senator, you're right. Markets go up and down, but over any long period of time, the evidence suggests that investments in the market over a working life will produce rates of return that are higher than what you could expect from Social Security. And while there's not a guarantee, there is this long history of the superior performance of markets.

But taking your point, under the President's proposal, and we're continuing to think about how to put this forward in a way that's most effective, there is the suggestion that it—I think it's 47—when a person turns 47, their account would automatically shift heavily into fixed-income instruments, bonds, so the principal would be protected. But it's a good point and one we've been giving a lot of thought to.

Senator BYRD. What happens if the checks that you mentioned prove insufficient? What happens when it comes time to retire and a worker discovers that he doesn't have enough saved away to ensure a decent, respectable living? What happens to that worker?

Secretary SNOW. Senator, the President recently indicated his support for a proposal associated with somebody named Bob Posen. And the Posen proposal is designed to make sure that nobody retires below the poverty level. That's a view I think that is widely held within the administration as well. And in the final legislation I'm confident that there would be language to assure that that outcome is achieved.

Senator BYRD. Under the President's plan, what guarantee would workers have of receiving the level of benefits scheduled under current law?

Secretary SNOW. Senator, the Social Security Administration Actuary indicates that in—I think it's 2041—the benefits will fall to the level the trust fund can't afford to pay, which is their revenue stream, which is about 70 percent. The idea of the personal accounts is that you could do better with the personal accounts than you could do with Social Security alone. But the details of that have to await the discussion with you and the members of the Senate and the House.

Senator BYRD. What happens to a worker whose account has not accrued enough to buy an annuity to guarantee a payment above the poverty line?

Secretary SNOW. Senator, as I said, the administration's view broadly stated, and the President indicated this in some comments he made recently, is that we need to assure people who have had a working life that they retire above the poverty line. And I think that idea will be incorporated in our final set of proposals.

Senator BYRD. Mr. Secretary, we've heard a great deal about the President's "plan". When will the President submit his "plan" in detail, and with respect to a draft bill that would contain those details so that the Congress will know what is being suggested and how to respond to that?

Secretary SNOW. Well, the President has indicated, Senator, that he wants this broad dialogue and he thinks that out of the broad dialogue in which he's put some ideas forward and invited others to come back with other ideas, that that broad dialogue, that environment of open ideas, is better calculated to create a good result than now laying out a firm set of proposals.

In part, I think it's because of the need for this education we talked about earlier. And I appreciate what Senator Murray said, that now because of this effort to go to the country, there is a better understanding of the importance of Social Security, the role it plays in our lives, and I think also of the need to find ways to put it on a financially sustainable course.

Senator BYRD. I have one final question, Mr. Secretary. You say that we seek information, that we seek a dialogue, that the President seeks a dialogue. How can we have a dialogue, when we don't know what's in the details of the President's plan? We need to know the details of that, so that we can then have a real dialogue. Can you respond?

Secretary SNOW. Well, I'll try, Senator. The President has set up his proposal that's fairly detailed on the personal accounts and how those would work, setting aside up to 4 percent of income, up to $1,000 growing at $100 a year plus the wage index, with a lot of other details.

On the solvency side, the President has said we need to have a permanent solution. It has to be done in a way that doesn't adversely affect retirees or near-retirees. And he's sent up a number of proposals. I think this came out of the State of the Union message on ways that you might fix the sustainability, how you might put it on a solvent course. That included going to a price index versus a wage index and changing the formula for calculating inflation on benefits and changing wage indexing and some means-testing and so on.

His point in sending that up was, these are good ideas. He subsequently said he sees merit in this Posen proposal I mentioned. And he's saying, if you, the Members of the Congress, the Republican side, Democratic side, like these ideas, I want to work with you, if you've got better ideas I want to work with you.

And the President's view is that out of this dialogue about these proposals, having to find the problem will get the best result. At some point maybe it will be necessary to come forward with a more detailed proposal. But the current hypothesis the President's working under is that laying it out the way he has is best calculated to get good results in the end. People can disagree on that, I agree.

Senator BYRD. Mr. Secretary, I thank you. I'll submit further questions. I don't think much of the idea of waiting beyond midterm to let the Congress and the people of the country know what the details are of the President's plan. Let's hear it from the President.

Thank you, Mr. Secretary. Thank you, Mr. Chairman, and thank you, Senator Murray.

Senator BOND. Thank you, Senator Byrd. Senator Murray.

Senator MURRAY. Thank you, Mr. Chairman. Mr. Secretary, I understand that the Treasury Department has reportedly formed a Social Security war room that included hiring five full-time employees. The stated purpose of the Social Security Information Center, as it's named, is to monitor political reaction to the administration's Social Security proposal, as well as to coordinate public affairs activities for it.

Our appropriations bill has included a provision for dozens of years that states the following, and I want to read it out to you: "No part of any funds appropriated in this or any other Act shall be used by an agency of the executive branch other than for normal and recognized executive/legislative relationships for publicity or propaganda purposes and for the preparation, distribution, or use of any kit, pamphlet, booklet, publication, radio, television, or film presentation designed to support or defeat legislation pending before the Congress, except in presentation to the Congress itself."

Mr. Secretary, do you have any reason to believe that any of the activities of this Social Security Information Center or any other part of your agency could be in violation of that provision?

Secretary SNOW. No, most definitely not, Senator. The President has identified Social Security as a priority. I serve as the managing director of the Social Security Trustees. The actuary of the Social Security system has pointed out in the reports and told the trustees that the system isn't sustainable.

I think we have a responsibility, given the financial condition of Social Security, to talk to the country about it, inform the country, have the dialogue with the country, and lay the foundation through that dialogue of public information, and that's what this is, public information, lay the foundation through that broad-based public information dialogue to——

Senator MURRAY. Well, Mr. Secretary——

Secretary SNOW [continuing]. To get some answers.

Senator MURRAY. Is the Treasury Department engaged in providing funds in the form of compensation for any opinion leader or any media personality for the purpose of advancing the President's Social Security——

Secretary SNOW. No.

Senator MURRAY. No? Okay.

Secretary SNOW. This office is four or five people. It's a normal public affairs function that serves under the Assistant Secretary for Public Affairs, Rob Nichols, who oversees the entire office, and it's funded entirely out of his executive budget.

Senator MURRAY. Okay. Has the Department used any of those funds to produce television or radio segments that address the issue of Social Security that have been disseminated to media outlets?

Secretary SNOW. Not that I'm aware of, Senator. I'll check and see. I don't think so.

Senator MURRAY. Okay. Have you taken any safeguards to ensure that any elements of your Department, especially the Social Security information center, are not in violation of the law as it relates to the promotion of legislation that's pending?

Secretary SNOW. Senator, the activities of this office are reviewed by the Inspector General and they're reviewed by the general counsel. Both parts of Treasury are peopled by very able staff, and they know our commitment to living within the rules of the law. So, no, I have no reason to be concerned there.

TAXPAYER SERVICE

Senator MURRAY. Thank you very much. I appreciate that. Mr. Secretary, last year your Department testified that the key to getting greater compliance with our tax laws was through a combination of enforcement and taxpayer service. This year, however, you are poised to make significant cuts to taxpayer services in order to pay for your requested increase in enforcement. These cuts, as I had talked about, are closing taxpayer assistance centers, reducing telephone service, eliminating phone-routing sites, discontinuing filing by telephone. All of these are used by millions of taxpayers and businesses.

And I wanted to ask you today why your agency abandoned its position regarding the important balance between taxpayer services and enforcement?

Secretary SNOW. Well, Senator, I don't think we have. It's a balance we always strive to reach. It's never easy, but it's certainly our objective to be balanced in law enforcement and in customer service.

Senator MURRAY. Are you concerned that any of these reductions will result in less compliance with the tax code?

Secretary SNOW. Senator, I don't think so, but that's something that we will monitor. This is a running dialogue when I meet regularly with the IRS Commissioner, and he knows my deep concern in seeing that the IRS find that middle way where they're collecting the revenues, enforcing the law, creating an environment of law enforcement, but doing so in a way that respects the rights of taxpayers and treats them with dignity.

On that very subject I had a long discussion yesterday with Nina Olson, the head of the taxpayer advocacy part of the IRS, and we do our best. I'm sure we make mistakes, but we do our best to try and find the middle ground. And with respect to the Taxpayer Assistance Centers, we're going to monitor that. We think that it's the right thing to do, but we're going to continue to monitor that to make sure that's the case.

Senator MURRAY. Well, I hope we do monitor it. I'm worried that it will monitoring something that's already closed, it'll be too late to start it. But I did—you mentioned in your remarks at the beginning your reprogramming request for fiscal year 2005?

Secretary SNOW. Yes.

Senator MURRAY. Well, given the priority that your budget places on tax and law enforcement, I'm kind of mystified as to why this reprogramming request asks us to transfer $11.5 million out of tax law enforcement to Business Systems Modernization. Can you address that?

Secretary SNOW. Yeah. Again, we're just trying to get the balance right, and getting that balance right is something that sometimes requires some movement of funds from one pocket to another or one box to another box.

Senator MURRAY. My time is up, Mr. Chairman.

OFFICE OF INTELLIGENCE AND ANALYSIS

Senator BOND. Thank you, Senator Murray. Mr. Secretary, I've asked you about intelligence operations and I want to follow up. Can you explain to us in simple terms what you're doing with OIA and the relationship with OFAC and FinCEN. I'd like to know what you think OIA's appropriate role is, especially when it appears to be duplicating some of the work of OFAC and FinCEN? In addition, has OIA produced any analytic product for Treasury or the intelligence community?

Secretary SNOW. Yes, Senator, but it's a new part of the Treasury. It's going to be a very important part of Treasury. It's going to underpin the whole Department actually, because everything rests ultimately on good intelligence. Having a strong intelligence component of the Department means we get a seat at the table with the other intelligence agencies of the United States Government, and that seat at the table with real capacity, with real status and resources means that we're going to be much more effective in drawing information, sharing information, and having the confidence of others in the intelligence community.

And that's really the objective here, having the confidence of others in the intelligence community, having a strong seat at the table, and being able to play effectively in the intelligence-sharing arena with the other 15 or 16 agencies of the Federal Government who were involved in intelligence.

BSA DIRECT

Senator BOND. You have delegated responsibility to administer the Bank Secrecy Act, or BSA, to FinCEN, and last year the committee provided $5 million over the President's request for FinCEN to complete the first phase of BSA Direct. Do you support the BSA Direct project, and what's its current status?

Secretary SNOW. Senator, I very much support it. I noted your comments in your opening statement on that. I share those views that it should be under TFI, it should be under FinCEN, and we hope to have that BSA Direct completed by, I think it's September or October of this year, where then FinCEN would have its own secure data system.

Senator BOND. Do you think BSA Direct is going to improve the security gaps of BSA data as the GAO reported?

Secretary SNOW. Yes, absolutely. I think it will, and that's one of its key purposes.

Senator BOND. What's the relationship between the IRS and FinCEN in the sharing of data, and what safeguards and firewalls are in place?

Secretary SNOW. Well, Senator, historically of course the Detroit Computing Center has been a source of substantial repository of data that was used. It was the principal data center. What we're doing is moving off of the dependence on the IRS data system to BSA Direct, which will then give FinCEN control over the data it needs to carry on its activities. I think it'll be a much better arrangement.

CUBA SANCTIONS

Senator BOND. Let me turn to trade. I'm a supporter of trade sanctions reform, the Export Promotion Act of 2000, and the Agricultural Export Facilitation Act. They first cleared the way for agriculture exports to Cuba. The second reforms the requirements of OFAC regulations that are frustrating farmers' efforts to sell in the market.

Congress has spoken clearly that there's a significant growing market for U.S. agricultural goods in Cuba, which has grown to over $400 million a year. However, the OFAC rules requiring advance cash payment or a letter of credit are essentially frustrating the efforts of U.S. farmers ability to sell to Cuba. This has all the earmarks and as well as smelling like a regulatory effort to stop agriculture trade with Cuba.

I don't think we can kick away a $400 million export market. If that is not the intent, what was the compelling need to issue the regulations? How are the concerns of farmers, the reason for passing the legislation, taken into account? And I'd like to hear an explanation of what's happening.

Secretary SNOW. Well, I understand this ruling has sparked some interest in the Congress.

Senator BOND. A master of understatement, Mr. Secretary. I give you credit for that.

Secretary SNOW. And it came about, Mr. Chairman, because of a request from financial institutions for a clarification of the so-called cash in advance policy. And cash in advance is the term of art used in the statute, and the OFAC lawyers, when they looked into that request for clarification, determined that the best statutory construction was cash in advance of shipment.

There had been some people in the trade who were complying with it through cash in advance of title transfer or cash in advance of lading transfer. And in looking into it and thinking about it, the lawyers at the Department, the lawyers at OFAC and then at the General Counsel's office, reached the conclusion that the better reading of cash in advance was that it meant cash in advance of shipment.

Senator BOND. We'll have to help the lawyers understand that better. Senator Murray.

TAX AND TRADE BUREAU

Senator MURRAY. Thank you, Mr. Chairman. Mr. Secretary, I talked a little bit about the wine industry in my State in my opening statement, and I wanted to ask you today about the large number of user fees you have in your budget request. In one small agency, the Alcohol and Tobacco Tax and Trade Bureau, you're asking to impose five new or increased fees equaling 31 percent of the agency's budget.

I'm told there's no direct relationship between the actual services the wine-making industry receives from TTB and the fees you now want to impose on them. And I want to know why there's no correlation. And wouldn't you agree that if there's no correlation that these really are new taxes and not user fees?

Secretary SNOW. Senator, I think the users, the people who get services from TTB, get something of value, and these charges or fees are designed to reflect some of the value that is received by the users back on to the users. The goal is to have the industry pay for some portion of the benefits that it gets.

Senator MURRAY. Well, are you aware that the wine industry already pays $550 million in Federal excise taxes every year? How did you ever come to the conclusion they needed to pay more?

Secretary SNOW. Well, Senator, the banks fund the Federal Reserve and the thrifts fund OTS, the national banks fund the OCC. There's a well-established tradition in this country that if you're regulated, some portion of the costs of the regulatory activities should be borne by the regulatees.

Senator MURRAY. Well, let me also ask you, I know your agency is planning to penalize vineyards that don't file their certifications electronically by charging a higher fee to use paper filing. But I'm told by the industry that they have a lot of problems with the electronic filing system. They have difficulty registering just to use it, it often rejects their label graphics, and when those labels are rejected, the system only cites the portion of the regulation the labels violated, which doesn't actually tell the vineyard what the problem is and how they can fix it.

You know, I also should tell you that the paper processing system isn't much better. TTB claims to be processing labels in 9 days, but I'm told it takes anywhere from 2 to 4 weeks. And I wondered if you considered improving the online processing system to make it workable for the industry before we started imposing fees.

Secretary SNOW. Well, Senator, I appreciate your comments. I will commit to you that I will look into that and get myself better informed about the paperwork burden and the feasibility of moving to electronic filing.

Senator MURRAY. Do you know if there's any—are there any new initiatives to make them more user-friendly, or is—the only new initiative is user fees? That's what I'm hearing from the industry.

Secretary SNOW. Well, I think TTB gets pretty high marks from the industry by and large. I think they're thought to be a responsive agency that tries to do things in ways that are reasonable. But we have Harry Damelin, the very able new head of the Inspector General's office here. He's listening to this. I'm sure he's taking this in and he'll help us take a look at that.

Senator MURRAY. Okay, very good. Well, I look forward to hearing more from you on that, because it really is concerning many of us. And I understand the chairman has a wine industry in his State as well, so I'm sure we'll be able to work on that.

Senator BOND. Long before yours.

Senator MURRAY. Long before mine, I'm told. Well, maybe we should compare. We can have a taste test. And professionally, of course.

Let me ask one more quick question. In the interest of better isolating terrorist financing, your Department is considering a proposal to track financial wire transfers into and out of the United States. Those wire transfers represent more than $6 trillion worth of activity per day, and while some officials and experts believe that wire transfers might contain useful information to track down terrorists, others are very concerned that the volume might overwhelm any tracking system you can put in place. And others are worried that your efforts might invade the privacy rights of individuals and businesses.

In my short time left, can you tell me how the Department can realistically monitor this, and how we're going to monitor the privacy of individuals?

Secretary SNOW. Senator, those are the very issues that are under review in this analysis that's been undertaken. And we will keep you posted as we move forward with our thoughts on that subject. But it is an issue that needs to be addressed.

Senator MURRAY. Are you requesting additional funds to do that monitoring, or how is that going to——

Secretary SNOW. I think there's a study underway right now that's adequately funded.

Senator MURRAY. So do you need—do you anticipate any new funding needed to monitor this, both for privacy and——

Secretary SNOW. Well, if there is one, we're some distance away from having a proposal on this, and as that is thought about and developed, we'll certainly think about the budgetary side of it and appropriations side of it as well. But I don't have an answer to you yet.

Senator MURRAY. Thank you very much, Mr. Chairman.

Senator BOND. Thank you, Senator Murray. Senator Dorgan.

CUBA SANCTIONS

Senator DORGAN. Mr. Chairman, thank you very much. Secretary Snow, I apologize for being late. I was over on the floor of the Senate. But I do have some questions, and I understand my colleagues have asked some of them. In fact, I was pleased to hear the question from the Senator from Missouri, the Chairman, about Cuba and family farmers.

Let me just make a point on that. You know, the Congressional Research Service in writing says that it believes what the Treasury is doing here does not conform to the law. So I don't know what lawyers you have over in OFAC that are giving advice there, but at least the Congressional Research Service says they believe you've gone outside of the law to do this.

Before I ask you about Cuba, I should tell you that Secretary O'Neill sat at that table before you, and I was chairing the subcommittee at that point, and I asked him repeatedly about Cuba and said, you know, just let me ask you a question, wouldn't you prefer to use the resources at OFAC, the Office of Foreign Assets Control, to track terrorist financing rather than track people who are under suspicion of vacationing in Cuba, or tracking Joan Scott, who delivered free Bibles in Cuba, tracking Joan Sloat, who took a bicycle trip with a Canadian bicycling group, or tracking the guy who took his dad's ashes to be distributed at the church his dad used to minister in.

I asked Secretary O'Neill three times, wouldn't you really sooner use OFAC to track terrorist financing rather than go after these people who are suspected of taking a vacation in Cuba or whatever. And finally on the third or fourth time, he said, you know, of course, of course. And within hours, he was upbraided with a press release from the White House. So I'm not going to ask you a question that's going to get you in trouble. My intent isn't to ask you a question for that reason, but wouldn't you sooner use the assets of the——

All right. Skip that question. You can put your answer in writing if you'd like and I promise I won't share it with anybody, Mr. Secretary.

The Chairman asked the question about the issue of shipments to Cuba, the agriculture shipments, and we have something called the Trade Sanctions and Export Enhancement Act of 2000. I helped write it. And it was put in the bill—these are sanctions that—it says you cannot do anything to impede the movement of agricultural products unless there's a vote of both the House and the Senate to do so.

And clearly this is a—what you have done is a prohibition or a condition or a restriction on the export of agricultural commodities. It is clearly done to impede the movement of agricultural commodities. Everyone understands that and believes that. And I would just ask, have you, Mr. Secretary, studied the Congressional Research Service report that says on its face they believe that what Treasury has done here is not legal?

Secretary SNOW. No, Senator. I haven't. But I'm sure the lawyers from Treasury have, but I have not.

Senator DORGAN. All right. Do you know how many lawyers in OFAC are tracking vacationers to Cuba and tracking all these issues dealing with agricultural sales to Cuba? My understanding is it's something like 21, which is a multiple of 4 of those who are tracking terrorist financing.

Secretary SNOW. Senator, I don't have that number in my head, but I will confirm——

Senator DORGAN. Would you send that to me?

Secretary SNOW [continuing]. It for you. Yeah, I will send it to you.

Senator DORGAN. I would hope that just behind the curtain you'll be a lonely voice in the administration saying, let's just stop the obsession here. We don't like Castro. The quickest way to get rid of Castro is through trade and tourism, just as we believe that engagement with communist China and communist Vietnam has enhanced—moving them in the right direction is enhanced by trade and tourism. We believe the same with respect to Cuba.

NEW HOMESTEAD ACT

But let me ask you two other quick questions if I have the time, Mr. Chairman. One is I want to show you a chart. This chart shows the depopulation of the heartland. The red are the rural counties in America. As you can see, kind of an egg-shaped in the heartland of America that's being depopulated in the last quarter century or last half century.

And Senator Hagel from Nebraska, Senator Brownback, myself, and others have introduced legislation called the New Homestead Act. We don't have land to give away anymore, but we clearly are seeing a relentless depopulation a century after we populated this through the Homestead Act. I'd like very much to visit with you at some point about the strategy here. It's bipartisan. We've had a big, broad bipartisan group put this together, and I'd like to talk to you about that.

TAX HAVENS

Finally, I want to ask you a question about tax havens. Let me express my concern. I think Senator Murray expressed concern about closing walk-in taxpayer assistance centers. I want to register on that. But I've introduced some legislation on tax havens. I read the other day that Exxon has the largest quarterly profit in the history of humankind, $8 billion for the quarter, and I know that Exxon has 11 tax haven subsidiaries in the Bahamas, not for the purpose of doing business there, but for the purpose of helping run the corporation out of a mailbox and reducing their tax burden in the United States.

And I've introduced legislation that says, you know, if you're moving to tax havens not for the purpose of doing business there, but for the purpose of avoiding taxes, you're going to be taxed just as if you never left this country. And I'm wondering, give me your observation about that approach.

Secretary SNOW. Well, Senator if the activity is done primarily to avoid taxes and not for a profit undertaking, profit-making purpose, then it shouldn't enjoy the tax advantages. I mean, that's part of the policy that we're trying to see incorporated in the enforcement. It's the essence of this doctrine that lies behind so much of our enforcement. If it doesn't have a legitimate business purpose, then you're not going to get the tax advantage associated with it.

Senator DORGAN. But I think you need a change in law to accomplish good enforcement here. And I think that when you take a look at all of these subsidiaries sort of being established, I mentioned Exxon, I mention Xerox, Halliburton, so many corporations have set up massive numbers of subsidiaries, not for the purposes of doing business, but for the purpose of avoiding taxation. I would fully support your increased enforcement efforts, but I think you need a change in legislation that would say, in those circumstances where they set it up exclusively to avoid paying U.S. taxes, they shall be taxed as if they had not left this country.

Mr. Chairman, thank you. I apologize for being late to you and the ranking member.

Senator BOND. Well, we missed you, Senator Dorgan. We're glad you could join us. Unfortunately, I'm going to have to turn the gavel over to my very capable ranking member because I have to go to the floor soon where I have a few things going on now.

CDFI FUND

But I want to ask you about two things, Mr. Secretary. I mentioned I'm very disappointed in the decision to—essentially to eviscerate CDFI. CDFI funds go to financial institutions that are serving areas that are underserved by financial institutions. And I, as a former Governor, can tell you there's a minimum amount of high enthusiasm for using a block grant to ensure that underserved areas have financial institutions. It just makes no sense.

What's the administration going to do to ensure that financial institutions which are serving underserved areas will continue to have the incentive and capacity to continue to serve these areas?

Secretary SNOW. Well, Senator, I'm not real close to all that's going on in that arena. That's really Secretary Jackson and Secretary Gutierrez. But I am pleased that the most important single part of the Treasury programs in this area, something called the New Markets Tax Credit, will remain fully funded as part of the Treasury Department.

With respect to the other consolidation of these programs, primarily in Commerce as I understand it, the view is that these programs will be more effective if they're streamlined and consolidated.

Senator BOND. I just disagree on that. But since you mentioned New Markets, CDFI would be funded at only $7.9 million. GAO found in a January 2004 report that under the New Market's formula, 39 percent of all census tracks qualify for these tax credits. I'm wondering if there's any effective administration in the Treasury Department to know that it's benefiting, truly benefiting economically distressed programs. What quantitative methods are used to determine if this program works? And what's the Treasury doing to ensure these tax credits are meeting benchmarks, and can you quantify the success or failure of the program?

Secretary SNOW. Mr. Chairman, that's a heck of a good question. This program——

Senator BOND. I thought it was too.

Secretary SNOW. It's a heck of a good question.

Senator BOND. Because I really—I have great questions about New Markets. I'm afraid it's just throwing money out the door.

Secretary SNOW. Well, it's the very question that I have put to the folks who oversee the program. Having participated in a number of these meetings though with local participants, you get a sense when you're out there and see a community—they only go to poor communities—that bringing private capital with the tax credits, with community leaders, produces some good results. Now, whether in the aggregate the benefits significantly or marginally or don't exceed the costs of the tax credits is something that we have to do more analysis on. It's probably too early to say. It would be too early to say.

Senator BOND. I tell you what, I've never gone to a community that has gotten some Federal money, either from direct strategic investment or a program like this that doesn't turn out a bunch of people who are very happy and enthusiastic about the success of the program that's funding them. That's not hard to do.

But I would—I'd welcome if you would provide for the record the benchmarks, how we know they're working, what you're doing as to oversight, what standards you expect them to meet, and how are you judging the effectiveness.

BUSINESS SYSTEMS MODERNIZATION

Let me go back to one question that I am very much concerned about, which as I said, I raised with the Commissioner of the IRS; namely, the Business Systems Modernization. Two billion dollars going down a rat hole may be a little harsh, but almost every procurement activity is behind schedule, over budget, and when the contractor delivers software, we have been told it does not meet performance requirements.

Since you've come from the private sector, Mr. Secretary, would you have spent $2 billion on the program? Do you believe the improvements are worth the money? And if you were directly in charge, would you consider pulling the plug, or what criteria would you establish to make sure it works?

Secretary SNOW. Mr. Chairman, like so many other large information systems projects, this one was probably overly grandiose at the beginning, promised too much and tried to do too much. I think the requirements were not adequately defined. They were poorly defined. I think the IRS was trying to do too much too fast, and the results show.

Commissioner Everson is taking, I think, a very enlightened, intelligent, thoughtful view, let's try and set forth to targets for the BSM that are achievable, let's not overreach. And he and the very able CIO there, Todd Grams, are getting good results. I think last year was probably the best year ever in the history of the BSM initiative. I know that Commissioner Everson takes a direct personal interest in it. He knows that the story there is not a good one and that there's a lot of recouping to be done.

But the updates of the Customer Account Data Engine are really showing good results. They've taken me through that. I'm very pleased. A long way to go, we can't declare victory. But I think sizing it better, having a better sense of requirements and milestones with a smaller budget actually is producing better results than the very large budget that formerly was standard operating practice.

Senator BOND. Mr. Secretary, I had suggested to OMB Director Bolten that with some $60 billion going out to IT programs that I think OMB should have, in the past and certainly now, a real talent pool with high-class capabilities to make sure that we don't continue to run into the IT problems which we see throughout the government; problems we see at every agency and in every IT solicitation. Consequently, I believe we need a professional and expert IT solicitation panel that can ensure Federal agencies can adequately address their IT needs.

With that, again, I apologize, I have to go to the floor, and I will now turn the hearing over to Senator Murray. Senator. Thank you, Mr. Secretary.

Secretary SNOW. Thank you, Mr. Chairman.

HR CONNECT

Senator MURRAY [presiding]. Thank you, Mr. Chairman. Mr. Secretary, in my opening statement I talked about the concern I had about the continuing reports we are getting regarding mismanaged and costly procurements at your Department, and I want to talk about one of them this morning in the hope that you'll tell us that the agency is implementing some lasting and effective improvements.

Five years ago, the Treasury Department decided to expand IRS's effort to develop a new common human resource information system to all of Treasury's offices and bureaus. It's known as HR Connect, and it's gotten excessively expensive and it is not delivering on its original goals.

Can you tell us why a similar human resources system at the Coast Guard and the Ag Department cost $24 million and $15 million respectively, but HR Connect is costing you $173 million?

Secretary SNOW. I'd want to talk to the people who were directly responsible for it to get a better feel for those numbers. HR Connect is, I understand, currently in operation. And—well, I would say it differently—it's in the operations and maintenance phase of its life cycle, and major systems development has been completed. The initiative though is far from complete in its totality, and the final steps of transition from development to operations and maintenance are expected to be completed for fiscal year 2006. And it's something that I'll have to look into to get you a more complete answer and I'll do that.

[The information follows:]

Appendix V

Management's Response to the Draft Report

RECEIVED
JAN 18 2005

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220
JAN 18 2005

MEMORANDUM FOR GORDON C. MILBURN III
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

FROM: Ira L. Hobbs
Chief Information Officer

SUBJECT: Draft TIGTA Report: The Department of the Treasury's HR Connect Human Resources System Was Not Effectively Implemented, dated December 3, 2004 (Audit #2003-10-022)

Thank you for the opportunity to review the draft audit report. We appreciate the discussion of an earlier version and acknowledge the changes you made concerning our comments. With the realignment of the HR Connect program to the Office of the Chief Information Officer (OCIO) in September 2004, we have now completed the transfer of all program responsibilities, including continued audit follow up. Effective with this response, the OCIO will handle all TIGTA inquires on HR Connect. It is our intent to use this report to enhance HR Connect program performance going forward and to strengthen oversight. Attached please find our response to your recommendations, and to the outcome measures that are addressed in the final four bullets beginning on page 2. Also, we identified no materials that require FOIA protection.

We would like you to be aware that:

- Despite the challenges of designing and implementing this large and complex program over a period of years, HR Connect is now successfully deployed throughout Treasury in eleven bureaus currently using the National Finance Center (NFC) for payroll services. HR Connect delivered 26 broad functions and is widely used in a self-service delivery mode by managers and employees throughout Treasury and by components of the Departments of Homeland Security and Justice. HR Connect is also being deployed at the Department of Housing and Urban Development. Through mid-September 2004, over 1.8 million tasks have been completed in HR Connect.
- Treasury rigorously reviewed the basis for its actual and estimated costs and benefits to improve the reliability of its assumptions, financial and metric data that established a solid foundation for enhanced program management, with the FY2006 Exhibit 300 submission to OMB. That submission also documented the incorporation of CareerConnector (which became operational in FY2004) into the HR Connect suite of services. We have taken steps to improve program oversight. With the realignment of the HR Connect program under the OCIO, we continued the governance structure that includes bureau and customer participation at the executive level (to recommend strategic direction and enhancements) and added an Executive Steering Committee, with membership composed of the Treasury's Chief Human Capital Officer (CHCO), the Deputy CHCO, the Chief Information Officer (CIO), and Associate CIO - HR Connect, with decision authority, to guide the program through its operations and maintenance phase of the life-cycle.

The Department of the Treasury's HR Connect Human Resources System Was Not Effectively Implemented

Specifically, our comments to the audit findings are as follows:

- The identification of factors that extended the IRS deployment accurately pinpoints several that were outside the control of the program office, such as filing season priorities. As of May 2004, all IRS employee records and transactions were being processed through HR Connect; thus completing IRS implementation.
- The comparison of different PeopleSoft implementations across government as a measure of effective management assumes similarity. However, the report does not account for differences in scope, methodology, and business requirements. The comparative data does not explain what is included in the costs of these implementations, making a comparison to HR Connect costs inconclusive, other than to say the latter took longer and cost more.
- IRS officials confirm that their HR Connect Working Capital Fund payments, from FY 2003 to present, included over $3 million for CareerConnector. The HR Connect Program Office also funded $1.2 million for CareerConnector to host support and system integration/data feeds. The full recruitment solution was provided by coupling the requisition capability, competencies, and announcement criteria already operational in HR Connect with the best features of CareerConnector (e.g., on-line rating and ranking). The agreement between Treasury and IRS to integrate CareerConnector into the HR Connect suite of services as a component of HR Connect recruitment functionality was effective for FY2003, although CareerConnector was not operational for use by any Treasury bureau until November 2003, when IRS began its pilot.
- We disagree that the projected productivity savings of $454 million were unsubstantiated. Each year, as part of the Exhibit 300 submission, the IRS provides the HR Connect Program Office with FTE savings actually achieved and those estimated. The IRS Human Capital Office and Agency-Wide Shared Services confirm the anticipated FTE savings previously identified as being attributable to efficiencies gained by implementing HR Connect/Career Connector remain accurate. Savings at the IRS occurred in increments beginning in FY 2004 and are projected to reach the end-state level of 743 FTE by the end of FY 2006. As the incremental savings occur each year they are applied against critical IRS funding shortfalls during that fiscal year and/or are reinvested to mission critical programs via the budget process. IRS identifies and pools Service-wide savings, prioritizes needs, and redirects the savings for unfunded costs (e.g., pay raise) and high-priority programs.
- We have reevaluated and improved HR Connect documentation that reflects the benefits attributable to program implementation. However, we disagree that $150 million in "other savings" (i.e., time freed up by using HR Connect to perform self-service actions) is unsubstantiated. We used sophisticated commercial software that compares pre-HR Connect process steps and data assumptions provided by the bureaus, with those created by the HR Connect system. This software calculates potential savings that could be realized by full HR Connect utilization. A report documenting the results of this analysis was provided to each bureau.
- IRS officials disagree that $21million spent on the Integrated Personnel System (IPS) was wasted. IPS documentation was used to jump-start the HR Connect deployment at IRS; that included the IPS Fit Gap analysis; IPS Master Project Plan, Transition to Support Plan, Communications Plan, and readiness checklists. Also, transfer of highly specialized IRS and PeopleSoft knowledge occurred with the reassignment of five IPS team members to the IRS HR Connect team.

The Department of the Treasury's HR Connect Human Resources System Was Not Effectively Implemented

- We disagree that the $20 million expended on two contracts by the Program Office was wasted. By 1999 a personnel processing system was produced and an NFC interface was operational for the Office of the Comptroller of the Currency and the Bureau of Alcohol Tobacco and Firearms. Recognizing the potential for improvements, the Program Office adopted the recommendation of an independent consultant to cancel the contracts to improve business efficiencies.

If you have questions, please contact me on (202) 622-0021 or members of your staff can contact Lynn Eddy, Associate CIO – HR Connect, on (202) 622-1520. For questions concerning audit follow-up, please contact Jose Villar on (202) 622-6141.

Attachment

cc: Acting Assistant Secretary for Management, Department of the Treasury

Deputy Commissioner, Support Services Internal Revenue Service

Senator MURRAY. I would like to know, the Inspector General reported recently that the IRS let the contractor for this system make decisions that the agency itself should have been making. The IG said that the IRS's oversight of this program has been weak to non-existent. In fact, when the Appropriations Committee noted the cost growth and asked for a report on the program, the IRS even let the contractor prepare that report for this committee. These problems are fairly similar to what we've seen with the IRS business system modernization.

Can you share with this committee, is the Treasury Department and IRS incapable of conducting routine management and oversight of programs like these?

Secretary SNOW. Oh, I don't think so. I think that would overstate the case. From my experience in private life, difficulties with new information systems are not unknown to the best-run organizations. And I'll look forward to talking with the HR people and with the IG's office to get a better sense of this situation so I can talk to you more.

Senator MURRAY. Are there any measures being implemented across the Department to improve management and contract execution that you can share with us?

Secretary SNOW. Well, yes, we talked about some of the major ones already, the BSM at the IRS is the biggest, most far-reaching. And I think because of the focus that's been brought to bear on it, we're seeing real results. We're seeing that setting up understandable requirements with reachable sorts of targets and goals with people directly accountable with milestones is producing results. That's the model that always produces results in the information systems arena, and it's the one we're going to be taking throughout the Department.

TBARR PROJECT

Senator MURRAY. Okay. Well, let me ask you about one other area, and that's the Treasury Department's modernization of its building. Since 1996, we've been doing this through a program called TBARR. After $237 million in appropriated funds and significant senior leadership turnover, the main Treasury building project still has not been completed and the Treasury Annex hasn't even been touched.

The Treasury Inspector General noted that the direct involvement of the Deputy Secretary at one point in the building modernization helped improve the project, but now the Deputy Secretary has left, the acting Assistant Secretary for Management, who's been involved in this project has left, and so have quite a few other senior Treasury officials.

With the record of mismanagement with this program and all the vacancies, how can we be assured that the remaining funds we're asking for this year, which is $10 million, will be managed properly?

Secretary SNOW. Well, the Deputy Secretary, of course, is now the Secretary of the Energy Department, so he's still part of the administration, somebody I——

Senator MURRAY. But he doesn't have direct oversight of this program.

Secretary SNOW [continuing]. See regularly. And we've appointed a very able, very competent Acting Deputy Secretary to continue to oversee this initiative. We have in the pipeline, I hope receiving approval very shortly, a new Assistant Secretary for Management, who knows this is a priority to be overseen. And all I can do is tell you that we are committed to getting this project done with the $10 million that we've requested.

Senator MURRAY. Well, am I correct that fiscal year 2006 is the final year you're going to be requesting funds for TBARR, even though there's been no work done yet on the Treasury Annex?

Secretary SNOW. Yeah. The focus here is on the main building, the main Treasury building, which really is a treasure. But as with all buildings that go back a century plus, it's got to be modernized and updated, and that's costly. But it's an appropriate investment in the Treasury building which I think is the third oldest building in continuous operation. Abraham Lincoln once walked the halls. It's historic and we need to preserve its historic role in our country's history.

Senator MURRAY. Do you anticipate requesting any funding for repair of the Treasury Annex through the TBARR program, or actually through any other program?

Secretary SNOW. Well, we're going to need to have some work done on the Annex. Some work has been done, some safety work, some work on the elevators, and some of the things that are directly related to the safety of the people in the building. I think we will now need to have a maintenance budget at the Department, a regular funded maintenance budget. And one of the things in the past we haven't had was a maintenance budget, and of course if you don't maintain these great old buildings, they deteriorate on you, and then the cost is even greater.

Senator MURRAY. Senator Dorgan has another question. We'll have one final one when he is through.

TRADE DEFICIT

Senator DORGAN. Mr. Secretary, again thank you for being with us today and answering questions. I know that you came to our State recently, and we're always honored when a Cabinet official visits North Dakota. You were there to talk about Social Security, and I suspect, although I was not able to be there because we had votes that day, I expect that you agree with President Bush that there is a "crisis" of sorts in Social Security. I've observed previously that Social Security, according to the Social Security actuaries and the CBO, somewhere between those two, Social Security will remain fully solvent until President Bush is 106 years old. That is not a crisis, although I admit that perhaps we'll need some adjustments along the way, not major surgery.

But I think there is a crisis, and I think there's a crisis in international trade. Our trade deficit is a dramatic deficit. We're choking on trade debt. The China debt was up 30 percent last year to $162 billion with that one country alone. Tell me, how do you assess our trade situation? Is this debt serious? Troublesome? Do you think our trade policies are working?

Secretary SNOW. Senator, thanks, I had a good visit to Bismarck, and Bismarck High is a great school. So is the University of Mary that we visited.

The issue of Social Security and the crisis, that's semantics. It's a problem that needs to be addressed, and I'll leave others to put the adjective on it.

The trade deficit is also serious, and it's something we are trying to address. A large part of the trade deficit grows out of the fact that the United States is growing faster, higher GDP growth, and creating more disposable income than our trading partners, our major trading partners, Japan, the Euro zone, and so on. Thus, we are buying more from them than they are buying from us. We also have a lower propensity to save, higher propensity to consume, and some of that shows us in our appetite for their goods.

It's important for our trading partners to grow faster. It's one of the messages we try and take to them. You know, you may not be able to grow as fast as we would, because your population is growing more slowly—but your productivity can be as high, and if you have better growth policies, we'll narrow the trade gap.

Senator DORGAN. Mr. Secretary, though, isn't that a position that on its face is wrong with respect to China? China's growing much more rapidly than we are. Their economy is—has a very rapid rate of growth, and yet our trade deficit with China is growing dramatically. So on its face, isn't that argument—isn't that an argument that doesn't hold water with respect to China?

Secretary SNOW. Well, it's an argument that holds water with Japan and Germany and France and Italy and Spain and all of our major trading partners. Now, clearly China is growing very fast, 8, 9 percent. But our exports to China are growing at a double-digit rate as well. So we need to keep pressing China to open up more and deal with issues like intellectual property rights and the thievery of our ideas.

But I know China's going to continue to grow, I think, at a pretty good clip. But our exports are also there growing at a good clip. They should grow faster.

Senator DORGAN. But our imports are growing more rapidly. That's why the trade deficit increases. I mean, if you just look at one side and portray that as positive when in fact the other side is growing much more rapidly. My point is that the basic argument, I've heard you make it before, and I think it's the administration's position, our trade policies are working, and the only problem is our trading partners aren't growing fast enough, just take a look at China. China's growing much more rapidly than we are, and so is our trade deficit with China. I just think that undercuts the debate here about that.

My own sense about China is that you're right about counterfeiting and piracy, but the fact is that China wants us to be a sponge for all their trinkets and trousers and shirts and shoes and all the things they produce including high-tech, and yet they don't want to open their market to us and we sit around without the will, the nerve, or the backbone to say this is nonsense, we're not going to put up with this anymore.

This is in many ways about enforcement, it's about good trade agreements. I want to just ask you about this, because it's—if you are reading about China, the country with whom we have the largest growing trade deficit, an alarming trade deficit, they are now ratcheting up an automobile export industry. They're very quickly putting together an automobile industry and they're anxious to have an automobile export industry. And in fact one of our major car companies is suing China for stealing the blueprints for a car that they're now producing.

In our bilateral agreement with China, not done by this administration, done by the previous administration, but then all trade negotiators have the same mind set. They want to get into a room and reach an agreement as quickly as they can, notwithstanding what the agreement is. In our bilateral agreement, we agreed with China that on bilateral with respect to automobiles, they could impose a 25 percent tariff on U.S. cars that go to China and we would impose a 2.5 percent tariff on Chinese cars that come here.

So with a country with whom we had a huge deficit we agreed that they could impose a tariff that is 10 times larger in bilateral automobile trade. That's not only incompetent, that's just nuts. And yet, we now watch the Chinese gear up for an automobile export trade after we have this fundamentally unsound trade agreement with them. I mean, what do you make of that?

Secretary SNOW. Well, Senator, I'm not at all happy with the situation. Trade's got to be a two-way street as you're suggesting, and the Chinese need to accelerate their commitments to WTO, they need to move to a flexible currency, they need to open up their markets, they need to enforce the piracy laws and the counterfeiting laws and stop stealing our intellectual property. There's a lot to be fixed there, a lot to be fixed, and probably including going back and looking at some prior agreements.

Senator DORGAN. Madam Chair, one more point if I might, and then I'll conclude. You know that much of our trade issue with China's foreign policy, in fact, the interagency task force recommended that we take action against China based on wheat trade, and the answer was, no, that would be a too much of an in-your-face thing to do. So this is all soft-headed foreign policy.

But I think that it's important for our country to recognize our trade deficit is a crisis, it is a genuine crisis, No. 1. No. 2, I think a little backbone would be good for us. I think, you know, if we told the Chinese, you know you have all these goods you want to sell, why don't you try selling them in Zambia for the next year and see what kind of market you have, because we are a cash cow for the China hard currency needs at the moment given our trade deficit. And the fact is China needs this trade relation. If—we just need to have some backbone to say to the Chinese, we're going to take action if you don't own up to your responsibilities.

Well, Mr. Secretary, you and I will have further discussions about this. I would like to send you my—on the tax haven issue, with respect to treating them as if they never left, I would like to send you that bill and ask for the comments of the Treasury Department.

Secretary SNOW. I'd be delighted, Senator, and I look forward to talking to you about it.

Senator DORGAN. Thank you.

BONNEVILLE POWER ADMINISTRATION

Senator MURRAY. Thank you very much. Mr. Secretary, I just have one other issue, and that is, last week Director Bolten was here with us, and I asked him about borrowing authority for the Bonneville Power Administration, and I'm curious as to your views on this issue.

In your administration's budget, you have proposed to hold certain financial transactions like third-party financing against BPA's borrowing authority. As I told Director Bolten last week, this proposal is rich in irony because it contradicts the President's own fiscal year 2003 budget. For 2 years the administration opposed the Northwest delegation's effort to raise BPA's borrowing authority by $1.4 billion. In the 2003 budget, the President finally called for increasing this borrowing authority by $700 million, or actually half of what was needed.

But the budget also said that BPA should use other financing means like third-party financing to meet the remainder of its investments' needs. Yet here we are again 2 years later and your administration proposed to undercut the ability of BPA to use third-party financing by holding these and other types of transactions against their Treasury borrowing authority limit.

Last week Director Bolten said he'd get back to me on this, and I expect you'll have to do the same. But I would recommend that before the administration proposes legislative language like this, we ought to have a common understanding on whose debt this is.

And I just wanted to ask you, do you believe BPA's investments using third-party financing are liabilities of the U.S. Treasury or are they liabilities of the Northwest rate payers?

Secretary SNOW. Senator, I really would have to look into that, because I don't know enough about it to offer a thoughtful opinion, and I'd be reluctant without more knowledge to answer——

Senator MURRAY. Well, this is a——

Secretary SNOW [continuing]. Such a complicated question. But I will look into it and I will——

Senator MURRAY. This is a critical question for us. And believe me, rate payers in the State of Washington have really been hit from Enron on, and the answer to this question is absolutely critical. So I would like a response back as soon as possible from you.

Secretary SNOW. I will commit to do that.

[The information follows:]

BONNEVILLE POWER ADMINISTRATION (BPA)

The administration has encouraged BPA to seek private sector participation and joint financing of its transmission system upgrades and other capital investments that are structured to ensure that the financial risks of these investments are jointly shared by BPA and the private sector participants involved. When financial transactions are structured in this way, any resulting BPA obligation should not be counted against BPA's $4.45 billion statutory limit on the aggregate amount of debt that BPA has outstanding at any one time (BPA debt limit). For this reason, the administration's proposal excludes from the BPA debt limit third-party financings in which the private sector bears real financial risk, such as operating leases.

In contrast, the 30-year capital lease transaction that BPA entered into in 2004 is an example of a transaction involving debt that should be counted against the BPA debt limit. Under this transaction, a third party issued bonds backed solely by lease revenues required to be paid by BPA and used the proceeds to finance the cost of BPA's acquiring, constructing or equipping certain new transmission assets.

While the third party holds title to the assets, BPA has exclusive use and control of the assets during the 30-year lease period and, at the end of this period, BPA has the option to acquire the assets at minimal additional cost. The third party that issued the bonds has not borne any real financial risk. BPA's obligation to make lease payments under the capital lease is unconditional and not terminable unless BPA makes arrangements for the bonds to be repaid in full. Since repayment of the bonds depends wholly on BPA's making its guaranteed lease payments, the bonds are, in substance, a form of BPA debt which should be subject to the BPA debt limit. Under the administration's proposal, such debt would be subject to the limit.

Despite the apparent perception of market participants that debt issued under the 2004 BPA third-party lease transaction is implicitly guaranteed by the United States, and the fact that BPA is a wholly-Federal entity in the Department of Energy, this debt is not backed by the U.S. taxpayer. As a matter of sound budgetary and financial practice, the administration supports having statutory limits on Federal agencies' debt regardless of whether or not the debt is backed by the U.S. taxpayer. A central purpose of BPA's debt cap is not just to limit its liability to taxpayers, but also to regulate and limit its financial risk exposure for its ratepayers. An effective BPA debt limit, one that applies to all forms of BPA debt, will make BPA's financial condition more transparent to its ratepayers and other stakeholders and serve as an important financial control device.

ADDITIONAL COMMITTEE QUESTIONS

Senator MURRAY. Members of the subcommittee who have additional questions will submit them for your response, and they will also be included for the record.

[The following questions were not asked at the hearing, but were submitted to the Department for response subsequent to the hearing:]

QUESTIONS SUBMITTED BY SENATOR PATTY MURRAY

MISMANAGEMENT OF IRS EMPLOYEE TUITION ASSISTANCE PROGRAM

Question. Several years ago, the IRS established a tuition assistance program to help employees improve their accounting and information technology skills. This program was also supposed to improve training at taxpayer assistance centers since these centers have not had a good record at providing taxpayers with accurate guidance. To date, it appears that more than 60 percent of the funding for this program—some $7.2 million—has been used for overhead while only the remaining $2.8 million has gone toward true tuition assistance. This problem has persisted while nearly half of the employees eligible for the assistance have been denied by the agency.

Given the fact that your Department has told us that they are trying to enhance the skills of the IRS workforce, how is it that no one at IRS knew that this program was failing so badly?

What is being done to rectify the problem now?

Your agency has periodically justified efforts to push Federal jobs over to the private sector on the grounds that private employees might be better trained.

Given the way your Department has mismanaged these efforts to train your own employees, aren't the employees justified in complaining about your efforts to send their jobs to private contractors?

Answer. Since 2000, when the Human Resources Investment Fund (HRIF) was funded and developed jointly with the National Treasury Employees Union (NTEU), the IRS has spent $499 million on employee training. This included tens of millions of dollars spent on technical training for employees in the taxpayer assistance centers and call centers. The HRIF was not directed at funding this technical training. Indeed, training for skills needed in current occupations is not funded from the HRIF but from the operating budget of the IRS business units.

The amount available for HRIF tuition funding is set at no more than 2 percent of the overall training budget. Administrative costs are not paid from this allocation, but from general management programs. Even though the overhead associated with the HRIF did not reduce the amount available to employees for tuition assistance, we are currently analyzing the program to determine how to most effectively reduce the administrative costs.

MISMANAGEMENT OF TREASURY COMMUNICATIONS ENTERPRISE CONTRACT

Question. The Treasury Department let a contract for a new secure communications network to AT&T about 4 months ago and the contractor began work. I'm told, however, that the remaining project bidders protested the contract award, which GAO subsequently sustained. Apparently, the bidders protested successfully because your Department apparently did not give each of them all of the relevant bid data at the same time.

Mr. Secretary, why was there never a line item in the budget for this initiative? Doesn't an initiative of this size and importance merit some discussion in your budget documents?

Please explain to me what happened with this attempt to purchase a new communications system and who you are holding responsible for this botched procurement?

Answer. There is no line item in the budget because this initiative represents a service that is funded out of the Treasury Working Capital Fund (WCF). The WCF, funded by contributions from Bureaus, provides common administrative services for the Department. The intent of the Treasury Communications Enterprise (TCE) contract was to replace the expiring Treasury Communications System (TCS) contract, which is currently funded through WCF. The scope of these services focus on providing enterprise wide area network data communications services to Treasury Bureaus and Offices.

Treasury and GSA entered into a Memorandum of Understanding (MOU) on December 2, 2004 which stated that Treasury would evaluate the GSA's Networx services 3 years after the award of TCE. The losing bidders argued that this MOU materially altered the basis under which option years would be awarded. Treasury did not intend nor did it believe the MOU impacted the procurement as the Department fully intended to fulfill the option years of the TCE contract provided it represented the best value for the government. Consistent with effective IT management and procurement principles, the goal was to evaluate the TCE contract and determine the most cost-effective long term strategy which we did accomplish.

Question. Secretary Snow, I was pleased to read in your testimony that you recognize the important role of the Community Development and Financial Institutions (CDFI) Fund.

The President's Budget justification for the CDFI Fund states that, "Historically, for every dollar in investments provided by the CDFI Fund, awardees have been able to leverage these grants with over $20 in matching funds." That is an incredible amount of funds flowing into these economically distressed areas, especially considering the small Federal investment.

I was disappointed to see that the President's Budget for fiscal year 2006 calls for almost all CDFI funding to be sent to Commerce and combined with other community development programs, which will then be reduced by approximately a third.

Under the President's smaller substitute grant program, would all current CDFI programs still be eligible?

Answer. Although the manner in which the CDFI Fund accomplishes its mission is unique—through building the capacity of these lenders to provide improved access to financial services—the underlying objective is not unlike any of the other consolidated programs from the various cabinet agencies proposed to be consolidated at the Department of Commerce, which holds a primary mission of economic opportunity. Commerce has shown great skill in managing its programs and in greatly leveraging private sector investment. As currently envisioned, nothing would preclude the CDFI industry from being eligible sub-recipients of "Strengthening America's Communities" grant funds from communities and States that receive funding.

Under the Strengthening America's Communities Initiative the Treasury Department would focus on its fiscal year 2005 New Markets Tax Credit Program which will award $780 million of tax credits using $2 billion of its investment authority ($0.39 of each investment dollar), which is roughly 20 times larger than the CDFI Programs ($40 million in fiscal year 2005) proposed for consolidation to the Department of Commerce.

Question. How will you be able to ensure that the new smaller substitute grant program would be able to continue to leverage over $20 for every Federal dollar?

Answer. These types of details will be determined in close collaboration with Congress and stakeholder groups as the administration creates legislation for the initiative, which will be submitted to Congress.

The accountability measures and other requirements will reflect the administration's belief that local flexibility is more effective than Federal control. The administration will set accountability measures for the use of taxpayer dollars, requiring communities to show that they have made progress toward locally selected goals for development (such as job creation, homeownership, commercial development, improving blighted or abandoned properties, and increasing the number of businesses in their area) in return for being able to determine locally how best to spend Federal dollars to meet those outcomes.

As noted in the previous question, under the Strengthening America's Communities Initiative the Treasury Department would focus on its fiscal year 2005 New Markets Tax Credit Program which will award $780 million of tax credits using $2 billion of its investment authority ($0.39 of each investment dollar), which is roughly 20 times larger than the CDFI Programs ($40 million in fiscal year 2005) proposed for consolidation to the Department of Commerce.

Question. We understand that the staff that has the expertise in this area will not be transferred to the Department of Commerce.

What expertise does the Department of Commerce have in creating and supporting financial institutions that can provide access to affordable credit to distressed low-income minority communities that are not served by traditional banks?

Answer. The engine of economic and community development is economic opportunity, ownership and job growth. Because the focus of this initiative is on economic development, creating local job opportunities, and helping communities transition to self-sustaining economies, the Commerce Department's mission (job creation, economic development, and opportunity) is more consistent with those goals.

The Fiscal Year 2006 Budget provides funding for salaries and other administrative costs to close out grants from previous years. The administration will continue to address these questions as it develops its legislative proposal, which will be submitted to Congress in the coming months. It will provide the necessary authorities to transition the programs and ensure the necessary administrative resources to support their activities. The President's fiscal year 2006 budget provides the Department of Commerce with adequate funding to start up the new program in 2006.

Question. Currently, the CDFI Fund works directly with financial institutions, giving resources to institutions that would then provide the much needed financial services to these low-income communities. However, under the President's proposal, the money would go out to States and local entities, and then to financial institutions.

Won't this make the process less streamlined and merely add one more layer of bureaucracy, contrary to the President's justification for this consolidation effort?

Answer. Currently, seven Federal agencies administer 35 different grant, loan, and tax incentive programs for economic and community development efforts. The current system forces communities in need to navigate a maze of departments and programs in order access economic and community development assistance, each imposing a separate set of standards and reporting requirements.

In addition, some programs duplicate and overlap one another, and some have inconsistent criteria for eligibility and little accountability for how funds are spent. In fact, the Office of Management and Budget, through the PART analysis, has determined that many of these programs cannot sufficiently demonstrate that they make or contribute to a measurable improvement in economic and community wellbeing.

FINCEN HAS NO PENALTY FOR REGULATORS THAT DON'T COMPLY

Question. The Financial Crimes Enforcement Network (FinCEN) created a new office of compliance in response to fundamental weaknesses in the Treasury Department's system for compliance examination with the Bank Secrecy Act. FinCEN has set forth procedures for the exchange of Bank Secrecy Act information with its five Federal banking agencies, but as part of the memorandum of understanding with those entities, FinCEN did not include any penalty for noncompliance. And in the future, FinCEN expects to enter into even more such arrangements with other Federal regulatory agencies and State entities.

So, if FinCEN has no recourse with agencies that don't comply with the exchange of Bank Secrecy Act information, then how will the regulatory agencies seriously undertake this effort?

Answer. Following a series of Congressional hearings in the wake of the enforcement action against Riggs National Bank, N.A., FinCEN took a number of steps to enhance its ability to oversee and support the Bank Secrecy Act examination function being carried out by Federal agencies to which the Secretary of the Treasury has delegated Bank Secrecy Act examination authority. FinCEN created a new Office of Compliance within its Regulatory Division devoted exclusively to overseeing and supporting the examination regime. In addition, FinCEN has allocated a significant portion of its analytical resources to supporting examination-related review and analysis. Central to FinCEN's plan of stepping up its efforts relating to examination oversight and support is to ensure that, for the first time, FinCEN has sufficient information to assess how well its delegated examiners are functioning and evaluate and act on their findings. The Memorandum of Understanding executed with the Federal banking agencies last fall creates the necessary framework to ensure the flow of information to FinCEN.

The Memorandum of Understanding ensures the production of the following categories of information to FinCEN—(1) information on the methods and structure of the examination function with each agency; (2) aggregate information on a quarterly basis concerning examination findings; and (3) the identification and production of supporting factual material on specific financial institutions with significant compliance deficiencies. For its part, FinCEN agrees to provide analytical support—in the form of reports on compliance issues generally and information concerning issues specific to individual institutions—to the banking agencies; coordination on all matters related to compliance and enforcement; and periodic reports on information provided.

Since last fall, FinCEN has executed a similar agreement with the Internal Revenue Service, and is currently negotiating similar agreements with the Securities and Exchange Commission and the Commodity Futures Trading Commission. Significantly, as of June 8, 2005, FinCEN has executed information sharing agreements with over 30 States and territories. These agreements, modeled after the agreement with the Federal banking agencies, will for the first time create a close relationship between FinCEN and those States examining banks or other financial institutions for compliance with the Bank Secrecy Act. This will substantially enhance FinCEN's ability to maintain consistency in the application of the Bank Secrecy Act, leverage examination resources, and ultimately ensure greater compliance.

While none of the information sharing agreements that FinCEN has executed contain "penalty clauses," FinCEN and the Department of the Treasury have ample ability to ensure that all signatories comply with the letter and spirit of the agreement. First, and most importantly, we have reached an unprecedented level of cooperation with the banking agencies. All involved realize the importance of working together to ensure better compliance across all regulated entities. To have sought a penalty provision within the agreement would quite simply have undermined our overarching purpose, namely, to cement a new and robust level of cooperation. Second, we do not believe that a penalty provision is necessary to ensure compliance with the agreement. Indeed, the concept of a monetary penalty for non-compliance is inconsistent with an intra-governmental information sharing arrangement. We believe that "non-compliance," to the extent it occurs, will be in the form of reasonable disagreements over the scope of the agreement rather than a refusal to honor clear terms. In the event of non-performance, however, in the first instance, FinCEN has considerable power to encourage compliance through our comparison of one agency against the others. If that proves ineffective, we will elevate the issue to the Department of the Treasury. The Secretary of the Treasury is responsible for the administration of the Bank Secrecy Act. Failure of an agency to comply with the terms of the information sharing agreement could result in action at the highest level of Treasury to ensure that any deficiencies are cured.

FinCEN is in the process of fundamentally redefining our relationship with the delegated examiners. Thanks in large part to the interest and support of the Congress; we have been able to make significant strides in this regard. Going forward, while we know that there will be issues, we expect to be in a position to resolve them, with Congress and others keeping a close eye on our progress. Our collective goal is to better ensure the protection of the U.S. financial system through the application of the Bank Secrecy Act. This will continue to demand that we work closely with all those involved, including the industry and law enforcement, to ensure that our regulations are reasonable and applied consistently.

LACK OF SECURITY OF INFORMATION AT TREASURY

Question. Among the many problems your agency has with its information systems, one of the most troubling is the opportunity for agency employees, contractors, and law enforcement personnel to have unauthorized access to secret information.

In addition to maintaining its own sensitive financial and tax information, IRS also maintains a significant amount of sensitive information for the Treasury Department relative to the Bank Secrecy Act. The GAO, in a report dated this month, stated that despite the progress the IRS has made in correcting information security weaknesses, more than half still remain unfixed since 2002. Moreover, because no overall agency-wide information security project exists, there are no security controls in place to prevent, limit, or detect unauthorized access to Bank Secrecy Act data or taxpayer copy data. So, any IRS employee, FinCEN employee, contractor, or State and local law enforcement employee involved in this effort, could have unauthorized access to secret information.

Mr. Secretary, since many of these security weaknesses have existed since 2002, why is it taking IRS so long to correct them?

What is your plan to establish an overall agency-wide plan as GAO recommends and to fix the remaining weaknesses?

Answer. Recognizing the criticality of the security weaknesses, the IRS began an initiative in mid-2004 to analyze and fix required security activities at each of its computing centers and campuses and to support security certification and accreditation. The IRS is accomplishing this initiative using the latest processes and guidance as specified by the National Institute of Standards and Technology (NIST), and in accordance with the requirements of the Federal Information Security Management Act (FISMA).

In responding to GAO's report, the IRS developed a detailed coordinated response to the 60 GAO findings. The response matrix includes the GAO findings, the specific actions the IRS is taking to implement corrections to the weaknesses, and the dates the IRS will complete the actions. A number of weaknesses have already been corrected and the appropriate documentation to substantiate the correction is being provided.

The IRS is aggressively pursuing corrective actions to address the vulnerabilities identified in the GAO report, including correcting numerous weaknesses and implementing internal controls. The IRS is also developing a new enterprise-wide approach to security issues and is working on a plan to bring all of its systems into compliance with Federal, Treasury, and IRS policy, in addition to correcting the issues at the Detroit Computing Center (DCC). To further enhance the security process, the IRS has strengthened the role of the Designated Approving Authority (DAA) at the DCC. A DAA is a senior level official responsible for ensuring information security and mitigation of identified weaknesses. The DAA has been specifically assigned to provide a single point of authority and accountability for secure operations while ensuring the required oversight over the Center's equipment and associated systems software.

Treasury also continues to improve the Departmental Cyber Security program as a whole. Treasury Bureaus and Offices are working collaboratively to strengthen Departmental governance processes and information security policies and procedures. The Department believes that the actions taken by the IRS are very positive steps towards improving the security posture at the IRS and in addressing the concerns outlined by GAO's report.

Question. Mr. Secretary, a significant number of high-level positions are vacant at the Treasury Department—quite a few Deputy Secretary, Under Secretary and Director positions. The Deputy Secretary has left. So have the Under Secretaries for International Affairs and Domestic Finance. Five Assistant Secretaries are vacant including the position of Assistant Secretary for Management. These are positions critical to the effective management of a $12.5 billion agency and to the appropriate oversight of some of the problems I have cited this morning.

In addition to funding your Department, this subcommittee also funds the Executive Office of the White House including the Office of Personnel.

Are you confident that you are getting all the help you need in getting these vacancies filled?

Answer. Absolutely. I have an excellent, close working relationship with the White House Office of Presidential Personnel. In fact, in recent weeks we have announced a number of important nominations, including Robert Kimmitt for Deputy Secretary, Tim Adams for Under Secretary for International Affairs, Randy Quarles for Under Secretary for Domestic Finance, Phil Morrison for Assistant Secretary for Tax Policy, and Kevin Fromer for Assistant Secretary for Legislative Affairs among others. A full list of Treasury nominees awaiting confirmation appears on the following page.

The White House has been instrumental in helping us find the right people to fill these very important positions. I think you will find that we have selected an excellent group of nominees to fill the senior posts here at Treasury.

Question. Do you agree that the significant number of vacancies has an impact on the ability of your agency to fully execute its mission and appropriately manage its people and programs?

Answer. The Treasury Department is fulfilling its various missions and meeting its goals effectively. Although we have some vacancies right now, there are strong, competent individuals continuing to do the work of the Department on an acting basis, and of course, there are thousands of Treasury employees nationwide who admirably perform their duties.

Currently, there 10 Treasury nominees pending before the United States Senate. I share your view that having a strong and effective team in place is important to making the Treasury Department run as well as it possibly can. These nominees will be a great addition to our team and I look forward to working with you to help the Senate consider these nominees carefully and then to get them confirmed as quickly as possible. I would greatly appreciate any help that you could provide to make the confirmation process for these nominees a smooth one.

Nominations Awaiting Senate Confirmation and Dates of Nomination

John Dugan.—Comptroller of the Currency (2/28/05).
Tim Adams.—Under Secretary, International Affairs (4/06/05).
Bob Holland.—U.S. Executive Director, World Bank (4/25/05).
Sandy Pack.—Assistant Secretary for Management and CFO (5/16/05).
Janice Gardner.—Assistant Secretary, Intelligence and Analysis (5/16/05).
Jan Boyer.—Alternate Director, Inter-American Development Bank (5/25/05).
Randy Quarles.—Under Secretary, Domestic Finance (5/26/05).
Phil Morrison.—Assistant Secretary, Tax Policy (5/26/05).
Kevin Fromer.—Assistant Secretary, Legislative Affairs (6/06/05).
John Reich.—Director, OTS (6/06/05).
Robert Kimmitt.—Deputy Secretary (announced, but not yet transmitted to the Senate).

BUDGET PROPOSAL TO RAISE THE CAP ON ALLOWABLE SPENDING IF TREASURY'S REQUEST FOR TAX LAW ENFORCEMENT IS FULLY FUNDED

Question. Mr. Secretary, this subcommittee is going to have some very severe funding constraints because of the President's proposals to eliminate Amtrak, cut the CDBG program, and rescind billions of dollars from HUD. The budget for your agency claims to recognize the linkage between enhanced tax law enforcement and receipts to the Treasury by including a special provision that would raise the cap on allowable spending by $443 million next year if we fully fund your request to boost tax law enforcement by 7.8 percent.

What disturbs me about this proposal is that it is "all or nothing." If we raise tax law enforcement spending by an amount that is $1 less than your request, that we get no scorekeeping relief at all.

How can this proposal possibly make budgetary sense?

If you believe that funding your 7.8 percent increase will yield an extra $443 million to the Treasury, how can you argue that if we provide a 7.7 percent funding increase, the Treasury will see no additional revenue at all?

Answer. Section 404 of H. Con. Res. 95, the Concurrent Resolution on the Budget for fiscal year 2006, reads:

"INTERNAL REVENUE SERVICE TAX ENFORCEMENT.—If a bill or joint resolution is reported making appropriations for fiscal year 2006 that appropriates $6,447,000,000 for enhanced tax enforcement to address the 'Federal tax gap' for the Internal Revenue Service, and provides an additional appropriation of $446,000,000 for enhanced tax enforcement to address the 'Federal tax gap' for the Internal Revenue Service, then the allocation to the Senate Committee on Appropriations shall be increased by $446,000,000 in budget authority and outlays flowing from the budget authority for fiscal year 2006."

The requested $446 million increase for enforcement consists of two parts—the pay raise and inflationary costs needed to maintain existing levels for our enforcement programs ($181 million) and the amount that funds increased enforcement efforts ($265 million). The request represents a balanced approach to increasing taxpayer compliance and should be considered in its entirety. Funding the $181 million associated with the costs to maintain current levels is particularly important. Without this funding, the Service would be forced to absorb these costs through base program cuts.

Investment in IRS enforcement yields more than $4 in direct revenue for every $1 invested in its total budget. In fiscal year 2004, the Service brought in a record $43.1 billion in enforcement revenue—an increase of $5.5 billion from the year before, or 15 percent. Beyond the direct revenues generated by increasing audits, collection, and criminal investigations, IRS enforcement efforts have a deterrent effect on those who might be tempted to skirt their tax obligations.

QUESTIONS SUBMITTED BY SENATOR ROBERT C. BYRD

Question. What steps are you taking to make certain that China acts immediately to end its decade long manipulation of its currency?

Answer. The Bush Administration, led by the Treasury Department, has been working intensively over the past year and half to move China to a more flexible, market-based exchange rate as soon as possible. This has involved frequent, high-level consultations with senior Chinese officials. The administration has also mobilized our G–7 partners, other East Asian nations, the IMF and the Asian Development Bank to make clear that this is an issue of multilateral importance. Finally, we have had an intensive program of technical assistance aimed at overcoming the obstacles China sees to adopting a more flexible, market-based exchange rate regime. Treasury's technical cooperation program has been highly successful in helping China address shortcomings in its banking system, such as poorly performing loans, and understand how to develop and regulate a foreign exchange derivatives market, and improve banks' foreign exchange risk management practices.

The Chinese authorities in turn have undertaken a number of significant steps to prepare its financial infrastructure for a change to the currency regime and wider fluctuations in the value of its currency. China is now ready and should move on its exchange rate without delay in a manner and magnitude that is sufficiently reflective of underlying market conditions.

Treasury has taken a number of steps recently to expedite the process of China moving to adopt a more flexible, market-based currency. In early May, Secretary Snow appointed a Special Emissary on China, Olin Wethington. The appointment of Mr. Wethington, who will be responsible for direct and frequent contact with Chinese leaders and key decision-makers on issues related to exchange rates, seeks to continue and intensify a constructive dialogue with China on this extremely important matter during this critical juncture in U.S.-China economic relations. In addition, in the recent Foreign Exchange Report submitted to Congress, Treasury emphasized that China's rigid currency regime has become highly distortionary and that it poses risks to the health of the Chinese economy, such as sowing the seeds for excess liquidity creation, asset price inflation, large speculative capital flows and overinvestment. Failure to move to a more flexible regime risks economic disruption and dislocation in China and in the larger global trading system. The Treasury report concluded that if current trends continue without substantial alteration, China's policies will likely meet the technical requirements of the statute for designation in a future report. Finally, Treasury continues to pursue high-level discussions with the world's major trading nations on how best to address imbalances in the global economy and, in particular, to urge support for exchange rate flexibility, especially in emerging Asian economies, notably China.

Question. Under U.S. law, the Treasury Department is required law to issue a semi-annual report on other nations' currency manipulation by April 15 of each year. The Department has missed the deadline for this year. Why has the Department not issued the report? Will the report find, as many believe it should, that China is unfairly and manipulatively undervaluing its currency?

Answer. The spring Report to Congress on International Economic and Exchange Rate Policies was submitted on May 17, 2005. Because of the complexity of these reports, they are time-consuming to prepare. While we always strive to deliver our reports to Congress on time, delays may be unavoidable from time to time. This administration has consistently delivered these reports much more promptly than most of its predecessors.

The report found "that no major trading partner of the United States met the technical requirements for designation under the Omnibus Trade and Competitiveness Act of 1988 during the second half of 2004 . . . Treasury has consulted with the IMF management and staff, as required by the statute, and they concur with these conclusions."

The report also stated that "Treasury has engaged, and will continue to engage, with several economies, including some in Asia, to promote the adoption of market-based exchange policies and regimes. Most notable among these is China. Current Chinese policies are highly distortionary and pose a risk to China's economy, its trading partners, and global economic growth. Concerns of competitiveness with China also constrain neighboring economies in their adoption of more flexible exchange policies. If current trends continue without substantial alteration, China's policies will likely meet the statute's technical requirements for designation."

Question. Last week in testimony before the Senate Finance Committee, USTR nominee Bob Portman stated that the Treasury Department is responsible for addressing any problems arising from China's undervalued currency. Mr. Secretary, would you agree that China's manipulation of its currency raises concern about China's legal obligations before the WTO?

Answer. As Treasury noted in its recent report pursuant to the Omnibus Trade and Competitiveness Act of 1988, current Chinese exchange rate policies are highly distortionary and pose a risk to China's economy, its trading partners, and global economic growth. As Ambassador Portman indicated, Treasury remains engaged with China to encourage its adoption of more flexible exchange rate policies. We believe that our intensive engagement with the Chinese authorities is the most effective way to bring about a change in China's exchange rate policy as rapidly as possible.

Question. The Trade Act of 2002 makes both strong trade remedies and addressing the problem of WTO Panels and the WTO Appellate Body's having created obligations not agreed to by the United States in the Rules area principle negotiating objectives. A review of the documents that have been filed by the U.S. government in the current WTO Rules negotiations shows that the United States is not acting to address these critical negotiating objectives. While some preliminary papers have been presented in the Rules area, little has been done by the U.S. government to follow-up on these preliminary papers with further explanatory papers or specific proposals and/or actions necessary to redress the harm that has been suffered by the United States as a result of the WTO dispute settlement process. As part of the interagency review process, the U.S. Treasury Department reviews papers and/or proposals of the U.S. Commerce Department and other U.S. government agencies prior to their submission to the WTO in the ongoing Doha Round of international trade negotiations. Can you confirm that the U.S. Treasury Department is working, and will continue to work over the coming months, to facilitate expeditious interagency approval of U.S. proposals put forward by the U.S. Commerce Department and other U.S. trade agencies—proposals that necessarily must be submitted in the WTO Rules and other negotiations to address the core negotiating objectives that were included by Congress in the Trade Act of 2002?

Answer. The Treasury Department participates in the USTR-chaired interagency Trade Policy Staff Committee and Trade Policy Review Group, the committees charged with helping formulate U.S. trade policy positions and papers. Treasury participates based on the deadlines established by USTR. Treasury supports effective and transparent WTO rules that provide protection from unfairly traded and injurious imports and assure fair treatment by other countries for U.S. exports.

SUBCOMMITTEE RECESS

Senator MURRAY. Thank you very much. This subcommittee will stand in recess until Thursday, May 12, when we will take testimony on the President's budget request on Amtrak.

[Whereupon, at 11:11 a.m., Tuesday, April 26, the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

THURSDAY, MAY 12, 2005

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

The subcommittee met at 9:33 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Christopher S. Bond (chairman) presiding.

Present: Senators Bond, Bennett, Burns, Murray, Byrd, Kohl, Durbin, and Dorgan.

DEPARTMENT OF TRANSPORTATION

NATIONAL RAILROAD PASSENGER CORPORATION

STATEMENT OF DAVID M. LANEY, ESQ., CHAIRMAN, AMTRAK BOARD OF DIRECTORS

ACCOMPANIED BY:

DAVID GUNN, PRESIDENT, AMTRAK

JEFFREY M. ROSEN, GENERAL COUNSEL, DEPARTMENT OF TRANSPORTATION

KENNETH A. MEAD, INSPECTOR GENERAL, DEPARTMENT OF TRANSPORTATION

OPENING STATEMENT OF SENATOR CHRISTOPHER S. BOND

Senator BOND. Good morning. The Senate Appropriations Subcommittee on Transportation, Treasury, Judiciary, HUD and Related Agencies will come to order.

Today we welcome a diverse panel: Mr. David Gunn, Amtrak's President and CEO; David Laney, Amtrak's Chairman of the Board; Jeffrey Rosen, General Counsel for the Department of Transportation; and Kenneth Mead, Inspector General for the Department of Transportation.

While I understand that Mr. Gunn will not be presenting testimony but is here to answer questions, I look forward to each of your views on Amtrak's fiscal year 2006 budget. More importantly, I look forward to understanding your views on the difficulty that Amtrak is facing and the options that will dictate the future or demise of Amtrak as we know it today.

Unfortunately, the 2006 budgets presents a very bleak and dour picture for the future of Amtrak. The OMB request includes only $360 million in the Commuter Rail Operations Account, intended to facilitate Amtrak's reorganization through bankruptcy. This budget request is some $840 million less than the $1.2 billion appropriated in the current year for Amtrak operations and related needs. Under any circumstances, $360 million is not enough to meet Amtrak's needs in 2006, whatever choice Congress makes about the future of Amtrak.

As I have told you individually, and I have told the Director of the Office of Management and Budget, I think it is irresponsible to propose bankrupting Amtrak without having any significant plans for reforming it or the money either to fund the bankruptcy which would be, in our opinion, far more expensive than you have any concept here if you look at the obligations of Amtrak, or keeping it alive.

Amtrak claims it needs $1.82 billion for 2006 and it cannot survive in fiscal year 2006 even on flat funding $1.2 billion. However, even if I was to agree that $1.82 billion for Amtrak is justified, I do not see how this subcommittee will be able to provide such a significant increase when we have been given such a shortfall across our entire budget by OMB.

It is not your problem directly. It is Senator Murray's problem and mine. But it has implications which are very serious for you because we have a number of very difficult funding decisions in a tight allocation.

The overall budget for domestic discretionary funding is such that this subcommittee will have trouble reversing many of the administration's recommendations that eliminate or reduce funding for many other important and necessary programs.

OMB, for example, has eliminated funding of $51.6 million for Essential Air Service, an important and popular program that subsidizes air travel from remote rural airports, often located in areas with few transportation options. I doubt that we would be able to pass this bill on the floor of the Senate if those funds were not included.

The budget request also proposes to dismantle the CDBG program as well as 17 other programs, and put them in a block grant with the Department of Commerce and take a huge whack at them, cutting them by about $2 billion. CDBG, again not your problem, it is ours. But CDBG is critical to HUD's mission of being both a leader and partner with States and communities in the development of housing and economic growth. The program is a priority for all States and most communities, and it is also a priority for the members of this subcommittee.

Under the budget request, the subcommittee will have to find a way to also absorb a $2.5 billion rescission of excess Section 8 funds. Over the last few years, the previous committee that I had the pleasure of chairing before it was blown up, VA/HUD, made a number of reforms to the Section 8 program to make it much more efficient and to reduce the availability of excess Section 8 funds.

Having made that change, I have no idea how the administration proposes to pay for this rescission. Neither the Secretary of HUD nor the Director of OMB have any idea or any methodology for determining this rescission of where the funds will come from.

Having given you the bright news, now these are just a few of the problems facing the subcommittee and unfortunately will severely limit our ability to backfill funding for Amtrak. Believe it or not, there is a laundry list of other program cuts and shortfalls I will not bother you with, but all have strong support and deserve funding. In truth, in a time of deficit reduction, a program must not only demonstrate its value but an ability to overcome substantial program flaws.

Unfortunately, Amtrak's problems only seem to get worse. Bankruptcy will not solve it. It is too complex, the costs potentially too great, and the results too uncertain. I am not sure anyone understands the true cost, but I am from the Show Me State and I would like to see it before I count on it.

Amtrak deficits run over $1 billion a year. The Northeast corridor has had problems with Acela. Mr. Gunn, your predecessor as president, Mr. Warrington, promised Congress that Amtrak was on a glide path to profitability. He left Amtrak in worse shape than he inherited it, with Amtrak's debt increased from $1.7 billion in 1997 to $4.8 billion in 2002. At least I would trust you not to make any promises like that until we see a little better prospect.

Trouble is dogging Amtrak. As I mentioned, the Acela Express, with 20 percent of the passenger service on the Northeast corridor accounting for 11 percent of Amtrak's ticket revenues, has been shut down because of the brake problems. There has to be a reform plan. There must be structural reform. And we cannot keep Amtrak on inadequate life support without a light at the end of the tunnel. At this point, that light appears to be an oncoming freight train.

We are looking for a responsible plan and we count on the witnesses at the table today and the organizations you represent to provide it.

In fiscal year 2004, the Omnibus Appropriations Bill encouraged Amtrak to provide off-peak travel discount for veterans and current military personnel. This has been ignored. I would trust that you would take that into account and consider implementing this positive policy.

PREPARED STATEMENT

Unfortunately, I am going to have to miss the latter part of this hearing. I have a small bill on the floor that I have to deal with. But we look forward to having your full comments in the record and we will ask each of you to make 5-minute opening statements and have time for questions. I will review the record.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CHRISTOPHER S. BOND

The Senate Appropriations Subcommittee on Transportation, Treasury, the Judiciary, HUD and Related Agencies will come to order. I welcome a diverse panel of Mr. David Gunn, Amtrak's President and CEO, Mr. David Laney, Amtrak's Chairman of the Board, Mr. Jeffrey Rosen, General Counsel for the Department of Transportation, and Mr. Kenneth Mead, the Inspector General for the Department of Transportation.

While I understand that Mr. Gunn will not be presenting testimony but is here to answer questions, I look forward to each of your views on Amtrak's fiscal year 2006 budget. More importantly, I look forward to understanding each of your views on the difficulties that Amtrak is facing and the options that will dictate the future or demise of Amtrak as we know it today.

Unfortunately, the fiscal year 2006 budget presents a very bleak and dour picture for the future of Amtrak. The administration's Budget Request includes only $360 million in the Commuter Rail Operations account and that funding is intended to facilitate Amtrak's reorganization through bankruptcy. This Budget Request is some $840 million less than the $1.2 billion appropriated in fiscal year 2005 for Amtrak operations and related needs. Under any circumstance, $360 million is not enough to meet Amtrak's needs in fiscal year 2006, whatever choice Congress makes about the future of Amtrak.

On the other hand, Amtrak claims it needs $1.82 billion for fiscal year 2006 and that it cannot survive in fiscal year 2006 on flat funding of $1.2 billion. However, even if I was to agree that the $1.82 billion request for Amtrak is justified, I do not know how this subcommittee will be able to provide such a significant increase from the Budget Request.

In particular, the subcommittee has a number of very difficult funding decisions to make under what is likely to be a very tight allocation. Because of the administration's overall budget for domestic discretionary funding, this subcommittee will have trouble reversing many of the administration's recommendations that eliminate or reduce funding for many other important and necessary programs.

The administration, for example, has eliminated funding of $51.6 million for Essential Air Service, an important and popular program that subsidizes air travel from remote rural airports, often located in areas with few transportation options.

The Budget Request also proposes to dismantle the Community Development Block Grant (CDBG) program along with 17 other programs and replace these programs with a new block grant in the Department of Commerce. The administration is proposing to fund this initiative at $3.7 billion which is an overall reduction of almost $2 billion from the fiscal year 2005 levels, of which CDBG would be reduced by some $1.6 billion. CDBG is critical to HUD's mission of being both a leader and partner with States and communities in the development of housing and community development initiatives. This program is a priority for all States and most communities. CDBG also is a priority for the members of this subcommittee.

Under the Budget Request, this subcommittee will have to find a way to absorb a $2.5 billion rescission of "excess" section 8 funds. Over the last few years, the VA–HUD Appropriations Subcommittee made a number of reforms to the section 8 program to make the program more efficient as well as reduce the availability of "excess" section 8 funds. I do not know how we pay for this rescission. Neither OMB nor HUD can identify the methodology for determining this rescission or from where the funds will come.

These programs are merely illustrative of the problems facing the subcommittee and which will limit severely our ability to backfill funding for Amtrak. I could provide a laundry list of other program cuts and shortfalls within this subcommittee that are troubling and deserving of funding for fiscal year 2006—all are programs that have strong support and deserve funding. In truth, in a time of deficit reduction, a program must demonstrate not only its value but an ability to overcome any substantial program flaws and problems.

Unfortunately, Amtrak's problems only seem to get worse. I do not believe that bankruptcy will solve our Nation's problems with Amtrak. Amtrak is too complex, the costs potentially too great and the result too uncertain to trust bankruptcy as the solution. I am not sure anyone understands the true costs of bankruptcy or who will pay for them. I am from the Show-Me State and a great believer in certainty.

To be blunt, Amtrak runs deficits of over $1 billion per year. Since 2001, Amtrak's annual operating losses have exceeded $1 billion and annual cash losses have exceeded $600 million Amtrak also faces some $600 million a year in capital costs, mostly with regard to the Northeast Corridor. Amtrak also will have debt service of nearly $300 million annually for the foreseeable future. In addition, the deferral of maintenance has created a significant risk of operational failure.

And it only gets worse. Mr. Gunn, your predecessor as President, Mr. Warrington, promised the Congress that Amtrak was on a glide path to profitability. Instead, Mr. Warrington left Amtrak in worse shape than he inherited it with Amtrak's debt increased from $1.7 billion in 1997 to some $4.8 billion in 2002. I credit your integrity with making no such promises. I also acknowledge your hard work and commitment to making Amtrak work successfully. Unfortunately, it is still not enough. In fact, Amtrak does not operate any more successfully than it did in 2002, or for that matter 1992, 1982 or 1972.

Trouble seems to dog Amtrak. Just this April, Amtrak was forced to shut down its Acela Express Service because of cracked brake rotors on most, if not all, of these passenger trains. The Acela Express has been one of Amtrak's few success stories, representing some 20 percent of its passenger service on the Northeast Corridor. As I understand it, Acela trains accounted for some 11 percent of Amtrak's ticket revenues for the month of February. Leaving aside Acela's success, how is it possible that there are problems with all or almost all of the brakes on trains just put in service a few years ago? How does Amtrak recover from these losses and who is responsible? Most importantly, how indicative is this problem of larger management problems at Amtrak?

There has to be a reform plan and there has to be reform legislation. There must be fundamental structural reform if passenger rail service is going to continue in the United States. This subcommittee has too many other priority funding needs to keep Amtrak on life support without a light at the end of the tunnel. In other words, I expect action and a consensus on the future of Amtrak. Without that, you do not have my support.

Finally, a small but important issue. The fiscal year 2004 Omnibus Appropriations bill included language encouraging Amtrak to continue providing an off-peak travel discount for our veterans and current military personnel. It appears Amtrak has ignored this language and has not made this service available since December of 2003. This is the type of program that engenders goodwill and builds ridership, and I urge you to reconsider this policy.

I am likely to miss much or most of this hearing as I have responsibilities for helping to manage the highway bill on the floor. I will have a number of questions for the record. Please be assured that I will review the hearing record very carefully.

Thank you, I now turn to my ranking member, Senator Murray.

Senator BOND. Now I turn to my partner and ranking member, Senator Murray.

STATEMENT OF SENATOR PATTY MURRAY

Senator MURRAY. Thank you very much, Mr. Chairman.

Today we will take testimony on what promises to be the most challenging issue this subcommittee will face this year. Amtrak, America's national passenger railroad, served 25 million passengers last year, the highest number in any year in its history. One-point-one million of those passengers were in my home State of Washington.

Even so, there are those in the administration and in Congress who want to push Amtrak into financial collapse and push 25 million passengers onto our already overcrowded highways and runways.

The benefits provided by Amtrak, as well as costs, have been debated in Congress every year since the Federal Government established the corporation 35 years ago.

But make no mistake, this year is different. This year Amtrak's detractors smell blood. As we take each step in the Federal budget process, they have additional reason to be optimistic that this will be the year that Amtrak service finally grinds to a halt.

Up until this year, the path of Amtrak's funding during each of the years of the Bush Administration has been largely the same. The Bush Administration proposes a funding figure that would throw Amtrak into bankruptcy. The Amtrak Board of Directors requests a sizable funding increase to truly allow the railroad to invest in its infrastructure and modernize. Congress has come along each year and generally provided Amtrak just enough money to limp along but not enough to invest and improve service.

Over the life of the Bush Administration, actual appropriations for Amtrak have been about 141 percent above the levels sought by the administration. But have also remained some 30 percent below what the Amtrak board has said it needed.

But as I said, this year is different. After working hard to keep Amtrak on a starvation diet over the last 4 years, the Bush Administration is now proposing to terminate all subsidies for Amtrak. Whether it is for State-supported trains like the Cascadia service in my State or the Empire Builder that runs from Seattle to Chicago, or for the service in the Northeast corridor, the Bush Administration's request is the same—zero funding. And zero funding means zero service.

While the administration seeks $360 million for a special rail account in the Surface Transportation Board, that funding, by law, can only be used to allow certain local mass transit agencies like the Sounder Commuter Rail Service to continue to operate over Amtrak property once Amtrak has ceased all operations.

Strangely, at the same time the administration is proposing to zero out subsidies and park all Amtrak trains, Secretary Mineta is flying around the country saying the Bush Administration is supporting Amtrak—they just want reforms.

In fact, Secretary Mineta has stated publicly that the Bush Administration would support between $1.5 billion and $2 billion in funding for Amtrak per year if his reforms were enacted. For me, the fallacy that this administration might actually support funding for rail service, reformed or not, was made clear during our hearing 3 weeks ago with OMB Director Josh Bolten. I specifically asked Director Bolten if the Bush Administration would be submitting a new Amtrak budget if reforms were adopted. Not once but twice Director Bolten made it very clear to us that the committee has received the only Amtrak budget from the Bush Administration that we are going to get, zero for Amtrak.

One week after we took testimony from Director Bolten, the Congress took another act to help push Amtrak into insolvency. It adopted the conference report on the budget resolution. That budget set the cap on discretionary spending at the level consistent with the President's budget request, a budget request that assumes zero funding for Amtrak.

On March 15 and 16, during Senate debate on the budget resolution, Senators Byrd and Specter offered an amendment to bring the level of funding for Amtrak up to $1.4 billion to provide some certainty and stability to the funding process for Amtrak this year. That amendment was defeated by a vote of 52 to 46.

So today our subcommittee finds itself in the posture of having to cut and cannibalize other programs as we have never done before, only to see if we can scrape together enough funding from other programs to extend Amtrak for another 12 months. If the Senate had voted differently back in March, we might not be in this predicament.

Today, we are joined by Amtrak's Board Chairman and President, David Laney and David Gunn. Three weeks ago, Amtrak's Board finally submitted its grant request to the Appropriations Committee. While I was disappointed that this request arrived some 2 months late, it is notable that the Amtrak Board, made up entirely of Bush Administration appointees, is asking this subcommittee to provide $1.82 billion for Amtrak next year, more than a 50 percent increase over current funding.

Much of the discussion of today's hearing might focus on the asserted proposals to reform Amtrak. We have two separate comprehensive reform proposals, one from the administration and one from the Amtrak Board. While senators might want to discuss these proposals, I want to remind my colleagues that these reform proposals are the responsibility of the Senate Commerce Committee.

What this subcommittee needs to focus on is how much these reform proposals are going to cost. I think my colleagues will find as we discuss these reform packages is that neither of them, not the administration's proposal or the Amtrak Board's proposal, save money in the near term. They all require investments over the long-term that will require larger, not smaller, annual appropriations in the future.

In that regard, perhaps the most important testimony we will hear this morning is not from the Bush Administration or the Amtrak Board. The DOT Inspector General Ken Mead has been a consistent monitor of Amtrak's finances. He will testify this morning that Amtrak can no longer limp along on $1.2 billion in funding it has received in each of the last 2 years. He will testify that in order to maintain that status quo at Amtrak next year, we will need to appropriate between $1.4 billion and $1.5 billion.

Given the failure of the Byrd-Specter Amendment, finding even $1.2 billion will be extraordinarily difficult. Finding $1.4 billion or $1.5 billion will be a monumental and painful challenge. Unfortunately, the majority of the Senate voted to put us in this box. Only time will tell if we can find our way out of it.

PREPARED STATEMENT

One thing that is certain is that Amtrak's 25 million passengers will be anxiously watching to see if we can succeed.

Thank you very much, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF SENATOR PATTY MURRAY

Today, we will take testimony on what promises to be the most challenging issue this subcommittee will face this year. Amtrak, America's national passenger railroad, served 25 million passengers last year—the highest number in any year in its history. One-point-one million of those passengers were in my home State of Washington.

Even so, there are those in the administration and in Congress who want to push Amtrak into financial collapse and push 25 million passengers onto our already-crowded highways and runways. The benefits provided by Amtrak, as well as costs, have been debated in Congress every year since the Federal Government established the corporation 35 years ago. But, make no mistake, this year is different.

This year, Amtrak's detractors smell blood. As we take each step in the Federal budget process, they have additional reason to be optimistic that this will be the year that Amtrak service finally grinds to a halt. Up until this year, the path of Amtrak's funding during each of the years of the Bush Administration has been largely the same. The Bush Administration proposes a funding figure that would throw Amtrak into bankruptcy. The Amtrak Board of Directors requests a sizable funding increase to truly allow the railroad to invest in its infrastructure and modernize. Congress has come along each year and generally provided Amtrak with just enough money to limp along, but not enough to invest in improved service.

Over the life of the Bush Administration, actual appropriations for Amtrak have been about 141 percent above the levels sought by the administration. But they have also remained some 30 percent below what the Amtrak Board has said it needed.

But, as I said, this year is different. After working hard to keep Amtrak on a "starvation diet" over the last 4 years, the Bush Administration is now proposing to terminate all subsidies for Amtrak.

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I specifically asked Director Bolten if the Bush Administration would be submitting a new Amtrak budget with reforms or without them. Not once, but twice, Director Bolten made it very clear to us that the committee has received the only Amtrak budget from the Bush Administration that we are going to get—zero for Amtrak.

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So, today, our subcommittee finds itself in the posture of having to cut and cannibalize other programs—as we have never done before—only to see if we can scrape together enough funding from other programs to extend Amtrak for another 12 months. If the Senate had voted differently back in March, we might not be in this predicament.

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In that regard, perhaps the most important testimony we will hear this morning is not from the Bush Administration or the Amtrak Board. The DOT Inspector General, Ken Mead, has been a consistent monitor of Amtrak's finances. He will testify this morning that Amtrak can no longer limp along on the $1.2 billion in funding it has received in each of the last 2 years. Indeed, he will testify that in order to maintain that status quo at Amtrak next year, we will need to appropriate between $1.4 and $1.5 billion.

Given the failure of the Byrd/Specter amendment, finding even $1.2 billion will be extraordinarily difficult. Finding $1.4 or $1.5 billion will be a monumental and painful challenge.

Unfortunately, the majority of the Senate voted to put us in this box. Only time will tell if we can find our way out of it. One thing that is certain is that Amtrak's 25 million passengers will be anxiously watching to see if we succeed.

Senator BOND. Thank you, Senator Murray. Senator Burns, do you have an opening statement?

STATEMENT OF SENATOR CONRAD BURNS

Senator BURNS. Mr. Chairman, I have an opening statement and I am going to make it part of the record. I think you and the ranking member have pretty well summed up our problems over here, and we could not add too much to that, other then we all have our different little sections of the country that we like to take care of.

I think we have got a sizable mountain to climb here and I am looking forward to hearing from our witnesses today. Thank you.

[The statement follows:]

PREPARED STATEMENT OF SENATOR CONRAD BURNS

Mr. Chairman, thank you for holding this hearing today. As I am sure you know, Amtrak is an issue near and dear to my heart. It is also an issue of great importance to Montana. The Empire Builder covers a lot of ground in Northern Montana, and is a valuable link in our transportation infrastructure.

The Empire Builder is more than just a popular train for tourism. Folks use the train to seek medical services, to travel across the State when roads are covered in snow, and as an alternative to air service that isn't always easy to come by in rural Montana. Estimates indicate that the Empire Builder brings $14 million annually to Montana. Amtrak is a vital link in our infrastructure, both in Montana and across the country.

However, clearly some type of reform is needed. Those reform proposals should be guided by some basic principles. We need to invest in infrastructure. Crumbling tracks, aging equipment, and outdated technology risk Amtrak's future. We need a national system. State budgets are already incredibly tight, and a national train system can not be jeopardized by individual States that may not be able to allocate funds to rail service. Reform proposals need to be informed by a commitment to public service. While I believe that Amtrak must be financially responsible, and get its budgetary house in order, I also think that Amtrak serves an important public need that can't be easily calculated.

Amtrak is America's rail system, and I think it will probably always need some type of public support. The public is committed to passenger rail, so allocating some amount of taxpayer dollars makes sense. Those investments need to be made wisely, of course, but they do need to be made. Looking at Amtrak only in terms of the bottom line fails to account for the public value it provides.

Mr. Chairman, the Congress faces an important and difficult task this year in authorizing Amtrak funding. We will need to be creative, but I am ready to roll up my sleeves and get this done. As a member of both the authorizing and appropriations committees that oversee Amtrak, I am dedicated to preserving passenger rail. I look forward to working with you on this challenging task, and I look forward to hearing from the witnesses today.

Senator BOND. Thank you, Senator Burns. I know what a champion you have been for Amtrak and I am looking forward to learning from you, your experiences, as well as the other members of this committee.

I think on early bird, Senator Bennett was the next one here.

STATEMENT OF SENATOR ROBERT F. BENNETT

Senator BENNETT. Thank you very much, Mr. Chairman.

I will repeat now to the board of Amtrak what I have said to this committee. I have been a supporter of Amtrak since before it was born, because I was in the Nixon Administration when the idea was conceived. And it was my responsibility to convince the Congress to pass the act. And I have a very nice letter from Secretary Volpe commending me on my success in bringing that to pass.

Having said that, I repeat the refrain that I have many times before. The debate of whether we are for or against Amtrak is the wrong debate. We need passenger service in this country. We need a good passenger service in this country. And we should be prepared to pay for that passenger service in this country. But it should be in places where it makes sense. And the present nationwide grid of the Amtrak system does not make any sense.

I got into trouble the last time I said that. I got some nasty letters from people in Utah saying how can you say you want to give up Utah's service? Utah's service is wonderful and we must hang onto it. I have now gotten the exact statistics. I may have been a little off in what I said before. The total Utah ridership is less than 100 people per day. One airplane per day could take care of the entire use of Amtrak. Two buses, all right three if you get a small bus, could take care of the entire use of Amtrak.

And what are we spending to run an Amtrak train? It has a wonderful name. It is the California Zephyr. And boy, for those who love train traffic, the California Zephyr calls up all kinds of wonderful, wonderful memories and images. It goes through Salt Lake City, arrives at 3:35 in the morning, and leaves at 4:06 in the morning. I have watched the terminal for Amtrak go from an old train terminal that had great nostalgia around it, that has now been turned into a mall, to a smaller building, to a smaller building. And now it is a quonset hut that handles those less than 100 people a day who show up literally in the middle of the night.

And I wonder if it really is the best use of public funds to keep that train running, all the way from Chicago to San Francisco, with this kind of service along the way when that money should be spent making sure the brakes are working on Acela and the Northeast corridor that is absolutely dependent on Amtrak is properly funded and properly taken care of.

I am willing to spend what is necessary to spend to keep Amtrak going. But I applaud the Bush Administration in a very significant wake-up call that says Amtrak has to be changed to face the realities of where the market is.

We do not have a market for transcontinental train traffic, either from the standpoint of those who are willing to pay for it. I realize we have to subsidize it. We are subsidizing Amtrak riders to the tune of about $200 per trip. I am perfectly willing to subsidize it with Federal funds in an area where it makes a significant contribution to the reduction in pollution and congestion. But I think subsidizing it to the point that less than 100 people per day can use it in my State does not make any sense.

So Mr. Chairman, I am perfectly willing to raise the amount of money above what the budget calls for from the President. But I do think we should recognize that Amtrak remains virtually unchanged in its route structure since I helped convince the Congress to create it in 1970. That is 35 years ago. It is time we brought it up to reality.

Thank you, Mr. Chairman.

Senator BOND. Thank you, Senator Bennett, for the confession. I know it is good for the soul. I appreciate your prospective suggestions, as well.

Senator Durbin.

STATEMENT OF SENATOR RICHARD J. DURBIN

Senator DURBIN. Thank you, Mr. Chairman. It is a pleasure to be with you at this new committee alignment. We see some new faces but some similar challenges to what we have faced in the past.

I come from a railroad family. My mother, my father, my two brothers and I all worked for the New York Central Railroad in East St. Louis, Illinois. I have many fond memories of steam locomotives and trains and just loved them as a child.

But I do not come to this hearing motivated by memories. I come to this hearing motivated by the economic reality of Amtrak in Illinois today. Amtrak in Illinois serves 3 million passengers a year. By Senator Bennett's standard, we are in the range of 8,000 to 10,000 passengers each day.

Amtrak is a huge part of our State's economy—2,000 employees. The thought of those 3 million passengers losing Amtrak and then turning to cars on the road is a frightening thought. The traffic congestion, the pollution that would result from it—how can that be good for us as a Nation? How can that possibly be a move in the right direction?

Many of the passengers, incidentally, happen to be college students. We serve a lot of campuses with Amtrak. I have met with the presidents and leaders at those universities and colleges downState who say the reason they bring kids in from Chicago is because students know the Amtrak service is going to be there to Champaign. It is going to be there to Macomb. It is going to be there to Quincy and all the other campuses served, Bloomington and other places. So it is not easy to replace that by saying buy all those kids a car. Let us take care of it that way. How can that possibly be the answer to moving people efficiently in an environmentally sensible way?

Let me just add one footnote. It is not as if the State of Illinois is just saying give, give, give. The State of Illinois is a contributor to Amtrak—a substantial contributor—$12 million a year from a State budget that is in trouble. About 90 percent of the operating costs of Amtrak come from our State taxpayers who believe it is important. But for the capital investment in Amtrak and the rest of the operating costs we rely on Amtrak itself.

I will just say one other thing. How many times are we going to go through this debate? How many times are we going to fight this battle? It is getting old. Amtrak cannot improve and modernize its service to the point where it attracts more passengers and more customers unless we are prepared to do for Amtrak what every successful company must do, invest in the future. We need capital investment in Amtrak so that they have better rail bids, faster service, and enough units.

My wife recently took the train with my daughter from Washington to New York. And she said that the entire trip there were people standing in the aisles and sitting in the restrooms. There just were not enough cars to accommodate all of the passengers that were needed. The same thing happened on a recent trip from Chicago to Springfield.

So there is a lot of pent-up demand out there. We need to make capital investments in Amtrak to make it work. I cannot justify every route in America. I will not even try to. But I can tell you in my State of Illinois we stand by Amtrak as an important part not of some nostalgic memory but an important part of our economic future.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF SENATOR THAD COCHRAN

Senator BOND. Thank you, Senator Durbin. Senator Cochran has submitted a statement to be included for the record as well.

[The statement follows:]

PREPARED STATEMENT OF SENATOR THAD COCHRAN

Mr. Chairman, thank you for holding this hearing today to discuss Amtrak's funding request for fiscal year 2006.

I want to thank David Gunn for appearing before this subcommittee to answer questions and for his good service at Amtrak.

When Congress received the President's Budget Request, many people were surprised to find that funding was not requested for our Nation's intercity train system. It is my understanding that the administration has still not requested funding for Amtrak, and I look forward to hearing from the Department of Transportation's representatives about this rationale.

I hope we will be able to consider legislation that will outline the legal authority for a new national passenger rail system. The Appropriations Committee can't do it all.

Senator BOND. Finally, we will get down to the meat of this and find out how those of you with responsibility and expertise in the area, what your recommendations are. First I call on Mr. David Laney, Chairman of the Amtrak Board of Directors. Welcome, Mr. Laney.

STATEMENT OF DAVID M. LANEY, ESQ.

Mr. LANEY. Thank you, Mr. Chairman, Senators.

I appreciate the opportunity to appear before you today. My name is David Laney. I am Chairman of the Amtrak Board of Directors. Joining me is, as you all know, David Gunn, President and CEO of Amtrak.

On April 21, Amtrak transmitted to Congress and the administration a series of strategic reform initiatives that are aimed at reforming Amtrak and maybe more importantly, revitalizing rail passenger service in the United States. Let me touch just briefly on our package before detailing our fiscal year 2006 budget request.

Our plan advances four essential objectives. First, development of passenger rail corridors throughout the country based on an 80/20 Federal/State capital matching program with States becoming purchasers of a variety of competitively bid corridor services.

Second, return of the Northeast Corridor infrastructure to a state of good repair and operational reliability over the next 4 to 5 years with all users of the Northeast Corridor gradually assuming increased financial responsibility for their share of corridor operating and capital needs.

Thirdly, preservation of our national long-distance system, with gradually restructured routes to address your concern, Senator Bennett, that will over time have to meet minimal financial performance requirements, in some cases requiring State assistance.

And finally, the opening of the intercity passenger rail industry to competition and private commercial participation.

This plan is the product of a significant amount of work by Amtrak's Board of Directors and senior management with considerable input from rail experts from outside Amtrak as well. Additional details on these reforms are covered in my full statement but this is a serious proposal that will revitalize the passenger rail industry if it is implemented and adequately funded. I believe it also answers the call to reform made by the administration and by so many others.

We have provided you with a full copy of the plan and hope you will take it into consideration as we move forward with the reauthorization and appropriations process.

I would also like to add a point and at least emphasize the very thoughtful proposals also from the Inspector General of DOT, Ken Mead. He will get into those this morning, but there is substantial common ground between the Amtrak board's presentation and proposals as well as Mr. Mead's and I recommend his proposals as well for your review.

FISCAL 2006 BUDGET REQUEST

As to the fiscal 2006 budget request, let me turn to that now. As Senator Murray pointed out, typically Congress receives our grant request in February. Since we were well into our strategic planning effort at that time, we elected to defer submitting the request in order to present it in the context of our reform package. The last dozen pages of the reform proposal detail our fiscal 2006 budget request and our requirements, which is $1.82 billion or $1.645 billion if our working capital needs are covered by a short-term credit facility instead of a grant.

We have also included a preview of how we would go about reporting Amtrak's financial information by business line.

Let me make a few points about this funding request. First of all, the increase over our current funding level of $1.2 billion is solely attributable to essential capital spending, not operating expenses. These investments have very lasting value.

The operating side is slightly lower than previous years and reflects the company's ability to keep operating costs constant despite inflation, rising insurance costs and the considerably higher cost of fuel.

During the last 3 years we have not borrowed any additional funds nor have we assumed any new debt except for the DOT loan during the summer of 2002, which is being paid back in annual installments.

We have lowered the head count at Amtrak from 25,000 in fiscal year 2001 to 19,500 today. Our deficit per train mile has decreased from $22 in fiscal year 2000 to $13 in 2004. Ridership, as a couple of you have pointed out, has continued to increase. Last year we had just over 25 million passenger trips, which was a company record. In fact, during fiscal years 2000 to 2004, ridership has grown from 22.5 million to 25.1 million, or 11.6 percent.

We are very confident that there is additional, significant suppressed demand.

On the capital side, we have made significant early headway in addressing the mountain of deferred maintenance in both plant and equipment facing us when the new management team arrived in 2002. The work that we have completed and plan to do is detailed in our budget proposal.

In fiscal year 2006, we expect to continue this type of capital investment, renewal of track, signals, wire, equipment, switches, and interlockings. But we also will begin major multi-year projects to rebuild structures critical to the Northeast Corridor operations. These include replacement of the failure-prone movable bridge spans over the Thames and Niantic Rivers, replacement of the 1930's era cables in the Baltimore tunnels, and major track work on the Harrisburg line. Until we complete the bridge and tunnel work, we will continue to court the risk of a failure that could sever NEC service.

These projects involve outside contractors and long lead times in ordering of materials as well as multi-year funding commitments to support the projects. But when they are completed, the repaired and rebuilt structures will last a lifetime.

CANNOT SURVIVE ON CURRENT FUNDING LEVEL

Finally, it is important to emphasize that Amtrak's board and management have concluded that the company cannot continue to operate on Amtrak's current funding level of $1.2 billion in fiscal year 2006. Moreover, the negative financial impact of the recent Acela problems will substantially deplete our working capital by year's end. We have taken and will continue to take aggressive steps to achieve short-term savings but we have very little maneuverability in our operating budget and cannot responsibly make material reductions in capital expenditures principally tied to Northeast Corridor infrastructure and its state of good repair. Over time, significant savings will be achieved only through aggressive and systematic multi-year transitioning with legislative assistance.

It is for this reason that we have brought forward our strategic reform initiatives to help inform your decision-making for fiscal year 2006 and beyond.

PREPARED STATEMENT

In closing, we look forward to working with you. We fully understand the difficulties you have in this budget year. We also look forward to working with stakeholders in the months ahead as we further develop and implement our reform plan and move this debate forward. I cannot emphasize enough that adequate funding for Amtrak in 2006 will be a critical first step in advancing the objectives of our strategic reform initiatives plan.

We look forward to your questions. Thank you, Mr. Chairman.

[The statement follows:]

PREPARED STATEMENT OF DAVID M. LANEY, ESQ.

Mr. Chairman and members of the committee, thank you for the opportunity to appear before you today. My name is David Laney, and I am Chairman of the Amtrak Board of Directors. Joining me is David Gunn, the President and Chief Executive Officer of Amtrak.

On April 21, Amtrak transmitted to Congress and the administration a series of Strategic Reform Initiatives that we believe will help shape the discussion on the future of Amtrak and intercity rail passenger service. While the majority of the report was geared toward the reauthorization discussion, it did contain Amtrak's fiscal year 2006 grant request. I will provide an overview of both.

For the past several months, the Board and senior management at Amtrak have worked to produce a set of proposals to reform Amtrak and revitalize rail passenger service in the United States. The reform initiatives released April 21 are the results of those efforts. The reform plan contains a detailed set of initiatives, some of which Amtrak will accomplish on its own and others which will require government action. Taken together, we believe that Amtrak's Strategic Reform Initiatives can revitalize intercity rail transportation.

Our proposal advances four essential objectives:

—Development of passenger rail corridors based on an 80–20 Federal-State capital matching program, with States becoming "purchasers" of a variety of competitively bid corridor services.
—Return of the Northeast Corridor infrastructure to a state of good repair and operational reliability, with all users gradually assuming increased financial responsibility for their share of corridor operating and capital needs.
—Preservation of our national long distance system, with gradually restructured routes that will over time have to meet minimum financial performance requirements, in some cases requiring State assistance.
—Finally, the opening of the intercity passenger rail industry to competition and private commercial participation.

We have identified three sets of reform initiatives to achieve the objectives that I just mentioned. They include, in general terms, structural, operating and legislative changes.

STRUCTURAL INITIATIVES

As you know, Amtrak has already made substantial progress in establishing an organizational structure and creating management controls which have resulted in cost savings and better management; but there is room for further improvement. We will continue to implement these types of changes and refine those already in place. To build on such improvements, our plan focuses on providing planning, budgeting, accounting and reporting of financial activity and performance along our distinct business lines—infrastructure management, Northeast Corridor rail operations, State corridor operations and long-distance operations. This type of change will improve our own planning and performance capabilities, and enhance the financial clarity of our operations.

OPERATING INITIATIVES

Separately, operating initiatives identified in our plan highlight a range of actions intended to improve the performance of each business line to provide better service, achieve savings and enhance revenues. Our recommendations for changes in legislation hinge directly on creation of a Federal capital matching program. Other recommendations in our view, if implemented, would create a more fertile environment for competition in intercity rail passenger services and operations.

LEGISLATIVE INITIATIVES

The lynchpin of this plan is the establishment of a Federal matching program appealing enough to attract and accelerate State financial involvement in emerging and existing corridors. Continued development of rail corridors is critical to the future of rail passenger service, and the pace of development will increase with the Federal Government as a reliable financial partner—the role it has played for almost half a century with highways, transit and aviation. The demand that exists today for high quality intercity passenger rail in this country will only grow with the rising congestion in highways and airports. A number of States have already begun developing rail corridors, largely on their own nickel. They have recognized the value of passenger rail capacity in responding to increasing congestion, and the popularity of rail service when it is adequately supported. (Ridership on corridor trains has grown 22 percent over the last 5 years.) However, to realize the full potential of intercity passenger rail in addressing transportation challenges will require a Federal match program comparable with other modes.

Returning the Northeast Corridor's infrastructure to a state of good repair is another essential part of our reform proposal. In compiling this plan, we studied various proposals and reviewed models that other countries have pursued for separating the maintenance and operations of busy rail corridors and have concluded for now that the complexities and risks associated with such a split outweigh any benefits. Amtrak owns most of the Northeast Corridor, is the only end-to-end user of the

Corridor and, in terms of train miles operated, is also the majority user. Amtrak NEC trains operate at the highest speeds in North America, and there are still segments of the NEC where Amtrak is the only entity operating trains. Our immediate challenge is to restore the infrastructure to a state of good repair, which we are doing, as detailed in our proposal. Ridership continues to grow along the Northeast Corridor; in the near term we will have to begin planning for additional capacity to meet that ridership demand.

Amtrak operates 15 long-distance trains and for more than half of the States we serve, they are the only Amtrak service. Unfortunately, long-distance trains have become the flash-point in the debate over "reform" of passenger rail service. That single-minded focus is misleading, although our long-distance service presents a variety of challenges. To be clear, Amtrak is committed to the preservation of national passenger rail service. Many communities served by long-distance trains lack real transportation choices and rely on these services. While we believe the continued operation of these trains is important to many communities they serve, they also represent the basis for interconnection and future expansion of rail corridors. We are confident that we will reduce the operating losses on long distance trains through a series of steps outlined in our plan, and we believe those reductions will be substantial; however, we will not eliminate the need for financial support for long-distance operations. Central to this is the establishment of a phased-in performance improvement program that will couple cost-saving efficiencies with revenue enhancement initiatives, so that over time these trains will achieve financial performance thresholds or be discontinued.

Finally, we believe that there are many opportunities for competition in the delivery of rail passenger services. Having a single provider such as Amtrak does allow for economies of scale and certain cost efficiencies. Yet, Amtrak is not always the most efficient provider of rail-related services. There should be alternatives. Key to our plan is the development of a competitive supply industry and multiple service delivery options. Amtrak can take a few essential steps in that direction, but without Federal legislative assistance, we will not reach the station. Some of the legislative decisions in this area will be difficult and will encounter predictable resistance from entrenched interests. Any discussion of competition will involve making decisions about access rights to the freight rail infrastructure, tort liability limitations and limited changes to certain labor and labor retirement laws. We have provided a discussion of these matters in our proposal.

FISCAL YEAR 2006 GRANT REQUEST

Let me turn to our fiscal year 2006 funding request. Typically, Congress receives our grant request in February. Since we were well into our strategic planning effort, we elected to defer developing the request, in order to present it in the context of our reform package. The last dozen pages of the proposal detail our fiscal year 2006 budget requirement, which is $1.82 billion or $1.645 billion if our working capital needs are covered by a short-term credit facility instead of a grant. We have also included a preview of how we would go about reporting Amtrak's financial information by business line.

Let me make a few points about this request.

—The operating request is slightly lower than previous years and reflects the company's ability to keep operating costs constant, despite inflation, rising insurance costs and the high cost of fuel.

—During the past 3 years, we have not borrowed any additional funds nor have we assumed any new debt, except for the DOT loan during the summer of 2002, which is being paid back in annual installments.

—We have lowered headcount from 25,000 in fiscal year 2001 to 19,500—its current level—or a reduction of about 20 percent.

—Our deficit per train mile has decreased from $22 in fiscal year 2000 to $13 in fiscal year 2004.

—Ridership has continued to increase. Last year we had just over 25 million passenger trips, a company record. In fact, during the period fiscal year 2000 to fiscal year 2004, ridership has grown from 22.5 million to 25.1 million or 11.6 percent.

On the capital side, we have made significant early headway in addressing the mountain of deferred maintenance in both plant and equipment facing us in 2002. The work that we have completed and plan to do is detailed in our budget proposal. In fiscal year 2006, we expect to continue this type of capital investment—renewal of track, signals, wire, equipment, switches and interlockings—but we will also begin major, multi-year projects to rebuild structures critical to Northeast Corridor operations. These include replacement of the failure prone moveable bridge spans over the Thames and Niantic rivers, replacement of 1930's era cables in the Baltimore tunnels, and major track work on the Harrisburg line. Until we complete the bridge and tunnel work, we will continue to court the risk of a failure that could shut down NEC service. These projects involve outside contractors and long lead time in ordering of materials, as well as multi-year funding commitments. But when they are completed, the repaired and rebuilt structures will last a lifetime.

Finally, it is important to emphasize that Amtrak's Board and management have concluded that the company cannot continue to operate at Amtrak's current funding level of $1.2 billion in fiscal year 2006. Moreover, the negative financial impact of the recent Acela problems will diminish our working capital significantly by year-end. We have taken and will continue to take aggressive steps to achieve short-term savings, but we have very little maneuverability in our operating budget and cannot responsibly make material reductions in capital expenditures (principally tied to NEC infrastructure, and its state of good repair). Over time, significant savings will be achieved only through an aggressive and systematic, multi-year transition process with legislative assistance. It is for this reason that we have brought forward our Strategic Reform Initiatives to help inform your decision-making for fiscal year 2006 and beyond.

In closing, David Gunn, his management team, my fellow Board members and I look forward to working with you and other stakeholders in the weeks and months ahead as we further develop and implement our plan and move this debate forward. I cannot emphasize to you enough that adequate funding for Amtrak in fiscal year 2006 will be a critical first step in advancing the objectives of our strategic reform initiatives plan.

We look forward to your questions.

Senator BOND. Thank you very much, Mr. Laney.

We are very excited that you are putting forth a workable plan. I must tell you that until somebody can talk to the Office of Management and Budget, no matter how good a plan is put forward, this subcommittee is going to have tremendous difficulty funding it. And with your background, experience and your ability as a skilled counselor and advocate, we are going to have to count on you to help sell that because without the dough this subcommittee just cannot go.

On that bright and cheery note, let me turn now to Mr. Rosen for his comments.

STATEMENT OF JEFFREY A. ROSEN

Mr. ROSEN. Mr. Chairman, Senator Murray and members of the subcommittee, thank you for inviting me here today. You have my full written statement, so I am going to limit my oral remarks to three primary topics.

The first item I would like to address is some comments on the President's budget submission for Amtrak. Some have asked if the administration's budget is serious in seeking reform of Amtrak this year, and it is.

Others have asked if we are serious that if we get real reform, we will support funding for a reformed system of intercity passenger rail. And the answer is that we are serious about that, too.

Still others have asked well, how much money? But I cannot answer that until we get actual reforms. The administration will be prepared to talk about the amount of funding when Congress itself takes serious steps to fix passenger rail. But the reforms have to come first. Otherwise, we know from history, we will never see any real reforms.

The administration is very serious about opposing the status quo arrangement. We do not support continuing funding for a broken system that has proven itself fatally flawed.

So the second topic that I want to briefly address is what constitutes reform? That is a fair question but the administration has submitted its proposals for reform to the Congress, both in 2003 and again this year. Those proposals would modernize, revitalize and enhance intercity passenger rail. The five key principles of those proposals are included in my written statement so I will not go through them because it would take too long here. But I encourage all to review them because they underlie the reforms that we seek.

By contrast, I should say that the administration does not consider a $2 billion a year simple reauthorization to be a serious plan and would certainly not be reform. In fact, any approach that relies on just funneling more money into operating subsidies is not reform.

And that takes me to the third and final item I would like to address for today, that some have already alluded to, and that is that the alternative to legislative reform is not the status quo. As Amtrak itself has said, the status quo is unsustainable. Amtrak continues to spend at a rate far in excess of its revenues. And that is why the $360 million that the President's budget proposes for protecting commuter train service and protecting Northeast corridor trains needs to be taken seriously in the budget. But that is also the reason that those of us who want to save intercity passenger rail hope to work with the Congress to change the system and change where the funding goes.

PREPARED STATEMENT

And while we are working with the authorizing committees to discuss the reform proposals, and we appreciate that Amtrak itself and Mr. Gunn are themselves supporting of the concept of reform, ultimately reform may also need some assistance from this committee as well as intercity passenger rail goes through a necessary transition away from the 1970 model that we have been living with for a number of years to something more contemporary and workable.

Thank you, and I will be pleased, of course, to respond to any questions.

[The statement follows:]

PREPARED STATEMENT OF JEFFREY A. ROSEN

Mr. Chairman, Senator Murray, and members of the subcommittee, I appreciate the opportunity to appear before you today to address the urgent need for reform of intercity passenger rail service before further appropriations are provided to Amtrak.

By now, everyone is of course aware of the President's budget proposal for Amtrak. That budget proposal was meant as a call to action. Fundamental change in the way we support intercity passenger rail service is not only necessary but inevitable. And that change needs to happen this year, before we appropriate one more taxpayer dollar to prop up a fundamentally broken system. As you are aware, the administration transmitted its legislative proposal to Congress, the Passenger Rail Investment Reform Act (PRIRA), and we hope Congress will move quickly to enact needed reforms.

At this juncture, the only funds this subcommittee should appropriate are $360 million to provide for directed service of commuter and Northeast corridor trains in the event the current Amtrak model cannot deliver that service. Intercity passenger rail needs major reform, and it would do more harm than good to simply continue funding the status quo without reform.

Amtrak itself has acknowledged the urgent need for reform, and that the 1970's model of passenger rail should not continue. Amtrak recently released its own strategic plan, which states "Business as usual for Amtrak and intercity passenger rail is not sustainable as currently structured or funded." While it is the responsibility of the Authorizing Committees to consider the reform legislation, the subsidy questions are closely related to the reform issues, so I would like to set forth some of the facts and analysis that underlie the administration's reform proposal to assist in the appropriations process for fiscal year 2006.

First and foremost, it is essential to recognize that the passenger rail service model created by the Federal Government in 1970 is not viable in 2005. The model created in 1970 was a single national monopoly set up to be a private corporation but it has instead become like a government agency relying on Federal support to survive, with a legacy system of routes incapable of adapting to market forces and demographic changes (but with less accountability than a government agency would have). It has little in common with our other modes of transportation and the deregulatory and market-oriented changes other modes have experienced in the last three decades. America's transportation system as a whole—our system of roads, airports, waterways, transit lines, and the mostly private operators who use them—provides excellent mobility, connectivity, and efficiency that have undergirded our economic growth. Sadly, intercity passenger rail has been a different story. The supposedly private for-profit corporation set up in 1970 to provide all intercity passenger rail nationally has never once covered its own costs, much less made a profit. And the Federal taxpayers have infused more than $29 billion into Amtrak during the last 34 years as it has lurched from crisis to crisis without ever achieving a stable and viable business model. Whatever one thinks of Amtrak or passenger rail more generally, this situation has been good for no one.

To some, perhaps this is old news. Congress directed change in the Amtrak Reform and Accountability Act of 1997, and actually required that "Federal financial assistance to cover operating losses incurred by Amtrak should be eliminated by the year 2002." In fact, the notion that Amtrak should operate free from Federal operating subsidies is codified as law in the United States Code: 49 U.S.C. § 24101(d) states that "Commencing no later than the fiscal year following the fifth anniversary of the Amtrak Reform and Accountability Act of 1997, Amtrak shall operate without Federal operating grant funds appropriated for its benefit."

In the 1997 Act, Amtrak was afforded new flexibility to get its house in order. But by 2002, Amtrak's situation was no better; to the contrary, it had grown worse, with massive increases in Amtrak's debt, continuing operating problems, and financial crises in both 2001 and 2002. Amtrak's response once again was to turn to the Federal Government for even greater Federal financial assistance, simply ignoring 49 U.S.C. § 24101(d) as well as §§ 204 and 205 of the Amtrak Reform and Accountability Act of 1997. In no other functioning service market would rising costs and declining revenues be defined as a "success" if this produced a small increase in the number of customers. Yet, that is exactly what the defenders of the 1970 approach now say, as if the loss for each rider were "made up in volume". In 2004, Amtrak increased its ridership by approximately 4 percent to a record 25 million passengers, asked for a record $1.8 billion Federal subsidy, and recorded a financial loss of more than $1.3 billion, of which approximately $635 million was a cash loss.[1] This year again, Amtrak indicates that it may have less than $75 million in cash remaining at the end of fiscal year 2005.

Things do not have to be this way. It is simply untrue that all passenger rail everywhere must have operating subsidies from government. It is simply untrue that there is no alternative to passenger rail remaining the most heavily subsidized form of transportation on a per passenger basis. The administration has made clear that there is an important role for intercity passenger rail in our transportation system, but only with a new model that will be responsive to the needs of the traveling public. We can only get there by reforming the failed model of 1970, and committing to a new approach. That is the point of the President's budget request.

RIDING THE RAILS: AMTRAK'S PAST AND PRESENT

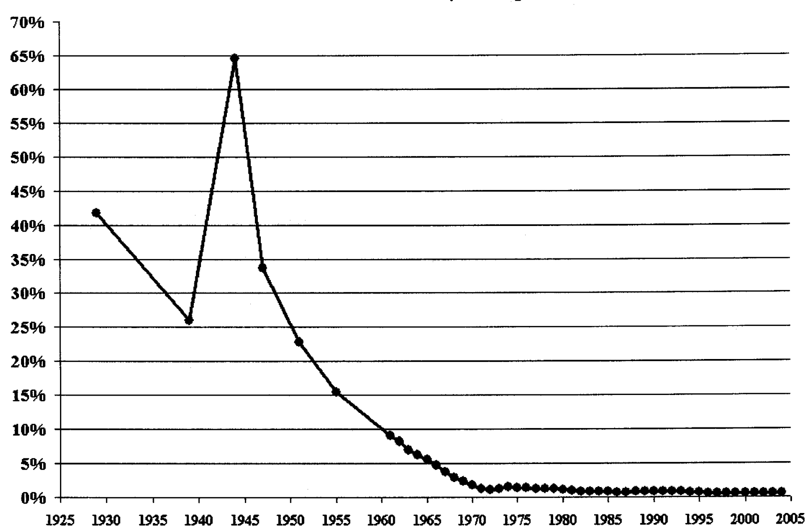
Amtrak was created in 1970 as a private corporation in a restructuring of the larger rail industry, which was in a state of major financial distress. In that restructuring, freight railroads ceased providing passenger service altogether. Instead, for the first time, there would be a single national provider of intercity passenger rail service to replace the multiple regional systems that reflected the areas covered by each of the freight railroads' route systems. The intent was that the national monop-

[1] These are unaudited numbers.

oly would reinvigorate passenger rail by permitting Amtrak to consolidate operations and achieve efficiencies that, after a very brief period of Federal assistance, would preserve and expand intercity passenger rail service as a for-profit company.

By now we know that the hopes of Amtrak's creators have never been realized. Intercity passenger rail service has not been reinvigorated. The Department of Transportation (DOT) expects that each and every one of Amtrak's 15 long-distance trains will this year lose money on a fully allocated cost basis, even excluding depreciation and interest. On a per passenger basis, with depreciation and interest, the loss for long-distance trains ranges from $47 per passenger to $466 per passenger. But the long-distance trains are not alone: with depreciation and interest included, every one of Amtrak's 43 regularly scheduled routes loses money. See Appendix A, attached. After 34 years and $29 billion in Federal subsidies, intercity passenger rail's financial performance has not improved, service and on-time performance are below expectations, and passenger rail's market share relative to other modes has continued to erode. Last year's so-called "record" Amtrak ridership amounted to a one-half of 1 percent share of the total intercity passenger transportation market. Airlines alone carry more U.S. passengers in 3 weeks than Amtrak does in a year.

Rail as Percent of Estimated Total Intercity Passenger Travel, 1929-2004



[SOURCES.—Rail travel: Association of American Railroads, Yearbook of Railroad Facts; Amtrak. Total intercity passenger travel is an FRA estimate synthesized from data provided by the Federal Highway Administration, Federal Aviation Administration, Bureau of Transportation Statistics (including travel behavior characteristics the 1995 American Travel Survey), the AAR, and Amtrak. For rail, "intercity" passenger-miles are an approximation as they include all passenger-miles generated on intercity trains, regardless of the length or purpose of individual trips. All air travel is deemed "intercity." For highway modes (privately-owned vehicles and buses), the synthesis approximates intercity travel as trips of 100 miles or more one-way.]

That also belies one of the frequent arguments of today's defenders of the 1970 model—that the Federal Government supposedly subsidizes other modes of transportation at a greater rate than Amtrak. In fact, fiscal year 2005's appropriated subsidy of $1.207 billion represented approximately 9 percent of the total discretionary Federal funds for the Department—9 percent of Department funds go for one-half of 1 percent of the market. The argument also passes quickly over another important fact: highways, transit and aviation are, unlike rail, funded substantially by user fees and also by State investments. Perhaps most importantly, however, the argument overlooks that Federal financial support for roads, airports, and transit goes to infrastructure and not to operations. In other modes of transportation, Federal aid goes to highway and airport infrastructure, for example, but Federal taxpayers are not regularly asked to write annual billion dollar checks to private trucking companies, private bus companies, private automobile commuters and vacationers, nor even to private airlines, although the taxpayers have regularly done so with regard to Amtrak.

In considering where we are with Amtrak, it is useful to consider the varied things that Amtrak presently does to understand that recent appropriations to this private company have not been limited to rail infrastructure, but also go into actual train operations. Generally, Amtrak's business can be grouped into activities relating to (1) rail infrastructure, (2) corridor train operations, and (3) long-distance train service.

Rail Infrastructure

Amtrak owns its own right of way and rail infrastructure along most of the Northeast Corridor (NEC), except in Massachusetts and part of Connecticut, where the infrastructure is owned by those States. Amtrak also owns some infrastructure in Michigan, as well as train stations in a number of States. Otherwise, Amtrak mostly operates trains on rail infrastructure owned by others.

Within the Northeast Corridor, Amtrak controls the infrastructure not only for its own use, but for use by numerous other railroads and transit agencies.

LIST OF USERS OF THE NEC OTHER THAN AMTRAK

CSX
Long Island Rail Road
Maryland Rail Commuter Service
Massachusetts Bay Transportation Authority
Metro-North Commuter Railroad
Delaware DOT
Rhode Island DOT
Canadian Pacific
New Jersey Transit
Norfolk Southern
Providence and Worcester Railroad
Shore Line East (Connecticut)
Southeastern Pennsylvania Transportation Authority
Virginia Railway Express
Consolidated Rail Corporation

These other users of the NEC pay Amtrak for access and associated services, such as train dispatching. In total, trains operated by other users on the NEC actually exceed the number of trains operated by Amtrak itself on the NEC.

Because of the way the 1970 model of intercity passenger rail was organized, maintenance and development of infrastructure in the NEC has been left to Amtrak.

In fiscal year 2005, Amtrak has budgeted $215 million on fixed facility infrastructure projects, and a total of $587.2 million for capital expenses, most of which will come from the $1.2 billion of Federal appropriations made available by this subcommittee. None of those funds will be allocated to States, or to infrastructure in locations where Amtrak does not presently operate. Federal infrastructure dollars are allocated by a private corporation, Amtrak, instead of by State, local, and even Federal transportation planning officials.

Corridor Services

When viewed from the perspective of moving passengers, and the distance they are moved (passenger-miles), Amtrak can be seen as providing two types of services: "corridor services" of approximately 100–500 miles and frequently under contract to States in which these corridors are located; and "long-distance", primarily leisure travel services. Within the category of corridor services, there are two different types: services on the NE corridor, where Amtrak operates on its own track and infrastructure, and services on other State corridors, where Amtrak operates on track and infrastructure owned and controlled by others.

Northeast Corridor.—Approximately 20 million people, or 80 percent of all Amtrak riders in 2004, traveled on a corridor service. The largest portion of Amtrak corridor trips are on the Washington-New York City-Boston Northeast Corridor (NEC). If one looks at NEC train operations, separate from the NEC infrastructure, this is the one area where Amtrak operates at something close to a breakeven basis.

Other Corridors.—In addition to the NEC main line, Amtrak operates trains for corridor service in 15 other States.

LIST OF STATES WITH CORRIDOR SERVICE

CALIFORNIA: Pacific Surfliner, Capitols, San Joaquins.
CONNECTICUT/MASSACHUSETTS: Inland Route (New Haven-Springfield).
ILLINOIS: Chicago-St.Louis, Illini, Illinois Zephyr, Hiawatha (with Wisconsin).
MAINE: The Downeaster.
MICHIGAN: Wolverines, Blue Water, Pere Marquette.
MISSOURI: Kansas City-St.Louis.
NEW YORK: Empire/Maple Leaf, Adirondack.
NORTH CAROLINA: Carolinian (Extended corridor), Piedmont.
OKLAHOMA: Heartland Flyer.
OREGON: Cascades (with Washington).
PENNSYLVANIA: Keystone Service, Pennsylvanian (Extended corridor).
WASHINGTON: Cascades (with Oregon).
WISCONSIN: Hiawathas (with Illinois).
VERMONT: Ethan Allen Express, Vermonter (Extended corridor).

NOTE.—States listed are the primary States served by each corridor.

In 2004, a total of approximately 8 million people (i.e., approximately one-third of the total Amtrak ridership) traveled on these additional corridor routes. In many instances, these corridors are subsidized in part by States. State operating subsidies for these trains totaled 10 percent of the combined Federal and State funding of Amtrak. However, States have not borne the full cost of these routes, and some States that have corridor trains have not paid anything at all, thereby producing issues of equity among the States, as well as market uncertainties about how travelers value the services. In the aggregate, on a fully-allocated basis, the non-NEC corridor trains (including both corridor and extended corridor service) had an average operating subsidy of $28 per passenger in fiscal year 2004.

Long-Distance Services

Amtrak's 15 long-distance trains have seen declining revenues and ridership—and increasing costs—over the last 10 years. DOT refers to these services as Transcontinental (more than 1 night), Overnight (1 night) or extended corridor (greater than 500 miles, but with no sleeping accommodations). Amtrak presently operates 15 such trains.[2] Amtrak has continued to lose long-distance trip customers to an airline industry that is offering a low cost, high quality service, and to automobile drivers who choose to use highways rather than rail. Amtrak has had little or no success responding to this competition. As Amtrak's presence in this segment of the intercity transportation market has dwindled, Federal subsidies per passenger have continued to grow. In fiscal year 2004, the average passenger on a long-distance train received a subsidy of approximately $214 per trip on a fully-allocated basis,[3] up from $158 in the year 2000—a 35 percent increase quintupling the 7 percent inflation over the same period.

FULLY ALLOCATED LOSSES OF LONG-DISTANCE PASSENGER TRAINS, FISCAL YEAR 2004 [1]

Service Type/Route	Route No.	Subsidy Status		Fully Allocated Loss (Fully Loaded with Depreciation, Interest, and All Overheads)	Fully Allocated (Loss) Per Passenger	Fully Allocated (Loss) Per Passenger-Mile
		Unsubsidized by a State	Subsidized by a State			
EXTENDED CORRIDORS:						
Pennsylvanian	RT57	x		($11,911,500)	($69)	($0.337)
Vermonter	RT04		x	($11,793,249)	($47)	($0.254)
Carolinian	RT66		x	($16,723,244)	($55)	($0.197)

[2] The long-distance routes are as follows: Vermonter, Silver Service, Cardinal, Empire Builder, Capitol Limited, California Zephyr, Southwest Chief, City of New Orleans, Texas Eagle, Sunset Limited, Coast Starlight, Lake Shore Limited, Crescent, Pennsylvanian, Carolinian. The Auto-Train, a specialized service, also operates over a long-distance route but with completely different characteristics. The Three Rivers (New York-Pittsburgh-Akron-Chicago) was discontinued in March 2005.

[3] Fully allocated costs include depreciation and interest.

FULLY ALLOCATED LOSSES OF LONG-DISTANCE PASSENGER TRAINS, FISCAL YEAR 2004 [1]—Continued

Service Type/Route	Route No.	Subsidy Status		Fully Allocated Loss (Fully Loaded with Depreciation, Interest, and All Overheads)	Fully Allocated (Loss) Per Passenger	Fully Allocated (Loss) Per Passenger-Mile
		Unsubsidized by a State	Subsidized by a State			
OVERNIGHT:						
Silver Service	RT16A	x		($173,078,522)	($234)	($0.374)
Three Rivers (discontinued)	RT17	x		($75,173,377)	($492)	($0.990)
Cardinal	RT18	x		($18,602,874)	($209)	($0.497)
Capitol Limited	RT26	x		($43,784,083)	($242)	($0.486)
City of New Orleans	RT30	x		($30,429,407)	($160)	($0.335)
Texas Eagle	RT32	x		($42,914,712)	($183)	($0.282)
Coast Starlight	RT34	x		($63,002,725)	($152)	($0.271)
Lake Shore Limited	RT45	x		($63,803,165)	($228)	($0.387)
Crescent	RT52	x		($64,761,043)	($252)	($0.445)
TRANSCONTINENTAL:						
Empire Builder	RT25	x		($75,338,574)	($172)	($0.223)
California Zephyr	RT27	x		($89,696,739)	($267)	($0.320)
Southwest Chief	RT28	x		($121,849,944)	($420)	($0.390)
Sunset Limited	RT33	x		($44,953,841)	($466)	($0.406)

[1] Source.—Amtrak Route Profitability System.
See Appendix A for a more detailed account.

Moreover, these long-distance trains have had considerable difficulty with regard to on-time departures and arrivals:

ON-TIME PERFORMANCE OF LONG-DISTANCE TRAINS, FISCAL YEAR 2004

Train Name	Service Type	Between	—And	Percent On-Time (Zero Tolerance)	Average Minutes Late per Train (All Trains)	Average Minutes Late per Late Train
California Zephyr	Transcon	Chicago	Bay Area	14.2	136	159
Capitol Ltd.	Overnight	Chicago	Washington	13.8	101	118
Cardinal	Overnight	Chicago	New York via Cincinnati.	33.1	48	74
Carolinian	Extended Corridor	New York	Charlotte	26.9	38	51
City of New Orleans	Overnight	Chicago	New Orleans	47.7	26	50
Coast Starlight	Overnight	Seattle	Los Angeles	10.8	139	157
Crescent	Overnight	New York	New Orleans	41.6	34	58
Empire Builder	Transcon	Chicago	Seattle	68.3	11	36
Lake Shore Ltd.	Overnight	Chicago	New York	8.2	123	134
Pennsylvanian	Extended Corridor	New York	Pittsburgh	17.2	32	39
Silver Meteor	Overnight	New York	Miami	25.6	84	113
Southwest Chief	Transcon	Chicago	Los Angeles	28.5	68	96
Sunset Limited	Transcon	Orlando	Los Angeles	1.6	359	366
Texas Eagle	Overnight	Chicago	San Antonio	41.9	57	98
Vermonter	Extended Corridor	Washington	St. Albans VT	32.1	21	30

Overall, the picture of where things stand in intercity passenger rail service is far from what was hoped for when Amtrak was created in 1970. In short, while service and ridership erode, Amtrak continues to require extraordinary and ever-increasing subsidies from the Federal taxpayer despite the original model's intent and Congress' clear call for an end to operating subsidies by 2002 in the 1997 Amtrak Reform Act.

Commuter Rail.—In addition, Amtrak has contracts to operate trains for certain transit agencies and State governments. These are: Connecticut Department of Transportation Shore Line East (SLE/CONNDOT), Long Island Rail Road (LIRR), New Jersey Transit (NJT), Southeastern Pennsylvania Transportation Authority (SEPTA), Delaware Transit Corporation (DELDOT), Maryland Transit Administration (MARC), Virginia Railway Express (VRE), Northeast Illinois Regional Commuter Railroad Corporation (METRA), Southern California Regional Rail Authority

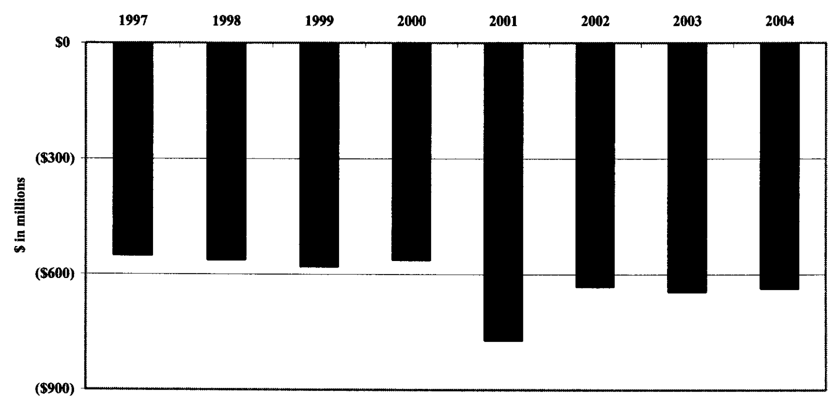
(SCRRA) Metrolink, North San Diego County Transit District Coaster Commuter Rail Service, Peninsula Corridor Joint Powers Board (CALTRAIN), Central Puget Sound Regional Transit Authority (Sound Transit), and Altamont Commuter Express Authority (ACE). In the event of a business failure by Amtrak, the President's budget calls for $360 million to be appropriated to fund directed service of these trains (as well as those of the NEC). Such funding would protect commuter service affecting approximately 2,342 trains and 1,187,860 passengers each weekday for the relevant transit agencies, so that they would not be impacted by Amtrak's problems involving intercity service.

RECENT HISTORY AND THE CALL TO CHANGE

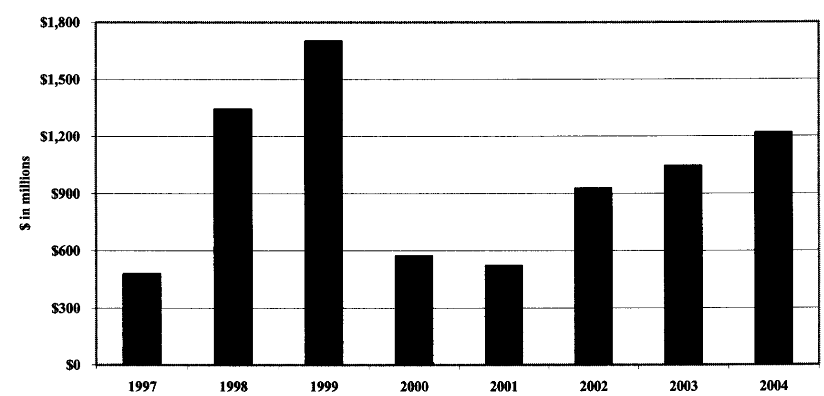
During the 1990's, there was an increasing recognition that the 1970 model of intercity passenger rail had developed some very serious problems. Congress sought to redress some of those in the 1997 Amtrak Reform Act. Unfortunately, the reforms embodied in the 1997 Act did not prove sufficient to solve the problems.

Many of the reforms in the 1997 Act empowered Amtrak to improve its own performance and removed impediments to its doing so. After passage of the 1997 Act, Amtrak's then-management repeatedly reported that it was it on a "glide path" to self-sufficiency by 2002. That did not happen. The problems worsened, and it became increasingly clear that they were not solely the result of business misjudgments, but also involved inherent flaws in the 1970 model.

Amtrak Cash Losses - 1997 Through 2004



Amtrak Federal Appropriations - 1997 Through 2004



Instead of a successful “glide path”, Secretary Mineta was greeted with some unwelcome surprises in his initial experiences with Amtrak during the current administration. Early in 2001, instead of Amtrak being months from self-sufficiency as reported, Amtrak’s then-management advised that Amtrak would be insolvent within 2 weeks unless the DOT subordinated the interest of U.S. taxpayers to a foreign bank so that Amtrak could mortgage its rights to use Pennsylvania Station in New York City. Within a year, Amtrak had lurched to yet another financial crisis, informing the Secretary that if the Department and Congress did not provide the company another $300 million, it would be insolvent within 2 weeks and would shut down commuter and intercity services. In response, to obtain time to assess and identify more long term reforms, DOT provided Amtrak a $100 million loan under the Railroad Rehabilitation and Improvement Financing Program, and Congress provided the remaining $205 million through a supplemental appropriation.

These crises highlighted fundamental problems, some of which needed immediate action by Amtrak, and some of which were revealed to be inherent to the 1970 business model and in need of legislative change. Among the most urgent for Amtrak itself was the state of its financial books and records. Indeed, it took independent auditors almost all of fiscal year 2002 to close their audit of Amtrak’s fiscal year 2001 financial performance. That audit required $200 million in net audit adjustments and found 5 material weaknesses and 12 reportable conditions that needed to be addressed to fix the problems with Amtrak’s accounting practices. It also revealed that Amtrak had taken on almost $3 billion in new debt in order to pay for (1) costly overruns of poorly managed capital improvements, (2) an unsuccessful foray into the express package business, and (3) day-to-day operational expenses.

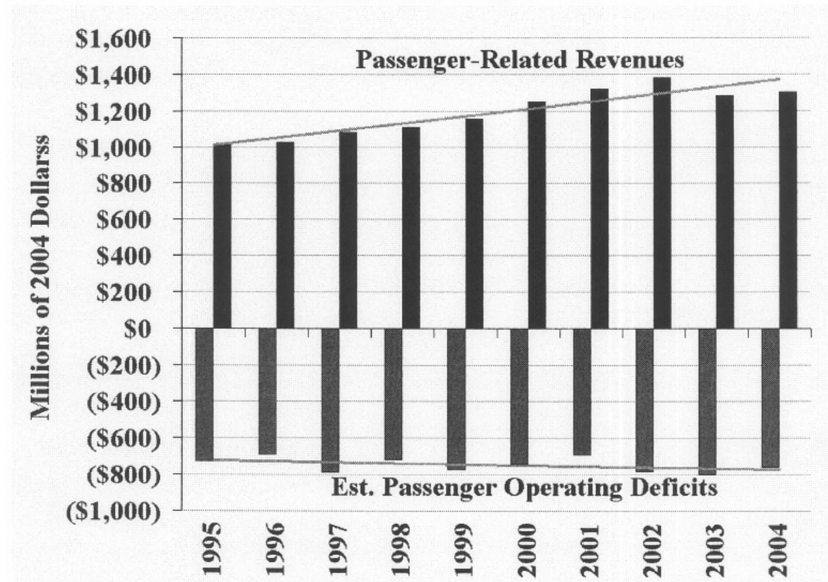
Since 2002, Amtrak’s record-keeping has improved. In 2005, the independent audit was completed in March instead of September and no material weaknesses were found. While Amtrak’s auditors still find significant areas for improvement, they comment favorably on developments over the last 3 years.

Through participation on the Amtrak Board, and through changes to the appropriations process that enabled stronger FRA oversight of the grant process to Amtrak, Secretary Mineta and DOT have sought a variety of improvements that Amtrak could make on its own. That process continues and is ongoing. Happily, Amtrak operates in a more efficient and better way than it did 3 years ago, and the new requirements imposed by recent appropriations bills have produced significant improvements, and need to remain in place.

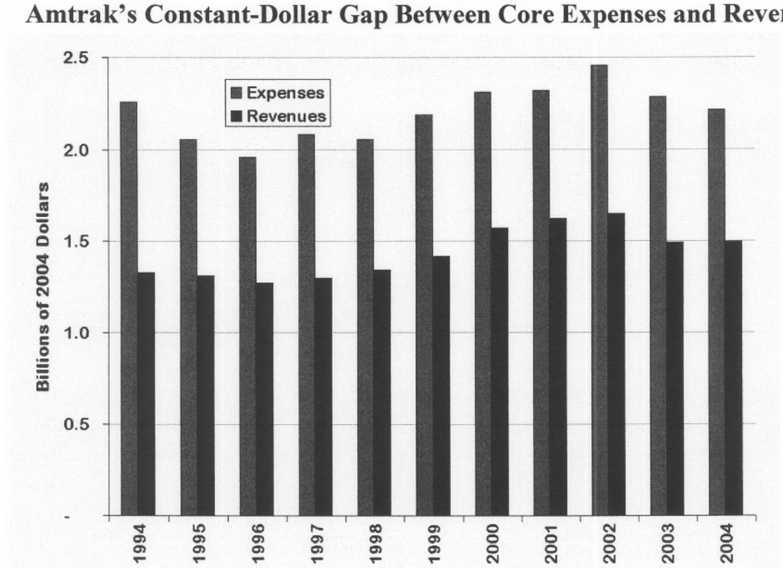
But notwithstanding the very significant management improvements and a much-enhanced and valuable involvement of the Amtrak Board, fundamental difficulties continue to confront Amtrak, because the 1970 model of intercity passenger rail is a framework that is flawed. Amtrak continues to spend dramatically more money than the revenues it generates, and this year is spending at a pace greater than the appropriation from Congress. Amtrak has estimated that by the end of fiscal year 2005 it will have less than $75 million to $100 million of cash remaining, with its costs continuing to far exceed its ticket sales.

As shown by the two charts below, the structural problem in Amtrak’s condition is long-term, and is getting worse, not better.

Amtrak's Constant-Dollar Passenger Revenues and Estimated Passenger Deficits



Amtrak's Constant-Dollar Gap Between Core Expenses and Revenues



Further adding to Amtrak's deterioration is that the company's debt increased massively in the late 1990's, from $1.7 billion in 1997 to $4.8 billion in 2002 (with $3.8 billion non-defeased), without adequately increased passenger revenues to pay the debt service. Because of this increased debt, Amtrak's repayment requirements (principal and interest) are forecasted to be approximately $273 million in fiscal year 2005 (up from $111 million in 1997). Amtrak has recently suggested that the company be absolved from this $3.8 billion debt by the Federal taxpayers' assumption of all of it, as compared with the Federal appropriation covering approximately 40 percent of all Amtrak expenses the last 2 fiscal years. Amtrak would give the Federal Government nothing in return. That is unacceptable to the administration.

The fiscal year 2005 appropriation for Amtrak of $1.2 billion itself represents a 134 percent increase over the appropriation for fiscal year 2001. Amtrak's President has said that as presently configured, Amtrak cannot successfully operate through fiscal year 2006 without much larger amounts of taxpayer funds being allocated to this private company. Indeed, the increase sought by Amtrak—256 percent above the 2001 appropriation—would far outstrip the 22 percent increase in domestic discretionary spending over the same time period. For the Federal taxpayers, that is a spiral in the wrong direction.

Passenger rail is already by far the most heavily subsidized form of intercity passenger transportation. When viewed on a per passenger-mile basis, analysis by the Bureau of Transportation Statistics indicates that the aggregate Federal expenditure for intercity passenger rail is 30 times greater than for commercial aviation. Likewise, the intercity bus industry, where there are no comprehensive or dedicated Federal operating subsidies, carries as many as 350 million passengers annually (according to Eno Foundation estimates)—14 times Amtrak's ridership. (Although not comprehensive or directed, FTA, under 49 U.S.C. § 5311(f) provides for grants supporting rural intercity bus service. This grant program amounted to approximately $22 million in fiscal year 2004, which is a minor amount relative to the taxpayer burden for Amtrak each year.) So continually increased operating subsidies is not the right answer.

What is more clear now than ever is that the basic business model through which we provide intercity passenger rail service in this country—a single national entity called Amtrak—is unworkable and is not adequately positioned to respond to the changing transportation needs of this country. Massive increases in funding to merely slow a downward spiral are neither sustainable nor justifiable. At the same time, doing nothing at all will eventually result in a business failure and a lost opportunity for intercity passenger rail for this country. A change is needed.

The administration's budget request reflects the importance of reform for America's intercity passenger rail system, which Amtrak has been operating at a loss for 34 years. As noted above, Amtrak has received more than $29 billion in taxpayer subsidies, including more than $1 billion in each of the last 2 years, despite the contradicting requirements of the 1997 Amtrak Reform Act. In 2003 and again this year, the administration sent to Congress, the President's Passenger Rail Investment Reform Act. This proposal would align passenger rail programs with other transportation modes, under which States work in partnership with the Federal Government in owning, operating, and maintaining transportation facilities and services.

Deteriorating infrastructure and declining service further the case that, without congressional action on the administration's reform proposals, continued taxpayer subsidies cannot be justified. Consequently, no funding is included in the 2006 budget for Amtrak. Rather, $360 million is budgeted to allow the Surface Transportation Board to support existing commuter rail service along the NEC and elsewhere should Amtrak cease commuter rail operations in the absence of Federal subsidies. The President's budget is a serious call to action: The time for reform is now. If the administration's management and financial reforms are enacted, the administration is prepared to commit additional resources for Amtrak—but if, and only if, reforms are underway. Today is too soon to know if funding will be appropriate, or what the right amounts should be under a new model of intercity passenger rail service.

THE ADMINISTRATION'S PLAN FOR REFORM AND PRESERVATION OF INTERCITY PASSENGER RAIL

As a matter of transportation policy, the administration supports the availability of intercity passenger rail, but with a very different vision than the failed model of the past. Secretary Mineta has repeatedly set out the fundamental principles needed to reform intercity passenger rail and place this form of transportation on a sound footing. These principles are:

—*Establish a long-term partnership between States and the Federal Government to support intercity passenger rail.*—Partnerships between the States and the Federal Government for the planning, decision-making and capital investment in transportation have been one valuable element in the success of Federal programs for highways and transit to date. The States, through their multi-modal planning mechanisms, are in a much better position to determine their intercity mobility needs and which form of investment makes the most sense in meeting these needs than a sole supplier company in Washington, DC. State-supported intercity passenger rail services in places like the States of Washington, North Carolina, California, and Wisconsin have been one of the bright spots for intercity passenger rail ridership. The administration wants to build upon these successes through a new program of Federal/State capital funding partnerships in which the Federal Government would provide matching grants.

—*Require that Amtrak transition to a pure operating company*.—Amtrak today is both an operating company and the owner and maintainer of significant infrastructure that forms a key component of the intercity and commuter transportation systems of eight States in the Northeast, as well as many stations and other facilities that have local or regional transportation importance. These are two very different functions. By having them both reside in the same entity, the company is faced with conflicting priorities, which the company has found difficult, if not impossible, to balance. Infrastructure decisions have depended on Amtrak decisions, rather than those of the States and localities who are largely responsible for such planning in other transportation modes such as highways, airports, and transit. Amtrak, and the Nation's transportation system, would be better off with Amtrak able to focus on one thing—operating trains—and doing it well.

—*Create a system driven by sound economics*.—One of the flaws of the 1970 model is that intercity passenger rail has sometimes been defined by politics, habit and fear of change. That is one reason that some routes have high subsidies, such as the $466 per passenger subsidy in fiscal year 2004 on the Los Angeles to Orlando Sunset Limited. Intercity passenger rail needs to serve the markets where there is an identifiable demand that intercity passenger rail can meet. It cannot and should not try to serve every market regardless of the cost and regardless of the revenue. Just as with other transportation modes and other successful businesses in general, intercity passenger rail needs to have the dexterity to recognize changing business patterns and demand, and that sometimes the services of yesterday are not needed or justified today or tomorrow. Intercity passenger rail service needs to be designed to cost-effectively meet and support the transportation needs of the traveling public and sponsoring public authorities.

—*Introduce carefully managed competition to provide higher quality rail services at reasonable prices*.—For the last 34 years under the 1970 model, intercity passenger rail service has not been subject to the discipline of the market place. On corridor services, for example, States do not have any alternative but to have Amtrak operate the intercity service. This has resulted in a service that is more costly than one would expect in a competitive situation, and which often has not been responsive to changing transportation patterns, demands or expectations. In a free market economy, competition leads to improved cost effectiveness, higher quality and innovation, elements that have been sorely lacking in intercity passenger rail for the past generation. Transition to competition is never easy, but it is necessary for the public to get the service it demands and deserves.

—*Create an effective public partnership, after a reasonable transition, to manage the capital assets of the Northeast Corridor*.—The Washington-New York City-Boston Northeast Corridor main line is the most heavily utilized rail route in the country, forming an essential link for intercity passenger and freight transportation and commuter access to the major cities of the Northeast. By some measures, such as the number of persons per day that use this infrastructure, Amtrak is a minority user of this infrastructure—particularly in urban areas. Transportation services on this corridor need to be insulated from the unpredictable consequences of Amtrak's own finances and needs at any given time. At least initially, the ownership of these assets should be in the public sector, and management and control of this asset should reflect significant input from the States that depend on the Northeast Corridor for passenger and freight mobility.

As noted, the administration's Passenger Rail Investment Reform Act was transmitted to Congress last month. It sets out and details the administration's proposals on specific ways to achieve these objectives. After a generous transition period, intercity passenger rail would become an economically viable and strategically effective mode of transportation, supporting numerous successful rail corridors nationwide. As set out in Secretary Mineta's transmittal letter accompanying our legislative proposal, we look forward to working with Congress to discuss and fashion the specifics of legislation in ways that will successfully reform intercity passenger rail for the future.

In addition, Amtrak itself released its plan of strategic initiatives crafted by Amtrak to begin the process of reform within the company itself. That is a timely development, with many positive elements. Amtrak's own recognition of the need for reform is a welcome response to Secretary Mineta's steadfast resolve to address the problems of intercity passenger rail, and create a viable future. But Amtrak's plan would not accomplish everything needed, and legislation will be needed that achieves all of the objectives set out by Secretary Mineta and the administration.

From an appropriations perspective, it is worth noting that the administration's reform proposals would authorize funding for rail infrastructure to States rather than to Amtrak (except during a transition period). Conversely, some have asked whether it would be sensible to authorize some form of Federal bonds to support Amtrak. That would be a serious error, from multiple perspectives. It is not appropriate to issue government-sponsored or supported debt for a private corporation like Amtrak in this circumstance. Amtrak has no real ability or revenue to repay any bonds. While Amtrak can issue bonds on its own, no one would currently buy them because it lacks the incentives that discipline private issuers. In addition, Federal financing of Amtrak through any non-Treasury debt would be more costly than a General Fund appropriation supported by U.S. Treasury debt. Whatever one thinks about particular forms of bonding for transportation needs, Amtrak is a poor candidate for any such approach.

CONCLUSION

My own experience with Amtrak's Board persuades me that Amtrak itself recognizes the necessity for reform and that time is critical. It is essential that others come to recognize this, too. Without reform, Amtrak is not sustainable at its current level of funding or at any level Amtrak is likely to receive in these difficult budgetary times. Moreover, history tells us that merely throwing money at the 1970 model of intercity passenger rail without addressing the problems that have been identified in the subsequent years does not result in any long-term improvements in Amtrak's finances or quality of service.

Some people appear to assume that reform necessarily means that many areas will lose intercity rail service, but that is not necessarily so. There are other ways to run intercity passenger service and, given the chance, States are likely to try some of them and succeed at improving service and eliminating operating subsidies. The experience of the Alaska Railroad, which has done just that since the State of Alaska bought it from the government 20 years ago, is instructive. It did not change routes; it got creative about providing service based on the markets it serves. Today, the Alaska Railroad gets capital grants, but no operating assistance. It makes a profit "above the rails." One of the Alaska Railroad's innovations is to supplement its basic, year-round passenger service by seasonally hauling special first-class cars belonging to the cruise ship companies. This is the kind of creative adaptation the administration's bill envisions, but making such improvements depends upon freeing intercity passenger rail from the frozen mold of 1970. It should not surprise anyone that continuing to do the same thing that failed before 1970 has failed again.

The administration has been clear that it cannot support the failed model of the past, nor pouring more funding into that failed approach. We have been equally clear that IF meaningful reform is accomplished and implemented, the administration would support funding of infrastructure and transition needs for train operations and related costs. Although this complicates the appropriations process, we do not believe there is a basis for arriving at any "baseline level of support" for Amtrak until Congress has sent significant reform legislation to the President and it is enacted with his signature. In this regard, while the administration maintains that no funds should be appropriated for Amtrak's use in the absence of meaningful reform, any future appropriations should be subject to a variety of necessary and stringent grant conditions to ensure an improved intercity passenger rail system is achieved.

Secretary Mineta and his team look forward to working with the Congress to resolve the recurrent crisis that plagues the old model of intercity passenger rail. Thank you for the opportunity to share our perspective on Amtrak and intercity passenger rail service. I would be pleased to respond to any questions you may have.

Senator BOND. Thank you, Mr. Rosen. Mr. Mead.

STATEMENT OF KENNETH M. MEAD

Mr. MEAD. Thank you, Mr. Chairman.

You know, the appropriations committees have been doing the heavy lift for passenger rail since Amtrak's reauthorization expired in 2002. We have testified several times since then on Amtrak's high debt of nearly $4 billion, large operating losses, poor on-time performance and deferred capital investment in the billions. Amtrak seems perpetually on the edge of collapse.

We are testified again today on the same subject, but with greater urgency. As time goes by, the limp along status quo system of today comes closer to a major failure but no one knows when or where that failure will occur.

The current model is indeed broken and the reasons why go beyond just budgetary shortfalls and extend to matters like who decides on the type and amount of service. Also, other than budget cuts, the current model provides few if any incentives for cost control.

Amtrak is quite literally coming to the end of its rope, now projecting cash on hand of about $30 million at the end of this fiscal year. That will cover less than 2 weeks of Amtrak's operating expenses. And that does not take into account at all the loss off Acela services.

I have heard some discussion of the bankruptcy option, but think that would be a complex and risky undertaking. Rather, a comprehensive reauthorization that provides new direction and adequate funding is needed and is needed soon.

Reauthorization, in our opinion, ought to focus on improving mobility in short distance corridors around the country, not just in the Northeast, and in restructuring long-distance service to complement corridor service. That is going to require new relationships between the Federal Government and the States, among the States, Amtrak and the freight railroads, and also give the States greater authority over passenger rail decisions.

But in order for that to work, Mr. Chairman, a considerably more robust Federal funding program for capital with a reasonable State match is going to be required.

The administration proposal confronts several key issues straightforwardly while leaving others unanswered. We concur with the emphasis on corridor development within and outside the Northeast corridor. These are the places where the demand actually is. And we concur also with the greater decision-making power vested in the States.

Also, reauthorization should leave open the door to competition. Amtrak is the sole provider and has few incentives other than the threat of budget cuts to operate efficiently. But we are not in a position to really say whether or how many potential competitors there might be, but there should at the very least be an even playing field for competition.

Freight railroads own the track outside of the Northeast and they, too, have very legitimate interests.

But a central issue left unanswered by the administration's proposal is the level of Federal funding it supports. This has fostered, in our judgment, a perception that while the States would be given more responsibility and authority, the funding burden would fall largely on them with no corresponding commitment to significantly expand Federal funding.

To be sure, the current model's problems extend well beyond just funding matters but you are going to have to tackle the funding issue to secure anything approaching consensus.

I would like to give you our own take, Mr. Chairman, on the funding situation. For 2005, Amtrak's appropriation was $1.2 billion. In addition, Amtrak anticipates another several hundred million dollars this year in State contributions. If Amtrak receives only $1.2 billion in Federal funds in 2006, service will need to be cut almost certainly in significant ways. For 2006, passenger rail needs Federal funding between $1.4 billion and $1.5 billion plus the existing State contributions in order to move the system forward towards a state of good repair and better performance.

For 2070 and beyond, Federal funding levels between $1.7 billion and $2 billion should put you on the road to bringing the system to a state of good repair and better position the States to invest in rail corridors. That assumes the States would provide a reasonable match of 15 to 30 percent for capital grants, would cover a larger portion of operating subsidies, and that cost-saving measures in such areas as food service would be implemented.

The committee may wish to consider the following, as well. First, a perspective on long-distance trains. It is important to appreciate that while they are highly subsidized and often inefficient, their total elimination will not come close to making ends meet. Savings ultimately would be in the neighborhood of around $300 million and the savings would not be immediate due to the need for labor severance payments. Also, 23 States have only long-distance service today. And of these, 16 have little potential for corridor development in the near term.

Second, formula grants with no match required to go primarily to those States who have only long-distance service today and no real potential for corridor development in the near term and hence, would not see a capital grant program as particularly advantageous to them. Formula grants could be used to help offset the cost of service. Today we send the checks directly to Amtrak.

Third, the Federal Government brings fleet and capital infrastructure to a state of good repair in the Northeast and outside the Northeast with no match required. But thereafter, once it is in a state of good repair, the States must share in the cost of keeping it in a state of good repair.

And finally, Amtrak's high debt. Portions of this debt, which approach about $4 billion, are financed at very high interest rates. One example is 9.5 percent at Penn Station, much higher than the Treasury borrowing rate. But we currently pay the full tab anyway through the appropriations process. Consider discharging portions of that debt where it is financially advantageous to do so and, in return, take title to the Northeast corridor.

PREPARED STATEMENT

Also, I would place very heavy restrictions on Amtrak's ability to incur debt in the future.

Thank you.

[The statement follows:]

PREPARED STATEMENT OF KENNETH M. MEAD

Mr. Chairman and members of the subcommittee, we appreciate the opportunity to testify on intercity passenger rail and Amtrak. Intercity passenger rail is an important component of a balanced transportation system. Amtrak's authorization expired in 2002. In the interim, Congress has provided direction in piecemeal fashion in the appropriations process. We have testified several times since then on Amtrak's unsustainably large operating losses, poor on-time performance, and increasing levels of deferred infrastructure and fleet investment. We find ourselves testifying again today on these same subjects, but with greater urgency. As time goes on, the current limp-along status quo system comes closer to a major failure, but no one knows where or when such a failure may occur.

We reported in November 2004, that the current model for intercity passenger rail is broken. And the reason it is broken goes beyond persistent budgetary shortfalls and extends to matters like who decides on the type and amount of service, who provides service, and who selects the providers. Other than budget cuts or the threat of budget cuts, the current model provides few incentives for cost control or delivery of services in a cost-effective way.

Amtrak is quite literally coming to the end of its rope. Amtrak's most recent cash flow analysis forecasts cash on hand of about $32 million by the end of fiscal year 2005, excluding the impact from the loss of Acela service. This amounts to less than 2 weeks of Amtrak's average cash requirements. For several reasons, a bankruptcy option would be an extraordinarily complex and risky undertaking—in our opinion, one not to be relied upon if the objective is to promote a more rational and reliable national passenger rail system. In short, a comprehensive reauthorization that provides new direction and adequate funding is needed and needed this year.

A reauthorization, in our opinion, should focus on improving mobility in short distance corridors around the country—not just in the Northeast Corridor—and in restructuring long-distance services to complement corridor services. This will require new relationships or partnerships between the Federal Government and the States and among the States, Amtrak, and the freight railroads, and give the States much greater authority and control over intercity passenger rail decisions. But, in order for this to work, a considerably more robust Federal funding program for capital, with a reasonable State match will be required, along with additional State contributions.

The administration's proposal recognizes that the current model is broken and confronts several key issues in a straightforward way, while leaving others less clear or unanswered. We concur with the emphasis on corridor development within and outside the Northeast Corridor—these are the places where the demand is—and we concur as well with the greater decision-making powers given the States.

Also, reauthorization should leave open the door to competition. Amtrak is the sole provider of intercity passenger rail service and, as such, has few incentives, other than the threat of funding cuts, to operate more efficiently. While we are not in a position to say how many, if any, potential competitors there might be, there needs to be a level playing field to promote competition, and consideration must be given as well to the legitimate interests of the freight railroads who own the rail infrastructure outside the Northeast Corridor.

Left unanswered by the administration's proposal, however, is a central issue, most notably the approximate level of funding it supports. This has fostered a perception that while the States would be given more authority, the funding burden for operating losses would fall largely on them, with no corresponding commitment to significantly expand Federal capital funding. The debate on reauthorization would be much better informed if the administration's bill spelled out Federal funding levels with greater clarity. We fully recognize that the problems of the current model extend beyond matters of money, but funding levels are an integral part of any solution and in reaching consensus.

Our own take on the funding issue is as follows. In fiscal year 2005, Amtrak received a Federal appropriation of $1.2 billion. In addition, Amtrak anticipates $140 million in State contributions for operating costs and $200 million for capital projects. In effect, Amtrak had access to funds totaling about $1.5 billion. This level of funding is not sufficient to make progress toward achieving a state of good repair.

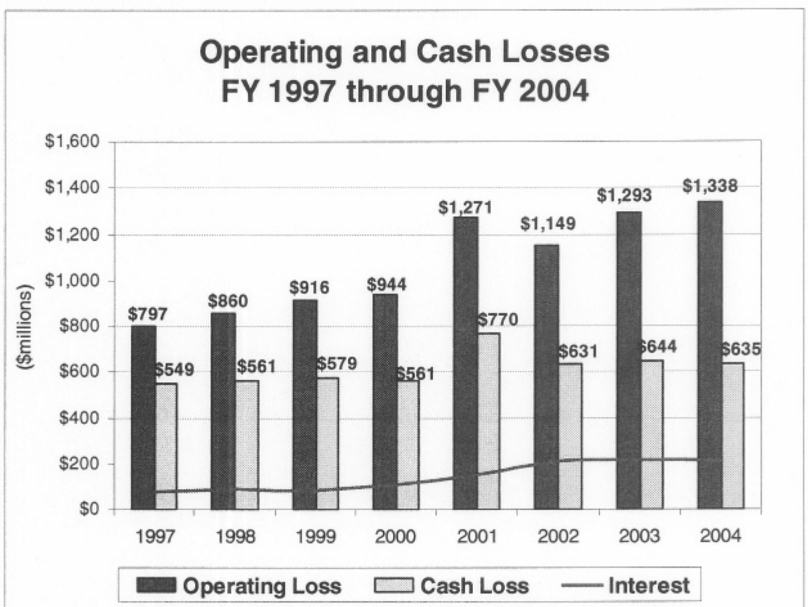
If Amtrak receives only $1.2 billion in Federal funding in fiscal year 2006, even combined with expected State operating and capital contributions, it will likely continue to defer needed capital investment and will need to cut services. Intercity passenger rail needs Federal funding between $1.4 billion and $1.5 billion, plus existing state contributions, in order to maintain the status quo as we know it today. However, this level of funding would not be sufficient to move the system to a state-of-good-repair, let alone permit investment in new corridor development.

For 2007 and beyond, Federal funding levels between $1.7 billion and $2.0 billion would put us on the road to bringing the existing infrastructure and fleet to a state-of-good-repair and better position States to use Federal funds plus their own revenues to invest in rail corridors. This assumes that States would provide a reasonable match of 15 to 30 percent for capital grants and would cover a larger portion of operating subsidies and that Amtrak would implement cost saving measures in such areas as food and beverage service.

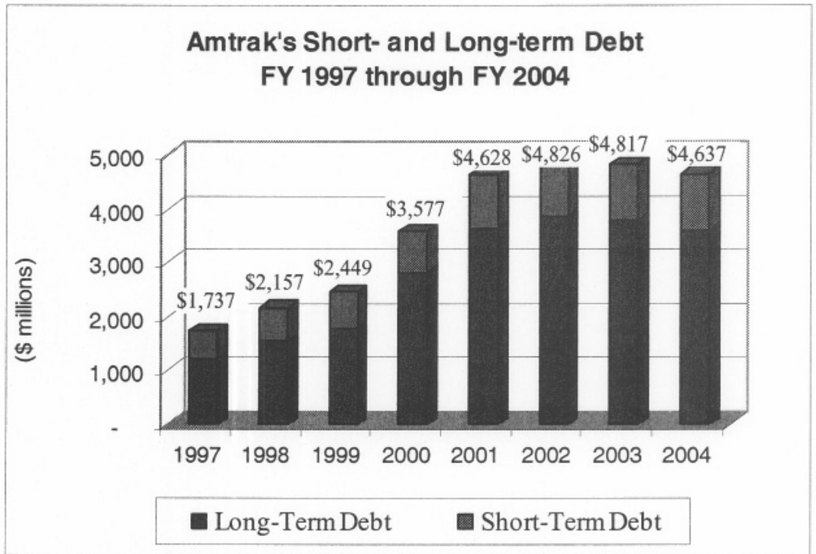
CURRENT MODEL IS BROKEN, RESULTING IN SEVERE FINANCIAL INSTABILITY AND DECLINING SERVICE QUALITY

Despite multiple efforts over the years to change Amtrak's structure and funding, we have a system that limps along, never in a state-of-good-repair, awash in debt, and perpetually on the edge of collapse. In the end, Amtrak has been tasked to be all things to all people, but the model under which it operates leaves many unsatisfied. Consider the following:

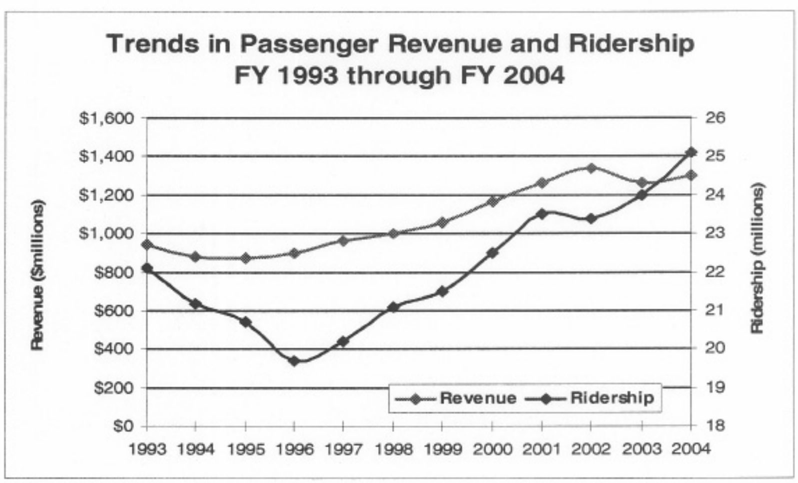
—Amtrak is in a precarious financial condition. Its system continues to suffer operating losses on all but a handful of routes. Losses on some long-distance trains (excluding depreciation and interest) exceed $400 per passenger. For the last 6 years the average annual cash losses have exceeded $600 million. The growth in cash losses since fiscal year 2000 is primarily attributable to rising interest expense.



—Amtrak is carrying a large debt burden. Its total debt grew 178 percent between fiscal year 1997 and fiscal year 2002, although it has declined slightly in the past 2 years. For the foreseeable future, Amtrak's annual debt service payments will approach $300 million.

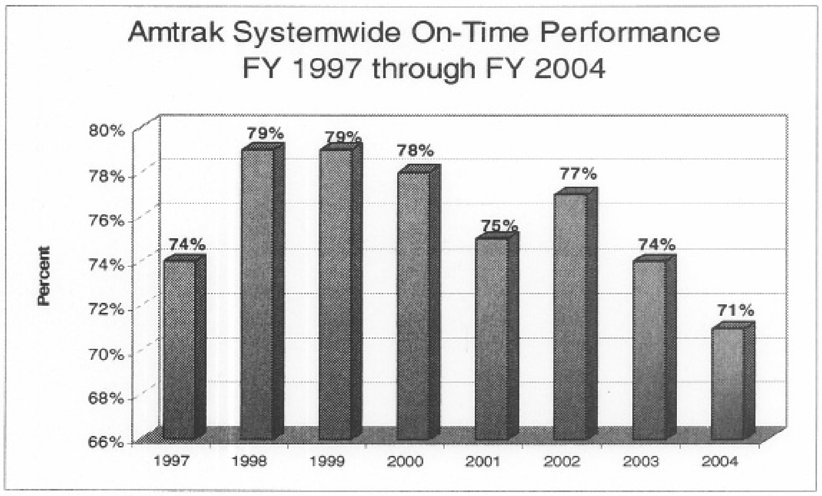


—While ridership increased to 25.1 million in fiscal year 2004, passenger revenues were $1,304 million, below the $1,341 million achieved in 2002, due primarily to fare pressures. For the first 6 months of fiscal year 2005, passenger revenues were $7.4 million lower than the same period in fiscal year 2004.



—Amtrak has an estimated $5 billion backlog of state-of-good-repair investments, and underinvestment is becoming increasingly visible in its effects on service quality and reliability. Deferred capital investment has led to several system failures in recent years, including a failure of a key 12-kilovolt electric cable during the August 2003 northeast power blackout; fallen overhead power lines (catenary) on the line between New York and New Rochelle; and broken bolts on the Thames River bridge in Connecticut. No one knows where or when a critical failure will occur, but continued deferral of needed investment increases the risk that it may not be too far away.

—Further, on-time performance fell from 74 percent in fiscal year 2003 to 71 percent in fiscal year 2004, with even Amtrak's premier service—Acela Express—achieving on-time performance of only 74 percent. On-time performance for long-distance trains averaged less than 50 percent. Last year, the poorest performing train, in this regard, was the Sunset Limited, with an on-time performance of only 4 percent.



Today, Amtrak's corridor trains outside the Northeast Corridor, based on current schedules, average 48 miles per hour and long-distance trains average only 46 miles per hour. These speeds reflect scheduled time and overstate the lower actual speeds due to delays. Deteriorating infrastructure and increasing freight and commuter rail congestion will continue to impact on-time performance.

BANKRUPTCY IS NO SUBSTITUTE FOR REAUTHORIZATION

A rail bankruptcy is an extraordinarily complex and risky procedure, and we cannot predict how the passenger rail system would emerge from bankruptcy. An Amtrak bankruptcy is no substitute for reauthorization. In our opinion, this is not an option to be relied upon if the objective is to promote a more rational and reliable national passenger rail system.

—*Labor Costs*.—Labor negotiations are outside the bankruptcy process. In a non-railroad bankruptcy, the bankruptcy court can cancel or change collective bargaining agreements, which some airlines successfully used as leverage when re-negotiating with their unions. In a rail bankruptcy, the Trustee would have to negotiate with Amtrak's unions under the Railway Labor Act.

—*Cash Crunch and Infrastructure Needs*.—Amtrak's cash crunch would be exacerbated in bankruptcy. Once in bankruptcy, vendors often demand cash or provide credit under stringent terms. As a result, absent a Federal cash infusion, there is a possibility that major assets such as Penn Station and the Northeast Corridor would need to be sold or remortgaged to raise cash to sustain operations. Meanwhile, the value of the Federal Government's mortgages on these properties would be diluted, and the infrastructure would continue to deteriorate.

—*Public Interest*.—Once in bankruptcy, a federally appointed Trustee would direct and manage Amtrak. The Trustee must consider the "public interest," which has generally been broadly interpreted as continued operations of the railroad, but in what fashion would clearly be left up to the Trustee, which might not be the best solution or a solution that the reauthorizers would prefer or what the States would prefer. For example, in order to continue operations, the Trustee may need to shut down various State corridors or long-distance service to stop the bleeding of cash and operating losses.

ELIMINATING LONG-DISTANCE SERVICE WILL NOT SOLVE THE FUNDING PROBLEM

Long-distance service has sparked widespread controversy, in part, because of its heavy subsidies. In 2004, long-distance trains cumulatively incurred operating losses of more than $600 million (excluding interest and depreciation). In fact, the loss per passenger exceeded $400 on two of these trains—Sunset Limited and Southwest Chief. Eliminating long-distance service reduces operating losses associated with long-distance trains by about half (or $300 million) but will not make Amtrak profitable.

Because long-distance trains share stations and facilities with corridor trains, eliminating the long-distance trains would not eliminate the shared costs. In addition, Amtrak allocates a share of overhead and infrastructure maintenance to the long-distance trains—some of these costs will be reallocated to all remaining trains. For example, we estimate that $300 million or more in shared and system costs would be shifted to other corridor trains. Thus, the expected net savings are only about $300 million. However, these savings would not be immediate. In fact, in the first year, it may cost Amtrak more to eliminate the service than to operate it because of its labor severance payouts (commonly called C–2).

Long-distance trains represent about 15 percent of total intercity rail ridership. However, many long-distance riders do not really travel long distances. That is, long-distance trains carry only a small number of end-to-end riders. Of the 3.9 million long-distance riders in fiscal year 2004, only 527,000 rode the entire length of the route and another 403,000 rode between city pairs also served by existing corridor service. The remaining 3 million riders traveled along portions of the route. These trips mostly ranged from 500 miles to 700 miles—slightly longer trip lengths than corridor riders.

While eliminating long-distance service may seem appealing from a Federal budgetary standpoint, especially with the large deficits, it ignores the mobility needs of rural areas of the country and the benefits passenger rail provides. Amtrak provides long-distance service in 41 States and is the only intercity passenger rail service in 23 of those States. The questions of whether to provide long-distance service, who makes those decisions, and who funds the losses are critical policy decisions that will need to be made.

WHERE DO WE GO FROM HERE? REAUTHORIZATION GUIDANCE IS ESSENTIAL

The “limp along” approach is costly and leaves many unsatisfied. The current model for providing intercity passenger service does not leave the States in a position to decide upon the best mix of service for their needs—what cities are served, schedules and frequency of service, and service amenities. The model provides little balance between the national goals of an integrated network and regional and State transportation needs. How much funding and who provides the funding—Federal, State, or a combination—are also critical questions that need to be addressed. In providing reauthorization guidance, some core elements need to be considered in determining how passenger rail is funded and delivered, specifically, deciding the levels and mix of Federal and State funding, achieving a state-of-good-repair in the Northeast Corridor, determining the appropriate framework to integrate competing demands of infrastructure and operations in the Northeast Corridor, and paying off Amtrak’s legacy debt.

In our opinion, a new model for intercity passenger rail should also include several important aspects. The first is that funding and governance build in incentives for cost cutting. Specifically, eliminating direct subsidies to Amtrak, or any other operator, and channeling funds through the States will likely promote more cost control because an operator will need to better justify costs in order to retain an operating contract. In addition, it will encourage States to maximize efficiency by keeping their own costs to a minimum. Second, the introduction of private competition into the management and operation of intercity passenger rail services will exert additional market pressures on operators to provide cost-effective, higher quality service.

ADEQUATE FEDERAL AND STATE FUNDING SHOULD BE PROVIDED IN ORDER TO RESTORE THE INTERCITY PASSENGER RAIL SYSTEM AND INVEST MEANINGFULLY IN CORRIDOR DEVELOPMENT

Federal funding levels, along with State contributions, have not been sufficient to subsidize operations, address deferred capital needs, and significantly improve service along the existing rail network. In the last 2 years, Amtrak has received annual Federal funding of $1.2 billion. This amount was supplemented by operating and capital contributions from State and local sources—in fiscal year 2004 these were

$135 million and $114 million, respectively. In effect, Amtrak received about $1.45 billion in public funds.

It will require at least $2 billion in funding from all sources to begin any meaningful corridor development. The policy challenge is determining who pays for what portions of the system. Federal funding of $1.4 billion to $1.5 billion would not provide sufficient funding to maintain a 5-year program for restoring the system to a state-of-good-repair. Projects in both the Northeast Corridor and in the corridors and long-distance routes outside the Northeast Corridor would continue to be deferred. This simply maintains the limp-along status quo.

One approach to promote adequate Federal and State funding could be to use a variety of grant programs similar to those used in aviation, transit, and highways that place funds in the hands of States. These programs are based on a combination of Federal/State matches and formula grants. More specifically:

—*Capital Grants With a Reasonable Match*.—Like the administration's proposal, this approach would provide capital grants on a competitively determined basis and would be administered by the Department of Transportation (DOT). States that desire to improve existing intercity rail service and/or develop new corridor services would apply to DOT for a matching grant, similar to the Federal Transit Administration's New Starts Capital Program. The administration's proposal also suggests such a program but provides a 50/50 capital match rate by the end of the reauthorization period. Our view is that a lower State match rate requirement would provide incentives for States to take an "ownership" role in developing rail corridors on a more competitive basis with other transportation modes (historically, highways and transit have used an 80/20 match rate).

To accommodate the need for different types of capital investments, two types of capital matches could be established. For investments that qualify as traditional capital investment, such as track or purchases of passenger equipment, the Federal share could go up to 80 to 85 percent. On the other hand, for investments that qualify as capital maintenance (for example, those under the transit definition) the Federal share might be 70 to 75 percent.

—*Formula Grants With No Match Required*.—This approach provides funds to States outside the Northeast Corridor that do not have corridor development potential and that rely on long-distance trains for substantially all intercity passenger rail service. By discussing this approach, we are not taking a position on the ultimate policy of whether long-distance service should be retained or eliminated but merely presenting it as an approach for funding States that do not have the population densities to support corridor development. There are at least 16 States with only long distance service and little potential for any corridor development. These States are unable to take advantage of the matching capital grants for corridor development.

This approach could initially include sufficient funds to subsidize existing long-distance and corridor services. Over the reauthorization period the funds associated with corridor services would be reduced and then eliminated at the end of the period. Further, we expect the level of Federal funds subsidizing the long-distance services would be reduced to reflect greater operating efficiencies resulting from capital investments as well as other savings resulting from food and beverage service changes, improved labor productivity, and efficiencies that may be introduced by competitive service providers.

As determined by the States, funds could be used to defray the cost of operating subsidies, capital investment, or both, with no match required. The amount of the formula grant could be calculated on the basis of Amtrak's fiscal year 2005 operating loss allocable per embarking/disembarking passengers in the affected State or some other formula that provides an equitable allocation.

—*Restore Northeast Corridor to a State-of-Good-Repair*.—The Northeast Corridor presents a difficult challenge. The funding priority for the Northeast Corridor reflects the accumulated deferral of investments which has resulted in an estimated $5 billion backlog of capital projects, threatening current and future service reliability. The effects of the deteriorating infrastructure are readily evident. For example, Amtrak's reported on-time performance in the Northeast Corridor as a whole between 1994 and 2002 ranged from 82 to 89 percent. In fiscal year 2003, it dropped to about 80 percent. For fiscal year 2004, even Amtrak's premiere Acela service posted an on-time performance of only 74 percent, far short of Amtrak's stated goal of 94 percent. If the decision were made to keep the current Northeast Corridor intact, we estimate Amtrak would need to spend about $550 million annually for an extended period on infrastructure and rolling stock to eliminate the backlog of capital investment in the Northeast Corridor.

Bringing the eight Northeast Corridor States and the District of Columbia together in a short period of time to direct and manage this effort is incredibly complex but may be achievable by the end of the reauthorization period. Recognizing this challenge, one option during the reauthorization period could be for the Federal Government to fully fund the Northeast Corridor's capital requirements until a state-of-good-repair is achieved. This would also address the States' reluctance to inherit a legacy system they did not create. We suggest that DOT distribute funds directly to the Northeast Corridor infrastructure manager separately from the competitive grant process.

Construct for 5-Year Reauthorization Funding

Congress and the administration have a difficult decision to make in determining the appropriate level of funding for intercity passenger rail. The level of funding can obviously vary. We have been giving this some thought and would like to present a construct for consideration. We recognize that many assumptions need to be made about who pays for what and how to balance national, regional, and State transportation needs. Those are decisions for Congress and the administration to make.

In building this construct, we made several assumptions for purposes of illustration as follows.

—Formula grants will not fully cover train operating losses. Amtrak's forecast net cash operating needs (excluding interest) were used as the starting point. The levels of funding represent imputed cost savings of 10 percent per year from a combination of revenue growth and operating cost savings.

—Over the 5-year reauthorization period, Federal subsidies decline for long-distance trains and corridor operating subsidies shift to the States. We expect States to place higher performance and efficiency demands on the service provider to lower operating costs to more affordable levels.

—Debt service is based on Amtrak's projected debt service payments through fiscal year 2009, adjusted for installment payments on their RRIF loan and possible early buyout options on leased equipment.

—Capital requirements to restore the system to a state-of-good-repair are based on Amtrak's Strategic Plan for fiscal year 2005 through fiscal year 2009 and on assumptions we made on allocating capital needs between the Northeast Corridor and the rest of the system. The funding allocation assumes a capital need of $550 million for infrastructure and fleet in the Northeast Corridor and $250 million for infrastructure and fleet outside the Northeast Corridor.

—Funds available for capital match represent funds remaining after state-of-good-repair funding requirements, formula grants, and debt service are met.

CONSTRUCT FOR REAUTHORIZATION FUNDING

[In millions of dollars]

Federal Contributions	Fiscal Year 2005	Fiscal Year 2006	Fiscal Year 2007	Fiscal Year 2008	Fiscal Year 2009	Fiscal Year 2010
Formula Grants (Capital and/or Operating Subsidy)	570	570	510	460	410	370
Debt Service	276	278	358	306	308	375
Capital to Restore System State of Good Repair	355	655	755	800	800	800
NEC Infrastructure + Fleet[1]	300	525	550	550	550	550
Non-NEC Infrastructure + Fleet	55	130	205	250	250	250
Subtotal	1,201	1,503	1,623	1,566	1,518	1,545
Available Capital for Match	....	....	27	234	432	455
Total Federal Contributions	1,201	1,503	1,650	1,800	1,950	2,000

[1] NEC: Northeast Corridor.

New Federal capital available for State match does not become available until annual Federal funding levels reach $1.65 billion. This construct highlights the policy choice that needs to be made between restoring the system to a state-of-good-repair and investment in new corridor development. At $2 billion, we would expect about $455 million to be available to States to match for use in new and/or improved corridor development.

TOO PREMATURE TO SEPARATE MANAGEMENT OF NORTHEAST CORRIDOR INFRASTRUCTURE FROM OPERATIONS

Proposals to separate the Northeast Corridor infrastructure management and operations into two independent companies present a level of complexity and risk that needs a more thorough examination. At some point down the road, this split might be feasible and may prove a better way of controlling costs. However, at this juncture, not enough is known about the benefits and risks of this proposal. As we witnessed in Great Britain's experience, there are risks associated with establishing a commercial, for-profit entity to operate the infrastructure. Allowing an infrastructure company to operate "like a business" may mean relinquishing control over how certain expenses are cut or which capital investments are made. An infrastructure company focused on its bottom line has incentives to make decisions that are in its financial best interest but may not be in the best interest from a safety or efficiency perspective for the operator. The result could be, at best, disruption to service and a decline in on-time performance and, at worst, compromised safety conditions.

Aside from the risks of separating the infrastructure from operations in the Northeast Corridor, there are benefits to the integration. In particular, an integrated Northeast Corridor provider of track maintenance, capital programs, operations, and dispatching is likely to be more efficient and less costly than two providers, each having a separate organizational support structure. In addition, a bifurcated approach would require a fully functional oversight and control organization at the outset lodged in the Northeast Corridor compact or the DOT to coordinate between operations and infrastructure. If formation of the Northeast Corridor compact is delayed, there could be disruptions to the operation of the corridor.

It may be possible at some point down the road to develop a model where all interests are best served, but a more thorough review and understanding of lessons learned from other similar attempts would be a valuable precursor to such a division in the Northeast Corridor.

PAY OFF LEGACY DEBT AND RESTRICT FUTURE BORROWINGS

As of September 30, 2004, Amtrak had long-term debt and lease obligations of about $3.8 billion with amortization periods extending beyond 20 years. Amtrak's balance sheet shows $845 million in escrowed proceeds to defease a portion of this debt, leaving close to $3 billion in unfunded long-term debt or lease obligations. Under the current model, these obligations are paid for with Federal appropriations. Because portions of Amtrak's debt were financed at higher interest rates than what the Federal Government can borrow, Congress and the administration should consider a one-time appropriation for the specific purpose of discharging any debt that can benefit from the Federal Government's borrowing power, producing long-term Federal savings. For example, Amtrak pays 9.5 percent interest on its mortgage obligation for Penn Station, New York, whereas recent 10-year Treasury notes issued by the Federal Government are yielding a little over 4 percent. In addition, Amtrak's ability to incur long-term debt should be restricted, except for refinancing opportunities that lower interest expense and do not increase the outstanding principal, and no commitments should be made without advance approval by the Secretary of Transportation. In return for discharging Amtrak's debt, title to Amtrak's assets would transfer to the U.S. Government.

Mr. Chairman, that concludes my statement. I would be happy to answer any questions at this time.

Senator BOND. Thank you very much, Mr. Mead.

I apologize for being jumpy but I am going to have to get back to the Highway Bill and I want to ask essentially two broad questions and then turn it over to my colleagues to run this.

First, let me say that when I was governor of Missouri, I started the process of subsidizing Amtrak, convinced by the silver tongue of now Senator Bennett. And Missouri now subsidizes Amtrak at $6.2 million a year, which is behind Illinois, Washington and several other States. And we have a very modest $32 loss per passenger, which it is certainly not quite the best looking one in the whole ugly bunch but it is up there.

Let me ask Mr. Laney and Mr. Mead and others to comment. While we are waiting for the Commerce Committee to act, and I gather your reorganization and restructure has go through the Commerce Committee, we cannot reauthorize in this committee. You are going to have to get it through there.

If Congress does what Congress sometimes does, and that is nothing, would you go bankrupt this year? What would be the prospects of trying to restructure Amtrak in bankruptcy? Mr. Laney?

BANKRUPTCY

Mr. LANEY. Bankruptcy presents an enormous set of challenges and complexities that we have not worked through from start to finish and it is much less flexible in the railroad context than it is in a normal business context.

Nonetheless, we have considered it because of the proposed zero budget from the administration, and DOT.

Senator BYRD. I am having difficulty hearing Mr. Laney. Could we have some way of making it louder?

Senator BOND. Can you pull that up a little closer?

Mr. LANEY. I thought I had run out of funds and you turned off the electricity.

It is an enormous challenge and really limits our flexibility. We have considered it. We do know that without any action by Congress that sometime, my guess is in the first quarter to the first half of fiscal year 2006—and Mr. Gunn may disagree with me and may think it is earlier—depending to some extent on the ultimate impact of the Acela problems right now, that we will in effect run out of cash.

Senator BOND. Can you restructure in bankruptcy or do you have too many costs?

Mr. LANEY. It is totally out of our control in bankruptcy. It is a different structure. There is a U.S. trustee appointed and he, with proposals from DOT, selects someone, in effect, to run Amtrak in bankruptcy.

Senator BOND. Mr. Mead.

Mr. MEAD. Pursuing the bankruptcy approach, in my opinion, is like taking a round peg and trying to pop it through a square hole. The reason why is most people, when you go through this type of bankruptcy, you want to emerge with something that is better or more rational. But you are going to need cash to do it.

The short answer, as I said in my statement, you are going to have $32 million at the end of this year. That is 2 weeks. You are not going to have much cash.

The second, big reason, very unlike the airlines. In bankruptcy for railroads, the labor issues, labor contracts which comprise over 40 percent of Amtrak's budget, they are handled on a totally separate track. They do not go to the Bankruptcy Court, they go to special labor boards.

I do not know if that separate track is going to work very well.

Senator BOND. Do you have a comment on that, Mr. Rosen or Mr. Gunn?

Mr. GUNN. I will agree with my chairman.

Senator BOND. Always a good idea.

Mr. GUNN. But I do think the problem of the threat of bankruptcy is very imminent, given the Acela problem.

Mr. ROSEN. Senator, the only thing I would like to say about that is the preferred course of reform is clearly legislative through the Commerce Committee and in other ways, as well as board actions. I think it would be a mistake for anybody to believe that any approach should be off the table, depending on how events unfold, and that there are airlines that are operating in bankruptcy as we speak today.

And clearly, one of the questions in a bankruptcy that anybody would be interested in is what would the service look like? How would it continue?

And so I do not mean to have this misconstrued to saying that is the preferred option, but I think the complexities of bankruptcy are things that there is some experience with.

Senator BOND. Mr. Rosen, excuse me. I want to ask one big question. Mr. Mead finally referred to what I believe is the 900 pound gorilla in the room. When I talk to my colleagues, the one thing they ask about are what some perceive to be unreasonable labor costs. People talk about 3- and 4-hour workdays, work weeks that are significantly less than 40 hours. What are the impacts? Are the labor costs of Amtrak out of line with other transportation companies and organizations?

I would ask Mr. Mead, Mr. Rosen, Mr. Laney and Mr. Gunn to comment on it. Mr. Gunn.

LABOR ISSUES

Mr. GUNN. I will start. I think if you look at Amtrak's labor situation, first of all, we have made a lot of progress tightening up the operation. As Mr. Laney said, we have dropped our head count from 24,800 to about 19,500. And at the same time we are running more trains and handling more passengers and doing a lot more maintenance work.

The basic problem we have, I think, revolves around some of the work rule issues that we have. I think that if you look at our rates of pay on, for example, locomotive engineer or machinist, the rates of pay are not the problem for those groups of people. The problem is work rules.

To give you a sense of what it means to us, these are probably between 700 and 1,000 people on the payroll that would not be there if you had control over crew consist and if you did not have the shops organized around crafts.

Senator BOND. Is it true that traveling from St. Louis to Kansas City they have to change crews in Sedalia?

Mr. GUNN. I do not know the crew change point on that train right now but——

Senator BOND. It is a 4-hour trip and at one point there was a crew change.

Mr. GUNN. On the Northeast Corridor we get a full day's work out of a crew. I think what they are doing on that is the crew probably takes the train and goes back home. In other words, they swap trains.

To give you a sense of this, an engineer in the Northeast Corridor, a day's work, they come to work in Washington, they go to New York, they have a break, they get back on a train and bring it back to Washington. That is a fairly full day's work.

If we have the frequencies and so forth, we get a day's work out of our train crews. The problem is we may have more people on the train than we need. That is the problem. It is not the basis of pay. That is my opinion.

Mr. MEAD. I think the labor rates are not out of line with what rail people would normally get. But I do agree with Mr. Gunn, that the work rules really do inspire a lot of inefficiencies. Plus, any organization where your ticket sales are exceeding—where your labor costs are exceeding your ticket sales is a prescription for problems. That is the case we have here.

Mr. ROSEN. The only thing I would add is that the difficulties that Amtrak faces go well beyond their labor difficulties.

Senator BOND. Mr. Laney, any comment on that?

Mr. LANEY. No, Senator.

Senator BOND. Thank you very much, gentlemen. I would have to say that to gain support on the floor, I think that the reorganization and restructuring plan may have to address the work rule question because there are a number of people who are reluctant to support anything for Amtrak until that is done.

With that, I turn now to Senator Murray.

Senator MURRAY. Mr. Chairman, I intend to be here for the duration of the committee and Senator Byrd wanted a chance to do a statement and he had another obligation. So I will let him go ahead of me on this round.

STATEMENT OF SENATOR ROBERT C. BYRD

Senator BYRD. Senator Murray, I thank you. You are very gracious.

Mr. Chairman, I thank you for holding this hearing.

I will speak today about the millions of Amtrak passengers who board in stations like Montgomery, West Virginia; Greenwood, Mississippi; Winslow, Arizona; and Cut Bank, Montana.

I recognize that Amtrak has problems. Amtrak provides crucial transportation services, not just for our major cities, but for millions of people across rural America. They pay the taxes that fund infrastructure in Iraq. They help to supply the men and the women from whose veins flow the blood that is shed in the deserts of Iraq. They need service. They are Americans, too.

It is perhaps those citizens who have the most at risk in losing rail service as a result of the Bush Administration's budget. Once those towns fall off the national rail map, they are not coming back.

Mr. Mead points out that many riders of Amtrak's so-called long-distance trains do not really travel long distances. We are talking about passengers who might be riding from Martinsburg, West Virginia, to Pittsburgh, Pennsylvania, on Amtrak's Capitol Limited, or passengers who may be traveling from Hinton, West Virginia, to Maysville, Kentucky, on The Cardinal.

For residents of those communities, Amtrak provides an essential transportation option. Not every grandmother can just get behind the wheel and drive to see her grandchildren. Not every college student has the option of driving home from school for the Easter recess. There are over 120 communities across the Nation that receive regularly scheduled Amtrak service but have no commercial air service whatsoever. Several of these communities have also seen their bus service eliminated as a result of the shrinking of the national Greyhound network.

The administration does not seem to grasp the transportation needs of rural America. Not only does its budget propose to eliminate all subsidies to Amtrak, the administration's budget also proposes to cut in half funding for the Essential Air Service program, causing dozens of communities across the Nation to lose their guaranteed air service.

These budget proposals appear to be consistent with many other provisions in the President's budget that do real harm to the quality of life in rural American communities.

The President's budget includes deep cuts for rural housing loans, and for water and sewer grants that help rural communities have clean water. The President's budget eliminates funding for vocational education grants that help students in rural America who are not going on to college but who need training to get a job that pays a livable salary.

When it comes to the President's budget for Amtrak, we are not talking about just another proposal to cut a program by 10, 20, or 30 percent. We are talking about a proposal to eliminate all of Amtrak's Federal funding and all of Amtrak's available services.

I should point out that, just 2 months ago, I tried to rectify this situation when the Senate debated the budget resolution for the coming fiscal year. On March 15, I offered a bipartisan amendment, with Senator Specter and several other Senators, which sought to boost Amtrak funding to $1.4 billion for 2006. I did not take that funding figure out of thin air. When President Bush submitted his budget request last year for Amtrak, $1.4 billion was the level that he, himself, included in his budget for 2006.

As I stated on the floor during debate on that amendment, the elimination of Amtrak's subsidy, as called for under the President's budget, is not a recipe for a streamlined railroad. It is not a recipe for a more efficient railroad. It is a recipe for a dead railroad.

My amendment sought to bring that railroad back to life as part of the budget for the coming fiscal year. Unfortunately, that amendment failed on a vote of 52 to 46. So, unfortunately, a dead railroad may very well be what we get from the coming fiscal year.

I have been fighting for Amtrak for a long time, Mr. Gunn, Mr. Rosen, for a long time. I was hopeful of landing a rail passenger route in southern West Virginia 30 years ago. In 1974, I had proposed to the Appropriations Committee, Subcommittee on Transportation, that we add money to Amtrak's budget to help bring this about. On April 11, 1974, in a hearing conducted by the Transportation subcommittee, which I chaired at the time, Roger Lewis, then-president of the National Rail Passenger Corporation, Amtrak, told me that $4 million would provide adequate funding to begin a route through southern West Virginia. The route that I had been trying to secure would run from Norfolk, Virginia, to Cincinnati, Ohio, with stops in West Virginia at Bluefield, Welch, Williamson, Fort Gay, and Kenova. I told Mr. Lewis that I would add the $4 million by offering an amendment to the Transportation Appropriations bill.

In answer to my questions, Mr. Lewis said that he anticipated no problem in securing the cooperation of the railroad. He also said that this amount of money would provide adequate funding to initiate capital improvements and initial operating costs for the operation of Amtrak on a new route from Norfolk to Cincinnati.

According to Mr. Lewis, N&W tracks could be used all the way; or, as an alternative, both N&W and C&O tracks could be used. In any event, repairing tracks and rebuilding passenger facilities along the route, Mr. Lewis explained, could be accomplished within 6 months if the railroad labor forces were available and if the N&W Railroad was willing to undertake that program.

On April 24 of that year, 1974, the Transportation Appropriations Subcommittee accepted my amendment, adding $4 million to the Transportation Appropriations bill to provide Amtrak rail service between Norfolk, Virginia, and Cincinnati, Ohio, and on April 30, the full Appropriations Committee approved my amendment.

Then, on March 24, 1975, 30 years ago, the Mountaineer, a new Amtrak passenger train, made its inaugural run in southern West Virginia.

Mr. Gunn, the Amtrak president at that time was Paul Reistrup. He and I were among the passengers on the maiden run. On its daily runs from Norfolk, Virginia, to Chicago, Illinois, the train would stop, as I have already indicated, at Bluefield, Welch, and Williamson in West Virginia, and would be made up of two coaches, a snack/diner, a sleeper, and a baggage car. A guaranteed operation of 2 years for the new route through southern West Virginia had been made by Amtrak.

Mr. Reistrup said that the Mountaineer would habitually lose money and that the run would lose $4.5 million in each of the first 2 years of operation, while taking in only $900,000 in the first year.

I had been instrumental in making the Mountaineer a reality by securing an appropriation of $4.6 million, which was reduced to $2 million in the Senate/House conference. That was an experimental run, and its continuance beyond the 2-year experimental run would depend upon the ridership achieved.

The Mountaineer did not last all that long. I was also instrumental in getting The Cardinal. Amtrak still serves West Virginia, the only State among the 13 in Appalachia that is wholly in the Appalachian regional system.

Unfortunately, a dead railroad may very well be what we get for the coming fiscal year. That would all depend, perhaps, on whether this subcommittee can find the resources to meet Amtrak's needs next year.

Mr. Chairman, I thank you for being a good chairman. I hope that we can come to the aid of Amtrak. We have people down there, people who pay taxes, whose sons and daughters die in the unnecessary war in Iraq, and who pay taxes to build the infrastructure in Iraq. Perhaps, we ought to have Amtrak in Iraq. Maybe we could get more money for it, even though it would lose money. That would not be a question over there, I suppose.

I recognize the problems. I want to help. I, for one, plan to work with my colleagues as best as we can to accomplish that goal.

In closing, I thank my leader on this issue, Senator Patty Murray, for her diligence and dedication to her work in providing the rail passenger service to people like those who have sent me to Washington for eight terms. I fought for them before, and I am going to fight for them now.

Thank you, Mr. Gunn, for your services. Thank you very much. You are trying hard, and I want to work with you.

Senator Murray, the challenge will be considerably greater due to the failure of the Senate to adopt my amendment a while back.

Now, when Cicero spoke, the people said he makes a good speech. But, when Demosthenes spoke, they said let us go against Philip. So, Mr. Chairman, let us go against Philip. Let us go against Philip, Mr. Gunn. Do not lose heart. It is going to be a problem. It is going to be hard work. I will tell you this, people in the rural areas of this country vote, too. Thank you very much.

Senator BURNS [presiding]. Thank you, Senator Byrd. I think I am next on the list here, and I will kind of open up this morning.

I also serve on the Commerce Committee. We have looked at this Amtrak thing for the last couple of years and we have drawn some conclusions from the testimony of Mr. Mead and Mr. Rosen, and then a short visit over here with my good friend from Utah.

We are going to have to be very imaginative if we make this thing work. But we cannot be imaginative if we are not a part of the overall transportation plan of this country and it does not sound like that has been the case.

I am going to be very critical of the Department of Transportation now. You say reforms but I have not seen anybody knocking on my door up here, saying we have got these reforms that we think would work for Amtrak or a national transportation plan. We have not heard that. I have had no request for an appointment to come up and say we should look at this because we think it is a vital part of the overall plan of this country.

And I aim to take this to the Secretary. We cannot expect any kind of imagination to flow unless we get some cooperation down there. Or, if it is not on the radar screen, tell us it is not on the radar screen and we will do something else. We will put it over in another department. Let's put it over in the Department of Defense because we might want to move some troops one of these days. Who knows?

We can sure get it out of here if it is not a priority.

Mr. Rosen, am I incorrect in that statement? What is your take on that?

Mr. ROSEN. Senator, let me first say I would be more than happy to be with you at any time or your staff, of course. So let me put that to the side.

But we have been working with the committee staff and have had a number of consultations. And as you know, I did testify before the Commerce Committee on April 21, both written testimony and oral testimony. The administration's bill was transmitted by the Secretary, I want to say the first week of April. It is substantially similar to a bill that was submitted previously, in 2003. My predecessors, as the Secretary's designee to the Amtrak board, each testified about that bill, Michael Jackson and Alan Rutter.

So I think there has been consistent efforts by the Department to explain, lay out, discuss the administration's reform concepts. But I hear you and we can certainly do more and better. And I would like to work with you.

Senator BURNS. It is going to take that kind of a situation. All of the questions have pretty much been covered. In my case across

Montana, for a transcon, we are a flyover State or we are a ride-through State. We do fairly well up there in the State of Montana in the support of Amtrak.

But you put it through the most desolate part of the State. If you run it down through Billings—and I know I am going to get telephone calls from my people that live in Havre and Wolf Point and Shelby and Whitefish, I will get a letter from them. But we used to have Amtrak service down on the southern part, too. And that connected all of the schools down there. In fact, that is where most of your population is.

Right now we have got about 129,000 people who ride that train in Montana and into some areas that are mostly recreation: over at Whitefish, skiing in the summer, vacation in Flathead. But it is also used by others because we have no bus service. There is no bus service. We cannot make that work.

And I am kind of like Senator Byrd. Those folks up there in those Hi-Line counties vote, too.

So I am going to go back to Senator Murray. I just do not think that we can make it work unless we have got an advocate down at the Department of Transportation. Everybody got all excited the other day when United made their announcement that they are going to forego and abandon their pension programs. And pension programs do not carry people but we sure got excited about it. And now with this, you are touching real people in areas where we have no other alternatives.

You made the statement that you want to go intercity. How many options do people have to get from point A to point B in the inner city? You have your competition bus service You can also go out here from 6 o'clock in the morning until 9 o'clock in the morning on 395, and it is the world's largest parking lot. You can go there and watch. But there are still options. And then there is the Metro. There are options there.

We have no other options. And that is the point I want to make.

ADMINISTRATION BUDGET REQUEST

Senator Murray.

Senator MURRAY. Mr. Rosen, last year, when the Bush Administration sent up its budget request for Amtrak, you proposed to cut Amtrak funding by $300 million. But you said that you would support as much as $1.4 billion each year if your reform proposals for Amtrak were enacted.

When we reviewed OMB's multi-year budget documents, the administration was true to its word. You budgeted $1.4 billion for Amtrak for 2006 and every year thereafter. That was last year.

This year, when you look at the President's budget, he is requesting zero for 2006 and anticipates requesting zero for every year after that.

If that is the case, why is Secretary Mineta publicly stating that the Bush Administration would support $1.5 billion to $2 billion for Amtrak if your reforms are enacted?

Mr. ROSEN. Two things, Senator, let me to clarify. The original proposal that you are alluding to, when the administration proposal was $900 million, contemplated that there would be an increase if the administration's reform proposals were adopted.

As you will recall, they were not adopted to date. And when this year's budget came out and the Secretary made clear that the President's current budget was a call to action. It was clear that the earlier budget proposals, if they were a call to action, they did not work.

So the President's budget this year, as a call to action, has at least had the effect of being more effective at calling attention to the need for reform. That is point No. 1.

I indicated in my opening remarks to the effect that we know from history that the reforms have to come first, the money to follow.

The second part is with respect, Senator, I think you are mistaken what you said that Secretary Mineta has said. Secretary Mineta has not said that the administration would support $1.5 billion to $2 billion a year.

What he said was he was asked, I believe, a question about what it would cost to bring the Northeast corridor up to a state of good repair. And he referenced what is a multi-year number, 5 or 6 years I believe, that there are estimates—I think Amtrak itself is estimated approximately $1.5 billion to $2 billion to do that. Although I would add the caveat that Amtrak has begun the process of spending to bring the Northeast corridor to a state of good repair. So some of that money has actually been spent last year and this year.

So I think there may be some confusion or a mistake as to what numbers are being referenced. I do not think the Secretary has said what the numbers associated with a true reform package would be.

Senator MURRAY. Mr. Rosen, let me just share with you that on March 4, 2005, I believe it was on NPR, Secretary Mineta was asked, "The budget says zero dollars. What is the real figure that the administration is willing to spend on Amtrak?" And Secretary Mineta said very clearly, probably in the area of $1.5 billion to $2 billion.

So he has stated that.

Mr. ROSEN. Again, with respect, I think you need to look at the full context of those remarks. I do not think that was a question that—I think it was a question that related to the Northeast corridor.

Senator MURRAY. No, I disagree. Actually, I will read you the whole question. He was asked: "Democrats in Congress who have criticized your proposal have said well, this thing that Secretary Mineta is talking about is not what the budget says. The budget says zero dollars. What is the real figure that the administration is willing to spend on Amtrak?"

To that, Secretary Mineta answered probably in the area of about $1.5 billion to $2 billion. So he has said very clearly.

Mr. ROSEN. Again, I have a different interpretation, that that figure relates to a multi-year capital item.

Senator MURRAY. I do not see any reference to multi-year capital. But I will tell you this, when OMB Director Bolten testified before our subcommittee, it was 3 weeks ago now, I asked him whether the administration would ever consider sending us a revised budget for Amtrak. And Director Bolten was really clear. He said that this committee has received the only budget we should expect to get from Amtrak under any circumstance.

I would like to know what conversation you or Secretary Mineta have had with the White House that makes you think that the administration might request Amtrak funding if a reform bill is enacted?

Mr. ROSEN. I am not sure if I fully understand the question, so let me try this. In formulating the administration's reform proposals, there have been regular discussions with the Office of Management and Budget. And indeed, the reform proposals had to be approved by the Office of Management and Budget when they were transmitted to the Congress, both in 2003 and 2005.

I think the earlier budget proposals that you referenced in the administration proposal for fiscal year 2005 came out, did contain both a number for that fiscal year and a number with regard to what reform funding would look like. This year, a different approach was taken and you have that before you.

Senator MURRAY. Mr. Rosen, you said you did not understand my question. Let me make it very clear.

The administration is saying that zero funding for Amtrak unless a reform is enacted. Director Bolten made it very clear to us that the administration was not going to request additional funding. So where do we get the idea that if Congress does enact reform, that the administration will then request the $1.5 billion to $2 billion that Secretary Mineta is talking about? Are we going to get a request or not?

Mr. ROSEN. So far we do not have reform legislation that has been enacted. I think perhaps that is the key point to start with.

Senator MURRAY. Say we pass reform. Is the administration going to request the $1.5 billion to $2 billion? Or are they just going to say they support it?

Mr. ROSEN. Well, first of all I have told you that I do not think you are accurate with regard to the $1.5 billion to $2 billion figure. But putting that aside——

Senator MURRAY. I am quoting—I will submit this to the record, the statement from Secretary Mineta.

[The information follows:]

[From Morning Edition, National Public Radio, March 4, 1005]

SECRETARY NORMAN MINETA COMMENTS ON THE PRESIDENT'S PROPOSAL TO CUT FUNDING FOR AMTRAK

Mr. STEVE INSKEEP [host]. The Bush Administration says it is not trying to bankrupt Amtrak. In the budget the President sent to Congress, there is no money for the passenger rail system and that prompted an angry response from Amtrak supporters. But the President's top transportation official says the administration is willing to subsidize Amtrak if it's restructured. Norman Mineta is a former Democratic congressman who's now Transportation Secretary.

Secretary NORMAN MINETA [Transportation Department]. The reason that the President has put no funding for Amtrak subsidy this year is that we submitted our reform legislation in 2004. There's been no action on it, and so finally we decided in order to get people's attention, we would just put no money in for the subsidization of Amtrak.

Mr. INSKEEP. The President called a lot of attention to this. He said he was cutting more than 150 Federal programs. Amtrak was described by the administration as one of them.

You're saying the administration didn't really mean that.

Secretary MINETA. If we get the reform that we're looking for, then we will be asking for the funds to fund a national inner-city passenger rail system. And that's why in our reform legislation, what we do is to make Amtrak an operating company. Right now we subsidize Amtrak, and so they put money into their capital investment program as well as the operational side of their program. And the problem is that much of their money goes into the operation of lines that nobody uses. At the same time capital improvements are being starved. So what we're saying is, let Amtrak be an operating company and the Federal Government will do the financing of capital infrastructure.

Mr. INSKEEP. Democrats in Congress who have criticized your proposal have said, "Well, this thing that Secretary Mineta is talking about is not what the budget says. The budget says zero dollars." What's the real figure that the administration is willing to spend on Amtrak?

Secretary MINETA. Probably in the area of about $1.5 billion to $2 billion. Right now the state of the tunnels and all those things are woefully neglected and we would bring those up to good standards and then turn it over to the States. And then we would participate on a local match on the continued improvement of any capital investment that's made into the system.

Mr. INSKEEP. You're proposing that the Federal Government would continue to pay for upkeep of track or new trains, Amtrak would run them and would be expected to run trains that at least broke even or made a profit?

Secretary MINETA. The lines would be determined by States and not by Amtrak itself. As an example, we have now some 12 States that are spending something like $345 million a year for passenger rail service; $140 million of that is for capital improvements. If our bill had been in place then those States would be getting a 50:50 match on the $140 million on capital investment, whereas right now they're making all of that investment with their own State money. By our taking over the capital investment part of it and let the operations of the railroad be done by Amtrak or other operating agencies, they then can concentrate on delivering the service that people deserve. We're treating Amtrak inner-city passenger rail no differently than we treat highways, airport improvements or transit right now.

Mr. INSKEEP. Although, forgive me, you can improve part of an interstate highway and leave the rest of it unimproved for later. But if you've got a rail line that goes across seven States and just one of them doesn't want to contribute, that rail line goes away. It can't run.

Secretary MINETA. No. No. The rail line will still run but we won't stop in that State or open its doors.

Mr. INSKEEP. Do you really think that this system could maintain political support if a number of States stopped having service there?

Secretary MINETA. We have spent over $29 billion in subsidies to this rail system. I don't think we should continue pouring money into a flawed system. If the President and I really were out to kill Amtrak, we wouldn't do anything.

Mr. INSKEEP. Secretary Mineta, thanks very much.

Secretary MINETA. Not at all. It's great to be with you, Steve.

Mr. ROSEN. Rather than debate that, I will put that to the side and say what I said in my opening remarks, that if the Congress itself takes the serious steps to reform and fix intercity passenger rail, then the administration is serious that if we get real reform we will support funding for reformed system.

Senator MURRAY. What does support mean? Does that mean request or you will just say it on the radio?

Mr. ROSEN. It does not mean that we will say it on the radio, but as I have said here and I have said previously, I think it is premature to talk about what exact steps and what exact amounts the administration will take or propose until we have the reforms.

Senator MURRAY. I take it your answer is——

Mr. ROSEN. We know where that leads.

Senator MURRAY [continuing]. We should not expect a request from the administration on the exact dollar amount? They will just say that they support money once reform is enacted.

Mr. ROSEN. I am sorry, Senator, I do not understand the question.

Senator MURRAY. It is a statement. It sounds to me like your response to us is that we cannot expect a request from the administration whether or not we do pass any kind of reform.

I believe my time is up.

Mr. ROSEN. I think what I can say is that if there is no reform, you have the administration's request. But that is not necessarily the end of the story.

Senator BURNS. Senator Bennett.

Senator BENNETT. If I could just pick up on what Senator Murray is saying, and give you a little advice, and I am fully supportive of what you are trying to do. I am fully supportive of reform. And I think the Congress needs a jolt and we certainly have had one.

But I would advise you to define the carrot instead of just saying we will support something. It would be nice to say if you really do come through with the reform, this is what we will do. And I think it is reasonable that Senator Murray is asking for some more concrete definition of what the carrot looks like.

You are saying there is a carrot out there for us. You have hit us with a 2 by 4 between the eyes and got our attention to the fact that something serious has to be done. And I am supportive of that. But having used the stick, I think a little bit clearer carrot would probably be a good idea.

I think that is what Senator Murray is asking for.

With that, let me go back to the subject I have raised. I have here the Amtrak strategic reform initiatives and fiscal year 2006 grant request, provided by Amtrak. I think it is a pretty good piece of work. We keep hearing yes, we are going to reform. In 1997, we were assured by Amtrak's management, Amtrak is absolutely going to be self-sustaining and profitable by 2005. And we heard right up through—pardon me, 2002. And we heard right up through 2001 that they were on track to profitability. And then on 2002, it was well, by the way, we are nowhere near it and the CEO resigned.

We have got to be serious. So let me ask Mr. Laney and Mr. Gunn, if you were kings and had a completely free hand, and you did not have to worry about past contract obligations that you feel now bind your hands, you could have any kind of work rules you wanted, you had access to whatever funds you needed for capital improvements, all of the rest of it. In other words clean sheet of paper time.

Could you design an intercity passenger system on rails that made sense and was sustainable over time? With the assumption that there would be some degree of Federal subsidy? Because I think we probably would have to have a degree of Federal subsidy. I do not think you could expect it all to come out of the fare box. But one would hope it would be a degree of Federal subsidy substantially less than we are doing now.

Is that a possibility? Forget where you are, in terms of the straitjackets of the past that are put upon you. Clean sheet of paper time, you are king. You can devise whatever you want. Could you, in fact, envision a passenger system that worked?

REDUCED FEDERAL OPERATING SUBSIDY

Mr. LANEY. Senator, let me first say I want to hear from Mr. Gunn on this, as well, because his perspective may differ slightly but I do not think much. But let me be king first.

Yes, absolutely. And I think, to a great extent, what we presented in terms of our strategic reform package does just that. We have erased the blackboard and started writing on it again. We have been constrained by some prior decisions by earlier boards and earlier managements and we bear the burden of those decisions and they are difficult. There is no question about it. Whether it is issues with respect to the Acela, whether it is issues with respect to long-distance trains, whether it is issues with respect to debt.

But absolutely, there would be different answers and different responses for our different lines of service. Whether it is the corridor service, Northeast Corridor, or other State service corridors, not only could we, we absolutely should, from a transportation policy standpoint, begin to address in a serious way State corridor issues. There been references to congestion, when it is aviation or whether it is highways. There is a very complementary role for passenger rail service to play.

You project it 25 years, 50 years, 75 years forward, we will have made a serious mistake if we do not begin taking incremental small steps now.

There is also a role for long-distance service.

Senator BENNETT. That is where the argument was going to come.

Mr. LANEY. There is also a role, but it would be a reconfigured long-distance service. And to address some of your issues, I think we have presented, in effect, a systematic approach by which we reevaluate and address current routes, ultimately eliminate some, and may begin to add others over time. But it cannot happen overnight and it needs to be managed carefully. But I think long-distance still plays a role. It just needs to be reconfigured slightly, or significantly.

Mr. GUNN. I basically support what the chairman said, not just because he is my chairman. I actually agree with him. I think that the way that you look at this is that in the future there is no way you get around the fact that the capital is going to have to come from the government, either a combination of State and Federal.

I think the operating deficits can be managed and they can be controlled and reduced, particularly if we have the kind of freedoms that you mentioned. They cannot be totally eliminated. And I do not think they will be eliminated except in some very dense corridors such as the Northeast Corridor. But you have to have volume.

I think the long-distance trains, the deficits can be—there is a lot of things we can do if we have freedom to control those deficits. And I think if you look at our plan, which you have, we actually give you sort of a vision of what would happen over 5 years, in terms of the Federal requirement. You see the operating subsidy dropping—or not going up certainly—but the capital is absolutely a governmental responsibility and you cannot avoid that. This is not a profitable business.

Senator BENNETT. I understand that. And if I may, Mr. Chairman, one last quick question in the spirit of Senator Murray's question, assume that we do everything you are talking about here, that Congress gives you the authority you want. We put in the capital to make the necessary improvements.

Can you give us a ball park as to what the operating subsidy then would be? Would we still be talking about $1 billion year out of the Congress? Or would it come down? You talk about long-distance and we can argue about that. That is $300 million and that is not inconsequential in this situation.

Mr. LANEY. You are just talking about an operating subsidy, Senator, not capital?

Senator BENNETT. That is right.

Mr. GUNN. We made a stab at projecting if our reforms were enacted what the Federal needs would be in fiscal year 2011 which is what, 5 years out. And basically we showed the Amtrak requirement dropping to about $800 million for the whole system. And if you look at this, that is capital and operating. Operating is $220 million.

Right now our operating deficit is about $570 million and we show that dropping to about $220 million. There is a combination of things. It is efficiencies brought about by work rule change, changes in the retirement package and some other things, but also a shift to the States of responsibility for their corridor development if they get the Federal capital.

But you can see the Federal piece certainly not rising. It would drop. We are estimating you can get it as low as $800 million, both capital and operating, if you got the reforms, the real reforms we are talking about. And those are tough. It is the Railway Labor Act piece.

Senator BENNETT. As I say, I think you ought to stress that to the Commerce Committee because $800 million is a much easier pill for the Congress to swallow, particularly in 2015 when it is an even smaller percentage of the Gross Domestic Product than it is today, than the amount we are currently paying today.

Thank you, Mr. Chairman.

Senator BURNS. Senator Kohl.

Senator KOHL. Thank you very much, Mr. Chairman and Senator Murray.

While I share the sentiments of our colleagues regarding the President's draconian approach to reform, I prefer to use my time to assess the merits and viability of passenger rail outside of the Northeast corridor.

Whenever we hear talk of passenger rail, we hear about the Northeast corridor. Indeed, the administration's fiscal year 2006 budget is no exception, providing funding only to operate this corridor should Amtrak be forced to cease operations.

As a Senator from the Midwest and Wisconsin, I have to say I find this approach to be shortsighted and potentially harmful to our Nation's intermodal transportation system.

In the Midwest, as in many parts of our country, passenger rail provides, as you know, a critical link for thousands of travelers.

While I understand that increased ridership does not necessarily equal success for Amtrak, I agree that reform is in order. However, I would argue that forcing the more than 545,000 Wisconsin riders who used Amtrak last year to find another means of transportation does not certainly by itself equal reform.

I do not think that anyone here would argue that shutting down Amtrak in the Midwest will result in reaching agreement on plans to reform the system. Putting more cars on congested roadways and more travelers in overcrowded airports cannot possibly be the solution and I hope that we can arrive at better suggestions.

Mr. Gunn, we have heard the administration talk about the need for reform at Amtrak, and as part of that reform the need for greater State investment in passenger rail. As you know, Wisconsin has been a leader in this effort, providing 75 percent of the necessary funding for the highly popular Hiawatha service between Chicago and Milwaukee. This line has continued to break all-time ridership records over the past years. Without the funding that Amtrak is requesting today, will this line be forced to shut down? And if so, when?

Mr. Mead, I would appreciate a comment from you.

Mr. GUNN. If the administration proposal went through and it was bankruptcy, the line would cease to operate.

Senator KOHL. It will cease to operate.

Mr. GUNN. It would still run freight and Metra but Amtrak would cease to operate.

Senator KOHL. Mr. Mead.

Mr. MEAD. I would not going to go so far as to say that Amtrak would totally cease to operate. I would say that there would be almost certainly very significant cuts in service, including the route that you mentioned.

Senator KOHL. That Chicago to Milwaukee——

Mr. GUNN. I was referring to if the administration's budget proposal went through, zero, we would cease to operate.

Mr. MEAD. I am sorry, I misspoke. Certainly, $360 million is just not going to—you are going to have to have a shut down. I was referring to $1.2 billion, which is the current year's appropriation. If you just reenacted the 2005 appropriation for 2006, that would give you $1.2 billion, you are going to have very significant cutbacks in service.

Mr. GUNN. You will have a cash crisis. If you have $1.2 billion, you will have a cash crisis and we will be right back where we are today very quickly.

Senator KOHL. I think we all recognize, and I am sure you know, that that particular line is really, really successful and serves an important purpose.

Mr. GUNN. Since the airport station opened, we have had ridership growth of 30 percent, 25 percent in the last few months.

Senator KOHL. Increase.

Mr. GUNN. Yes, because of the airport station, which is just south of Milwaukee. It has just taken off.

HIGH-SPEED CORRIDORS

Senator KOHL. I worked to get funding for that so I am very much aware of what you are saying and I cannot imagine a decision that, in effect, would close down that route.

Yesterday, I met with a group of constituents from La Crosse, Wisconsin. Currently, La Crosse is only served by the Empire Builder line with one round-trip stop in the city each day. My constituents shared with me the potential economic impact of bringing high-speed rail to the western side of Wisconsin.

Due in part to the heavy debate over Amtrak's funding needs, the debate over the merits of high-speed rail seems to have quieted. I did note, however, that the administration zeros out funding for the next-generation high-speed rail program which funds the research needed to determine the viability of high-speed rail in America.

Mr. Mead, can you provide some insights as to why the administration would zero out funding for this relatively modest program? Do you believe that there is any merit in having high-speed rail outside of the Northeast corridor? And Mr. Gunn, I would appreciate your view.

Mr. MEAD. I think it depends on what your definition of high-speed rail is. I think the average speeds of some of these long-distance trains that we have today is around 46 or 48 miles per hour, and that is scheduled. That does not count whether there is going to be delays. So if you go up to about 80 miles an hour, I think for those people that ride those trains that are doing 46 miles an hour, that would be relatively high speed.

Actually, I would just like to, if I might, just take a moment to point out something that is in the administration's bill that I think is very important. The administration's bill proposes capital grants to develop rail corridors such as those that you are describing. The problem is that the States are saying well, this is nice. It is a capital grant program. But how much funding is the Federal Government going to put into it?

And it becomes a chicken or egg issue, in my judgment, that the States are not going to buy into a capital grant program and take on more decisions and take on more responsibility and authority for making rail decisions that affect their corridors and agreeing to a capital grant program until such time as they understand the financial consequences of that.

And I think that is a core element of the debate here, is the uncertainty over what the funding conundrum is going to look like. That certainly is what Senator Murray's line of inquiry was after.

Senator KOHL. Mr. Gunn.

Mr. GUNN. I would only comment that Amtrak's management position has been that there are a number of corridors outside the Northeast that should be developed and we worked with the States for them. For example, the Milwaukee and perhaps onto Madison, Chicago to Madison, is one of those corridors where there is real potential. There are also corridors in California and in the Northwest.

Our view is that they should be done incrementally. In other words, when you go into these, do not go in trying to go to 150 to

200 mile an hour trains. What you want is to get up to the 90 or 100 mile an hour trains, which we can do with conventional equipment, and have frequent service. That is the key, good, solid and reliable service. But it does not have to go 150. And you can do it on a relatively modest budget if you use existing technology.

But, I think, we have about eight corridors that we think are really ripe for development if the States get this new State/Federal partnership where there is capital money available. But they have to know what that is. But there are corridors, definitely.

Senator KOHL. Thank you. Thank you, Mr. Chairman.

REDUCING THE OPERATING SUBSIDY

Senator MURRAY [presiding]. Mr. Laney, let me go back to you again.

You submitted a grant request seeking $1.82 billion for next year. That is more than 50 percent above your current funding level. And you also, of course, submitted a comprehensive set of reform proposals. As part of that grant request you said—and I want to read it to you—we believe that these initiatives will, in time, dramatically reduce the requirement for ongoing Federal financial support for Amtrak and reinvigorate intercity passenger rail.

How soon would your subsidy needs dip below the current level of $1.2 billion if that reform package is enacted?

Mr. LANEY. Certainly not during fiscal year 2006. There is no question about that. Fiscal year 2006 we would stay at the same level, if not higher. But let me make clear what I said earlier, and that is the increase from $1.2 billion to $1.85 billion is capital only, our capital investments as well as working capital. It is not an increase in operating expenses. The operating expenses are basically flat.

Largely in 2006, it would be an increase, as I mentioned, in capital. And my guess is that capital expense would stay flat but higher for the next 4 or 5 years as we rebuild, in effect, the Northeast Corridor infrastructure and rehabilitate a bunch of very old and tired equipment. And there is enormous demand, I think, growing demand for equipment beyond just the Northeast Corridor.

But I believe perhaps as early—but I do not know, this is conjecture—as 2007 we will see——

Mr. GUNN. It depends on when the reforms are enacted. In other words, the ability to start winding down or trending down some of the cash demands for Amtrak depend upon when you enact a proper capital grant program for the States, an 80/20 program. And then how long you give the States to adopt, to get into that program and to begin to assume full responsibility for the operating deficits for the corridors.

Senator MURRAY. So the costs of Amtrak are not going to be reduced. It is just going to be the States who are going to have to come up with that?

Mr. GUNN. No, actually Senator, there are two pieces to this. If the reforms that we have in there—if we got our work rule reform and we got the Social Security reforms and some other things, there is probably $200 million or $300 million which we could ultimately, over time, reduce.

Senator MURRAY. Over time when? From my understanding, at this point——

Mr. GUNN. We assume, for example, if we got work rule reform, we would implement it through attrition rather than just laying people off. That has been our position with our unions. And so, once you got the reform, it would take a number of years, 2 or 3 years or 4 years, to attrit out the people that were surplus.

Senator MURRAY. To get to the point where you are saving $200 million to $300 million?

Mr. GUNN. One hundred million dollars on the labor. There are some internal reforms that we are going to do, or changes that we want to make in terms of food service and some other things, that will take place gradually over the next 2 or 3 years.

Senator MURRAY. But the vast majority of this is just putting money to the States. It is not like these costs disappear?

Mr. GUNN. A big part. I would not say vast. It is very important, if we can get the changes that we are suggesting, if we can move from railroad retirement to Social Security, if we can get either through reform of the Railway Labor Act or through negotiation and get the work rule reform and make the others, it is probably $200 million or $300 million of operating subsidy that we can deal with.

But it is also—I do not want to be argumentative. It is that there is a significant portion of improving the efficiency of Amtrak.

Senator MURRAY. Mr. Mead, you are familiar with both of the reform proposals. Can you tell us whether you think either of these proposals save any money in the short-term, Federal tax dollars?

Mr. MEAD. Well, they save money in the sense that—some of them, they save money in the sense that they would avoid cost that you would other otherwise incur. But the bottom line in terms of how much money you would need, because of a backlog in capital inside and outside the Northeast corridor, you are going to need some money to put the system in a reasonable state of good repair and to improve performance.

So you are not going to—in my opinion, it is a myth I think that you are going to save your way somehow out of this. There are savings. There is no question. This food service one, for example. I do not mean to get emotional about it, but it is something that they could have been doing for some time. And it is about $80 million, $90 million, $100 million. There is no need to wait for 3 or 4 years to do that.

But I am telling you, I would take the $100 million and I would pump it into capital. That is what we need to do. We are talking about several billion dollars in capital.

The other area that I think that we get some savings on is in this debt service. I think the loan they took out or the mortgage they took out on Penn Station was about $300 million at 9.5 percent. Your committee is paying for that at 9.5 percent. And that means the Treasury Department is, too. So I think there are some savings there.

Senator MURRAY. Can you tell us what your estimate is of what the President's reform bill, if it was passed, would cost us in 2006?

Mr. MEAD. I would put it in at about $1.4 billion or $1.5 billion.

Senator MURRAY. Mr. Gunn, do you have an estimate of what it would cost to implement?

Mr. GUNN. I approach it a little differently, if I may. If you look at the administration's reform package, it basically is internal to Amtrak, restructuring the corporate structure. And I think it will be a disaster because it is impractical. And it does not deal with some of the real issues that need to be addressed that I think the board's reform package deals with.

Senator MURRAY. Can you explain that?

Mr. GUNN. If you look at the administration proposal, what it does, it is based on the assumption that the services we operate can be privatized and contracted out, which they cannot. They are not profitable. You can contract them out, but you have to subsidize them.

Also, the basic proposal is to create three Amtraks instead of one. You have a residual Amtrak, you have an Amtrak passenger service operating company, you have an infrastructure company. And it all has to happen on a fairly tight time frame. That will be extremely disruptive and expensive. It also has some operating problems associated with it.

But you will end up with—overhead departments will have to be replicated. In other words, the way we function now you have one law department. Well, if you have three separate companies, you are going to need three. You have one personnel department, you will have to have three.

And it is all being done in an environment where it is not clear how it is going to be funded. I think it does not address any of the real cost issues that are associated with Amtrak. And what will happen is you will end up with a lot of the service coming off and you will have an enormous C(2) bill, the labor protection.

Senator MURRAY. This committee will not decide the reform package, the Commerce Committee will.

Mr. GUNN. I am just saying it will cost you money.

Senator MURRAY. But you are saying to us that if we pass a reform proposal, we are not going to save money in 2006, which is what this committee is currently looking at?

Mr. ROSEN. Senator, could I suggest that I do not think Mr. Gunn is actually the best expert you are going to find on the administration's proposal. And I would say I think his characterization of it was totally wrong.

AMTRAK FUNDING NEEDS FOR FISCAL YEAR 2006

Senator MURRAY. Mr. Rosen, again, this committee is not here to debate the different reform proposals. What this committee has to do is provide the funds for the expenses for next year.

So what I am hearing is that zero funding is not going to do it and, in fact, it is going to cost more no matter which proposal is put in place in the short term. I think that is what this committee is concerned with.

Mr. Mead, I do want to ask you, for the last 2 fiscal years, the subcommittee funded Amtrak at about $1.2 billion. In fact, the funding level for the current fiscal year is actually somewhat smaller than the assistance provided last year because of the across-the-board cut and the fact that Amtrak is now required to pay back part of its Federal loan.

Even though Amtrak was able to make it through a funding freeze for 2005, you are now testifying to this committee that they need a $200 million to $300 million boost simply to maintain the status quo in fiscal year 2006. Can you explain why that is the case?

Mr. MEAD. It does sound a bit inconsistent, but I can explain it, I think.

Actually, for this year, Amtrak has $1.4 billion already in Federal money. And that is because they closed out the last fiscal year flush with cash. They had $200 million extra, which they are going to spend this year. And that puts you at $1.4 billion, not withstanding the fact that the appropriated level is $1.2 billion.

Now, we are not going to end this fiscal year like we did last fiscal year. I have pointed out in my statement that we are going to have about $30 million or $32 million in cash as you roll into the new fiscal year. So it kind of makes the time pressures on the appropriation process more of a priority.

Senator MURRAY. Are you certain that Amtrak services would have to be reduced if we froze Amtrak funding at $1.2 billion?

Mr. MEAD. Am I certain?

Senator MURRAY. That Amtrak services would have to be reduced if we did $1.2 billion?

Mr. MEAD. Senator, I think that—I am concerned about the capital condition in the Northeast corridor. I do not want to analogize the situation to the kid at the dike where he is putting his fingers in the different cracks in the dike. But I am concerned about the number of go slow orders in the Northeast corridor. And I think Amtrak would have no choice but to cut back service in some significant ways.

Senator MURRAY. Mr. Gunn, what are your views?

Mr. GUNN. To build on what the Inspector General said, I think that he has explained why the $1.2 billion does not work because we are spending this year at the rate of $1.4 billion. But what makes the problem even worse is that we have a number of very serious infrastructure issues that have to be dealt with which add up to about $100 million that are not in this year's budget. So that gets you up to like $1.5 billion.

If you were to drop back to $1.2 million, what would happen is you would basically have—you would have $350 million available for capital instead of the $650 million that we are saying we need.

The problem is that we have already—with the lead times on materials, the $350 million would be—probably $100 million of it would be for material which would sit because you would not have the money to install it. So your actual capital available for the railroad would be about $200 million or $250 million.

And if you look at our budget right now, just the car budget for the Northeast Corridor would be $100 million of that, to repair the Amfleets, to rebuild the Amfleets. You would have almost no money for infrastructure work. You would have $100 million for infrastructure.

That is not sufficient to maintain a high-speed railroad. What will happen, the Inspector General is correct, you immediately will have slow orders show up. But more importantly, the operating budget will go through the roof because you will have emergency repairs all over the place. It will quickly come unglued.

Senator MURRAY. To that point, you were required to suspend all service of Acela, high-speed Acelas, a few weeks ago because of the brakes. My understanding is that the loss of revenue from that is requiring you to eat up a lot of your available cash right now.

Mr. GUNN. Yes.

Senator MURRAY. What confidence do you have that Amtrak will be able to finish this year, knowing that, with a cash positive situation?

Mr. GUNN. I think we will probably limp into next year.

Senator MURRAY. What is limp?

Mr. GUNN. By limp, I mean we will have like $20 million left in the bank, something in that neighborhood.

Senator MURRAY. That takes into account the Acela?

Mr. GUNN. Yes, I think that will be the case. But I really—the problem we are having is that the ridership is still moving around. In other words, we have got replacement service in effect and the riders appear to be coming back. But we are definitely going to be hurt to the tune of $5 million a month net. That is an optimistic number. It depends on what that number actually turns out to be.

Senator MURRAY. Mr. Rosen, are you and other members of the Amtrak board monitoring the situation?

Mr. ROSEN. Absolutely, and I think that one of the things that the company is going to need to do is look for ways to reduce expense and conserve cash.

Mr. GUNN. The reality is at this point we do not have a lot of options left to conserve cash.

Senator MURRAY. Mr. Rosen, if it looks like Amtrak is going to sink into bankruptcy before the end of this current fiscal year, is the administration looking at a supplemental appropriation request for Amtrak to keep it out of bankruptcy?

Mr. ROSEN. I think that the board is looking carefully, as is DOT, at what the cash situation is, and that it will be incumbent on any responsible management to look for ways to make that situation work. I cannot speak for all of the board members but I have some confidence that all of the board members will, in fact, want the company to do that.

Senator MURRAY. So it is possible that we could see a supplemental appropriation if we see a bankruptcy occurring?

Mr. ROSEN. Senator, I was referring to monitoring the cash situation and the company taking appropriate steps to ensure that it is satisfactory.

Senator MURRAY. Mr. Gunn, let me go back to you. You have been required to operate a railroad in the midst of all this debate over proposals by the administration to put Amtrak into bankruptcy. I am concerned about how the railroad's day-to-day finances have been impacted by the language in the President's budget stating the administration's intention to put the railroad into bankruptcy. And I am curious how that and the Senate vote that failed to reinstate your subsidies may have impacted your daily finances?

Have any of railroad's costs, be they borrowing costs or insurance costs or expense costs been negatively impacted by the discussions of bankruptcy or the failed vote in the Senate to restore your subsidy?

Mr. GUNN. Yes.

Senator MURRAY. Can you be specific?

Mr. GUNN. A number of things have happened. One, on insurance, we did have an insurance policy that was up for renewal. And it was an important policy. And I think we probably ended up spending $500,000 to $1 million more than we would have. We had our bond rating downgraded. We are beginning to get from certain—and I do not want to be specific—but we are beginning to get from certain suppliers requirements for changes in payment terms. We are pretty current. We pay on a current basis. We try to be a good neighbor in that sense. But we have a number of fairly large accounts that are talking about our escrowing cash or giving them cash in advance.

We have been unable to close our books, and that means the meter is still running on our accountants. There is nothing wrong with the books; the issue is the management letter. So there has been a number of real impacts, and the biggest impact which could happen, of course, is on the payable side, commercial payables.

Senator MURRAY. We are going to have a vote in just a few minutes so I will end shortly. But Mr. Rosen, I just want to say that the only funding for passenger rail included in the President's budget is the $360 million for the Surface Transportation Board. As a matter of law, those funds can only be used to continue the operation of commuter rail services that operate over Amtrak property or by Amtrak employees once Amtrak ceases to operate. That is what the law says. The funds can be used once Amtrak ceases operations.

Your formal statement kind of glossed over that fact and you seemed to imply that this funding provided to the Surface Transportation Board could actually be used to continue operations of Amtrak trains on the Northeast corridor.

So Mr. Gunn, I want to ask you to clarify this question. If this committee adopted the President's budget of providing zero to Amtrak and $360 million to the Surface Transportation Board, do you think that the Northeast corridor trains will be able to operate next year?

Mr. GUNN. Absolutely not. I can give you a real simple reason why. If you look at the engineering department's operating budget and capital budget for fiscal 2004, for example, it was $550 million, $150 million operating and $400 million capital. And basically that is all corridor, 90 percent of it is corridor.

But on top of that, in order to run the corridor, you have to have a payroll department, an accounting department, a law department. You have to have the support. You have to have procurement.

We gave the IG—actually the FRA Administrator but it was also to the IG—a report a year or so ago where we calculated the cost of a stand-alone corridor and it is $1 billion a year plus.

Senator MURRAY. So would it be even safe to operate the commuter trains under these conditions?

Mr. GUNN. I cannot answer that. I do not know how they are going to spend the money without an organization to spend it. That is the problem. We are the ones that spend the money, that know how to fix the wire, the signals, the track. If we are gone and have been liquidated, I do not know who spends the money.

Senator MURRAY. Mr. Mead, do you want to add anything else before we recess?

Mr. MEAD. Just that I do not think anybody really thinks that the $360 million is the best way to go. It is a road we have never been down before. I do not think anybody really wants to go there.

Senator MURRAY. Thank you very much. Mr. Rosen, you look very anxious to clarify.

Mr. ROSEN. I would like to add a couple comments to that, if you give me 1 last minute here.

The question as to whether the STB's funding could be used for Northeast corridor trains would require a legal determination as to whether those trains, particularly the ones that make multiple stops, could be deemed to constitute commuter service. So I think there is a legal question there that it would have to be resolved. And it is not a given that it would only be the trains operated by say New Jersey Transit or SEPTA and others.

Second, one should not forget that the Northeast corridor trains, on the operating side, operate at something approximating break even. They do generate cash. It is not a given that those would need to stop if Amtrak was otherwise in a problematic financial situation.

Senator MURRAY. Unfortunately, we have a vote. I have to say that Mr. Gunn, let me just ask you, how many years have you spent working in the railroad and transit industry?

Mr. GUNN. Forty-one.

Senator MURRAY. Mr. Rosen, how many years?

Mr. ROSEN. How many years working in the railroad industry?

Senator MURRAY. I am sure you are a great lawyer but I just wonder how much time you have spent working in the railroad and transit industry?

Mr. ROSEN. Given that I have been a lawyer my whole career and have not been a train operator, I think you know the answer to that.

Senator MURRAY. I appreciate that. So you cannot blame me for considering Mr. Gunn's views to be authoritative on this.

Mr. ROSEN. I hope you will take my views as the authoritative ones on the administration's reform proposals, rather Mr. Gunn's, too.

ADDITIONAL COMMITTEE QUESTIONS

Senator MURRAY. Any additional questions submitted to your department should be answered in a timely manner and will be included in the record.

[The following questions were not asked at the hearing, but were submitted to the agency for response subsequent to the hearing:]

QUESTIONS SUBMITTED TO THE AMTRAK BOARD OF DIRECTORS

QUESTIONS SUBMITTED BY SENATOR CONRAD BURNS

Question. Your proposal for long-distance trains requires the performance of trains to be measured against a set of undetermined performance criteria, which would seem to be mostly—if not entirely—financial. Under such a system, how would the public service value of Amtrak be measured?

For example, if folks are riding the Empire Builder to go to a doctor, or to receive long-term medical care, the cost of that service might not pencil out, but it is certainly valuable. How would that be considered, under your proposal?

Answer. The clear signal we have received from Congress and the administration is that financial performance must improve. The Board agrees with that message. Nonetheless, I anticipate that the criteria for evaluating the performance of long distance trains will attempt to factor into account public benefits and not just financial performance. For example, the route performance criteria might include a measure that reflects the number or percentage of passengers on a long distance route traveling to/from communities where alternate public transportation services are limited or non-existent.

Question. Your proposal also relies heavily on the development of corridor trains. Do you have a sense of what the real potential for such service is?

Answer. Despite the absence of a Federal corridor rail program, 13 States are currently partnering with Amtrak to fund the operation of corridor services in shorter distance markets (less than 500 miles). Many of these States have also made capital investments with their own funds. The growth in ridership and service that has resulted from these investments—on the Amtrak Cascades route in Washington and Oregon, the Capitol Corridor in California and the Hiawathas route in Wisconsin to name just three—demonstrates the potential for corridor rail development in densely populated corridors throughout the country.

Due to the lack of a Federal capital program for States, there is no data source to indicate the potential for development of corridor rail service. Knowing this, over the past 2 years, Amtrak has surveyed States to get an indication as to their plans for existing or future corridor development. In 2004, 29 States responded to the survey and provided details about their plans. Many of them also indicated that lack of a Federal funding match program is a major impediment to corridor development, and that enactment of such a program would act as an incentive to more aggressively develop existing passenger rail corridors or begin developing new ones.

Based upon the information States provided in the 2004 survey, the Corridor Appendix to Amtrak's fiscal year 2005–2009 Strategic Plan (transmitted to Congress and available at www.amtrak.com) identified eight "Tier I Corridors" and four "Tier II Corridors". These are corridors where States have "ready to go" plans—including capital investment plans and funding commitments for State matching funds—for corridor development projects that could provide significant near-term benefits if Federal dollars were made available to match State investments.

Question. Can you discuss the recommendation to shift new workers away from the Railroad Retirement system into Social Security?

Answer. Amtrak's Strategic Reform Initiatives propose that the provision of intercity passenger rail services be opened to competition, and that intercity passenger rail be placed on an equal footing with other transportation modes. Requiring Amtrak and many potential new operators of interstate passenger rail service to pay Railroad Retirement taxes places interstate passenger rail at a disadvantage with respect to other transportation modes. For example, the airline industry is subject only to Social Security, and a large portion of its retirement obligations to its employees has been assumed by the Federal Government as a result of airline bankruptcies. The fact that some potential operators of intercity passenger rail might not be subject to Railroad Retirement taxes under existing law also creates inequities that ultimately must be eliminated to create a truly competitive market. Conversely, potential interstate passenger operators are unlikely to attempt to enter the Amtrak market as competitors if the cost of doing so includes Railroad Retirement taxes.

Amtrak believes that placing all new intercity passenger rail employees under Social Security is the best way to transition to a level playing field and reduce Federal subsidy requirements without impacting the retirement planning or benefits of current Amtrak employees and retirees.

QUESTIONS SUBMITTED TO AMTRAK

QUESTIONS SUBMITTED BY SENATOR BYRON L. DORGAN

VETERANS ADVANTAGE

Question. Thousands of North Dakotans depend on Amtrak each year for their transportation needs. However, long distance trains, including the Empire Builder that serves my State, are under attack by the Bush Administration. The administration provides no Federal subsidy in its fiscal year 2006 budget for Amtrak's long distance rail service. I understand that Amtrak has submitted a sizable request for funding for next year, and I will do what I can to support it as a member of this subcommittee.

On a related note, I would like to talk to you about a program to provide discounted train service to America's veterans. For more than 2 years, Amtrak offered a 50 percent discount for veterans in off peak periods. I am told that this was a very successful program.

You may recall that this committee included language in the 2004 conference report strongly urging Amtrak to continue the 50 percent discount for veterans. Would you please let this committee know what Amtrak intends to do in the future about this program?

Answer. As you know, Veterans Advantage (VA) is a paid membership program, and the discount associated with this program is only available to their subscribers. Amtrak currently offers VA members a 15 percent discount.

The 50 percent discount that you refer to was initiated as a promotional offer, and the promotion had a mutually agreed upon end date of December 2003. This deep discount offer was never intended as a permanent fare program. VA was aware of the terms and conditions of the promotional discount and knew that it would expire in 2003. No other business partner with Amtrak received as generous an offer as what was given to VA for this promotion.

Last year, in an effort to work cooperatively with VA, Amtrak offered a buy one get one free promotion that was rejected by VA. Amtrak then offered a limited 50 percent off promotional program to VA members for the fall of 2004 that too was rejected by VA. The Amtrak offer was from September 14, 2004 through February 8, 2005. VA sent a letter dated September 16, 2004, declining the Amtrak 50 percent discount offer. Since then, Amtrak has tried to work reasonably with VA in the hopes of reaching a mutually beneficial arrangement for additional temporary promotional offers for its members, yet our offers have been turned down.

I want to be clear that for the past year we have worked sincerely to find a mutually beneficial solution to this matter. In fact, Amtrak not only continues to offer a 15 percent discount to VA members, but the program is also promoted on Amtrak's website, system timetables and other marketing materials. In addition, to provide the program with an incentive to attract new members, Amtrak is also offering 500 free points in its Guest Rewards program to new Veterans Advantage members. Amtrak remains committed to continuing to work with VA and its members.

AMTRAK'S IMPACT ON RURAL COMMUNITIES

Question. Do you believe long distance passenger rail routes will be able to survive if States are left held responsible for making up the funding? Has any State indicated to you that they would have the resources to make up such shortfalls?

Is it your expectation that some of the long distance routes would cease to exist?

Answer. Under Amtrak's Strategic Reform Initiatives, States would be required to provide operating funding for long distance trains only if, after efforts to improve performance, a particular train still fails to meet minimum performance thresholds, and then only to cover the "gap" between the threshold amount and the train's actual operating losses. While no State has indicated that it is in a position to bear the full operating losses of multi-State long distance trains, we believe that it is possible that some States might provide some "gap closing" amounts required under this proposal.

Amtrak does not anticipate that long distance routes would survive if States were responsible for covering all operating losses. Significant impediments to States assuming such responsibility include the large number of States (generally 6–12) served by each long distance route; differences in relative benefits received by individual States; and variations in States' financial resources, transportation policies, and constitutional statutory frameworks governing transportation funding. It bears noting that on no occasion in Amtrak's 34-year history has a group of States offered to provide operating funds to retain long distance routes slated for discontinuance.

Whether some trains are ultimately added to or subtracted from the long distance system will depend upon the performance of individual routes and, for any routes that do not meet minimum performance thresholds, States' willingness to fund a portion of operating losses so that those thresholds are met.

AMTRAK AND COMPETITION

Question. Part of the Amtrak reform plan is aimed at promoting competition. Have other rail operators indicated to you that they wish to provide passenger rail service for the long distance routes, such as in my State of North Dakota?

Answer. No other railroad has indicated to Amtrak that it is interested in operating long distance trains. Some private companies have expressed very preliminary interest in providing on-board services (food and beverage/sleeping car) on long distance trains. Amtrak remains open to other providers assuming additional services, or ultimately operating entire routes, if legal and contractual impediments are addressed.

CONCLUSION OF HEARINGS

Senator MURRAY. The subcommittee stands in recess, subject to the call of the Chair.

[Whereupon, at 11:32 a.m., Thursday, May 12, the hearings were concluded, and the subcommittee was recessed, to reconvene subject to the call of the Chair.]

DEPARTMENTS OF TRANSPORTATION, TREASURY, THE JUDICIARY, HOUSING AND URBAN DEVELOPMENT, AND RELATED AGENCIES APPROPRIATIONS FOR FISCAL YEAR 2006

U.S. SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS,
Washington, DC.

MATERIAL SUBMITTED BY AGENCIES NOT APPEARING FOR FORMAL HEARINGS

[CLERK'S NOTE.—The following agencies of the Subcommittee on Departments of Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies did not appear before the subcommittee this year. Chairman Bond requested these agencies to submit testimony in support of their fiscal year 2006 budget request. Those statements submitted by the chairman follow:]

UNITED STATES POSTAL SERVICE

PREPARED STATEMENT OF JOHN E. POTTER, POSTMASTER GENERAL AND CEO

Good morning, Mr. Chairman and members of the subcommittee. I appreciate this opportunity to talk to you today about the Postal Service's accomplishments in recent years; the continuing challenges we face in the years ahead; and our appropriations request for the next fiscal year.

Since I became Postmaster General in June of 2001, I have focused the Postal Service on transforming into a leaner, more efficient, more modern organization. Our continuing Transformation efforts are delivering results for the American people. In the last few years, we have seen significant positive results in the areas of service, customer satisfaction, finances, and workplace improvements. I am very proud of our employees and our management for helping us achieve these impressive results in these challenging times.

Our record of accomplishment is clear. We again set records for service performance and customer satisfaction in 2004. Last year, we reduced our debt by $5.5 billion. At $1.8 billion, our debt is at its lowest level in 20 years. We also recovered all prior years' losses and, for the first time since postal reorganization in 1971, ended the year with positive retained earnings. We have achieved an unprecedented five consecutive years of growth in total factor productivity—the equivalent of $6.1 billion in cost savings. Financially, we had a second straight year of positive earnings—with a net income of $3.1 billion. Career staffing has declined from its peak in 1999 to pre-1985 levels, thanks to our embrace of new technologies and greater efficiency. And, this was accomplished without layoffs. The workplace environment is improving, with grievances awaiting arbitration down by 61 percent. Accidents are down by 36 percent. These results can all be directly tied to our 2002 Transformation Plan—a plan that continues to be our guide and that we are in the process of expanding and extending—with the help of our stakeholders—through fiscal year 2010.

We remain focused on aggressively managing our business. Our employees are doing an exceptional job utilizing resources efficiently while holding down costs. This focus will not change.

Yet, our success continues to hide the long-term structural problems that are impeding the viability of our outdated business model. Designed to meet the needs of a 1970's marketplace, this business model assumes that the revenue from continually rising mail volumes will offset the costs of an ever-growing delivery base.

The model worked well for the marketplace it faced at the time it was created—long before the advent of electronic communications such as e-mail. Then, we faced little competition in hard-copy mail and package delivery. At that time, the Postal Service was granted a limited monopoly to protect its universal service mandate—that is, the ability to provide quality, affordable mail service to every single home and business in America.

While this model has served the American people well for the past 35 years, communications and normal business practice have undergone profound structural change. Today, we face a competitive marketplace for hard-copy mail and package delivery services. As businesses and individuals make ever greater use of electronic communications to place orders, pay bills, obtain account information and communicate with friends and loved ones, their use of the mail continues to decline.

Since 2000, First-Class Mail volume, which provides the highest contribution to overhead, has fallen by almost 5.6 billion pieces. These changes are evidence that the value of our monopoly has diminished. As recently as 2002, First-Class Mail was by far the largest component of the mailstream. Over the past 4 years, First-Class Mail volume has declined 5.4 percent while advertising mail volume has grown 6.1 percent. However, it takes nearly three pieces of advertising mail to generate the same contribution as one piece of First-Class Mail.

Last year, First-Class Mail was less than half of total mail volume and we expect that this year, for the first time in Postal Service history, Standard Mail will overtake First-Class Mail as our largest-volume product. The shift in the mail mix from First-Class Mail to lower revenue-per-piece mail has significant implications for our long-term bottom line. At the same time, the number of deliveries continues to grow. In 2004, we expanded our delivery network to accommodate 1.8 million new addresses. That base grew by 1.9 million the year before. Structural changes in societal and business communications have altered the economics of our business model. We are squeezing the margins within that model's narrow parameters.

Without modernization of our business model, the opportunities for savings and efficiencies can only decline and the only available alternative to cutting costs is raising rates. Raising rates normally has a negative effect on volume growth. We could find ourselves in a vicious cycle—a cycle of rising rates forcing volumes to decline which would then force additional rate increases to cover the continued expansion of delivery points. Ultimately, the service that America expects could be in jeopardy.

We have filed a request for a rate increase in 2006. This across-the-board rate filing is not a function of revenue failing to meet operational costs. We expect to end this year in the black, with positive net income of more than $1 billion. There would be no need to raise rates before fiscal year 2007 were it not for the $3.1 billion escrow funding required by Public Law 108–18. However, the Postal Service must now begin the process of seeking a rate increase to comply with the requirements of Public Law 108–18, the Postal Civil Service Retirement System Funding Reform Act of 2003. The Act adjusted Postal Service payments to the Civil Service Retirement System so that we would avoid over funding our obligations to the program.

It also stipulated how the so-called "savings" we realized under the Act were to be used. In reality, those "savings" are the difference between our former, higher payment rate that would have resulted in over funding, and the current, lower rate. From 2003 to 2005, the "savings" realized under the Act were used to reduce debt, offset operational expenses and hold postage rates steady. Beginning in 2006, however, the Act requires that we pay $3.1 billion to an escrow fund.

Postal reform legislation under consideration in the House and Senate would eliminate this escrow fund, but require payments to pre-fund future health benefit liabilities. We will continue to monitor the costs associated with pending legislation and reassess our rates requirements for 2006 as appropriate.

Over the past 2 years, we have seen a broad consensus—among government leaders, legislators, the mailing industry, customers and postal employee organizations—about the need for reform of the laws governing the Postal Service.

The administration and both houses of Congress have explored new business models for the Postal Service. The Postal Service's goal throughout this process has been to identify a model that will protect the ability of all Americans to continue receiving affordable, universal mail service well into the 21st century.

I look forward to continuing my discussions with this subcommittee and others as we work to find a business model that is best for our customers, our economy and our Nation. We must define this business model now—before we face a crisis in the Postal Service.

And speaking of now, I am also here today with more immediate needs—our appropriations request for fiscal year 2006. This request covers funding for revenue forgone and free and reduced rate mail, as well as additional funding to complete the system modifications that will improve mail safety and security for our employees and for the American people. Our request differs from the amounts recommended by the administration's fiscal year 2006 budget in several ways.

Our first request is for $29 million for revenue forgone reimbursements. The administration's budget does not include funding for the Federal Government's own debt to the Postal Service for services required by statute. In accordance with the Revenue Forgone Reform Act of 1993, the Postal Service is to receive $29 million annually through 2035. This payment covers the cost of services we were required to provide in fiscal years 1991 through 1993, but for which there were insufficient amounts appropriated. It also covers payment for services provided from fiscal year 1994 through 1998.

For two decades after the creation of the Postal Service, Congress continued to fund reduced postage rates for certain categories of mail and mailers through the so-called "revenue forgone" appropriations. Congress required that the Postal Service provide reduced postage rates as well as free mail for purposes which Congress considers to be in the public interest. These favored types of mail included reduced-rate bulk standard mail advertising sent by qualified non-profit organizations, and in-county mailings of local newspapers. These appropriations were devoted entirely to the benefit of these historically-favored mailers, and did not financially benefit the Postal Service.

Under the provisions of the Revenue Forgone Reform Act of 1993, approximately half of the former taxpayer subsidy to non-profit mailers was transferred to regular-rate postal customers, and that portion of the "revenue forgone" subsidy was ended. In this same legislation, Congress authorized a series of 42 annual appropriations of $29 million, without interest, as reimbursement for $1.2 billion in costs incurred by the Postal Service ($515 million in past under-funding of revenue forgone plus the cost of phasing reduced postage rates to higher levels over 6 years, under the Revenue Forgone Reform Act). The outstanding balance on this debt is approximately $870 million. This year's appropriation would be the thirteenth in the series of 42 annual payments to reimburse the Postal Service the $1.2 billion owed for these purposes. Failure to fund this authorized appropriation places the remaining debt of nearly $870 million at risk of nonpayment.

As the Postal Service continues to responsibly address its long-term obligations, it is counter-productive to increase those costs through non-payment of a debt already deferred by interest-free installment payments spread over a period of 42 years.

The second part of our request is for $108.5 million in payment for costs imposed on the Postal Service by statute. This $108.5 million is for current year costs of $79.9 million and a $28.5 million reconciliation adjustment for prior years. This appropriation reimburses the Postal Service for the statutory obligations to provide free mail for the blind and others who cannot use or read conventionally printed materials, the mailing of absentee balloting materials that can be mailed free by members of the armed forces and other United States citizens residing outside of the United States, and balloting materials that can be mailed in bulk between State and local election officials.

This request differs from the administration's budget request of $87.3 million. The administration provides $58.7 million for current year costs plus a $28.5 million reconciliation adjustment. The administration's proposal not only provides an amount less than that requested, but also continues an "advance funding" process adopted in recent years of deferring actual payment of the recommended funding until the following fiscal year.

Although this approach provides limited funding for these services, these funds are only made available long after the service has been delivered. These actions place the postage ratepayer at a greater risk of absorbing a social service cost beyond the mission of the Postal Service. The Postal Service does not have the authority to control or limit these mailings to reduce the funding needed. And we have no way to mitigate the shortfall in funding. Providing less than the requested amount will continue to compound the financial burden caused by the current "advance" funding.

The third part of our appropriations request is for costs associated with the nationwide deployment of the Biohazard Detection System, the Ventilation and Filtration System, and a Mail Sanitization Facility to be located in the Washington, DC area. We are requesting $51 million to complete these initiatives. The administration's budget does not include funding for the Postal Service's efforts to improve the safety and security of the Nation's mail system. In the past 2 years, we have accomplished significant improvements in our emergency preparedness. For example, we successfully decontaminated and re-opened major mail-processing facilities in Washington, DC, and Trenton, New Jersey—rehabilitation projects on a scale never before attempted.

While we agree that funding for homeland security needs must be prioritized, the Postal Service believes that funding to continue efforts to improve the safety and security of the mail for postal employees and customers should be one of those priorities.

I appreciate the support we received for these important initiatives during the 108th Congress, when funding of $503 million was appropriated to continue these efforts. While those funds will permit the Postal Service to continue to purchase and install state-of-the-art Biohazard Detection Systems and Ventilation and Filtration Systems in our mail processing centers, additional funding is needed to complete this installation process. The Postal Service will continue to cover the operating expenses for these systems from our operating budget.

Both the administration and Congress have recognized that supporting the costs for postal system changes has been a critical element in the enhancement of the security of the Nation. These costs have been—and should continue to be—funded by the government as part of its homeland security activities. These are not costs that should be borne by postal ratepayers.

The Postal Service has dedicated its resources to identifying the best and most effective approach to detecting biohazards in the mail. Our Biohazard Detection System continuously gathers air samples as mail passes through the initial pinch point in the mail processing system. Sample analysis occurs at intervals of approximately 1 hour, followed by a 30-minute analysis cycle. The test intervals help assure that no mail will leave a facility before the analysis is completed.

To date, these Biohazard Detection Systems have performed over 625,000 tests involving more than 12 billion pieces of mail. There have been no false positives. These systems allow for quick response to a positive test result, triggering the local integrated emergency management plan, which includes cessation of operations and facility shutdown, and notification to community first responders, including local public health officials who would make any medical decisions regarding potentially exposed employees and customers.

These automated systems, developed in conjunction with experts from the Federal Government, the military and the private sector, provide rapid on-site analysis of aerosol samples collected during one of the earliest stages of mail processing. These systems are now operational at 114 locations. By the end of the calendar year, this equipment will be deployed in every State of the Nation, at all of our 282 major processing centers.

Since the initial development of the Biohazard Detection System concept, the Postal Service has actively sought to improve this flexible and expandable system. New, improved components of this system are being developed to detect threats in addition to anthrax.

A new technology with promise for expanding our detection ability uses electrochemical luminescence, "ECL". ECL technology has the capability to detect both biological agents and toxins, such as ricin, that escape detection by our current testing process. ECL hardware and software were integrated into an existing system in March 2004. The technology is being tested to determine its level of sensitivity and reliability before the Postal Service proceeds further. As was the case with previous BDS testing, the Postal Service is working with the U.S. Army at the Edgewood Arsenal facility.

We have also moved forward with the deployment of a Ventilation and Filtration System that, used in conjunction with the Biohazard Detection System, will isolate and contain mail-borne biohazards. The Ventilation and Filtration System draws air across the surface of letter and flat canceling systems through a series of ducts, and ultimately into High Efficiency Particle Air (HEPA) filters capable of trapping one-to-three micron-size anthrax spores, as well as a variety of other potential contaminants that might be released in mail processing operations.

In addition, we are finalizing our plans for the construction of an irradiation facility here in Washington to minimize the delays involved with rerouting government mail to New Jersey for this purpose. The construction of this Mail Sanitization Facility will reduce Postal Service costs and improve mail service to Congress and the Federal Government.

The Postal Service is currently spending approximately $800,000 of its own funds each month to irradiate mail destined for Congress, the White House and Federal Government agencies in Washington, DC. Irradiation is conducted at a leased sanitization facility in New Jersey. In addition to the cost to truck mail to the New Jersey facility, this procedure causes 2–3 day delays in mail delivery. We have not requested funding for these costs in the past, nor will we now request funding for these costs.

The emergency preparedness funds we are requesting today would enable an enhanced level of protection for our Nation. Through the field testing phase of the Biohazard Detection System, the Postal Service has forged important and productive partnerships with government and public health officials at the Federal, State and local levels. With the events of recent years, the historic responsibility of the Postal Service to safeguard the Nation's mail, and those who deliver it, has greatly expanded. We carry this trust all across America, at each Post Office and every postal facility, and at every address in the Nation. Your favorable consideration of this appropriations request will help us to fulfill this role to the best of our ability.

In closing, I should note that the Postal Service takes great pride in its success in funding postal operations solely through the sale of postal products and services. While we are authorized by statute to request a public service appropriation every year for costs incurred in providing effective and regular postal services nationwide, even in communities where Post Offices may not be deemed self-sustaining, we have operated without this appropriation since fiscal year 1982, saving the American taxpayers more than $11 billion. Again, for fiscal year 2006, we are not requesting an appropriation for public service.

Thank you, Mr. Chairman and members of the subcommittee for the opportunity to discuss our fiscal year 2006 appropriations request. I would be pleased to respond to any questions at this time.

OFFICE OF PERSONNEL MANAGEMENT

PREPARED STATEMENT OF HONORABLE DAN G. BLAIR, ACTING DIRECTOR

FISCAL YEAR 2006 PERFORMANCE BUDGET FOR THE OFFICE OF PERSONNEL MANAGEMENT

Mr. Chairman and members of the subcommittee, I appreciate the opportunity to submit for the record a statement addressing both the appropriations request for the Office of Personnel Management (OPM) for fiscal year 2006 and the significant administration initiatives we intend to pursue in furtherance of the President's management agenda.

To provide some context for the President's request for appropriations for OPM, I would like to review briefly the progress we have made during the last year, particularly in developing new human resources management systems for the Departments of Homeland Security (DHS) and Defense (DOD), and to outline the plans we have to extend that progress throughout the civil service.

First, our joint development, with DHS, of the new human resources management (HRM) system for that department was unprecedented from the standpoint of the joint regulatory process through which the system was established. In addition, the collaborative process through which those regulations were developed included employees and managers and the largest labor organizations representing the department's employees, as well as numerous Federal and private experts and stakeholders. The final regulations were published on February 1, 2005.

Simultaneously, we have been engaged with DOD in the development of their National Security Personnel System (NSPS), building on the experience we had gained through the DHS process. The proposed regulations for NSPS were published on February 14, 2005, and the comment period ended on March 16, 2005. The many comments received are currently being analyzed and will be considered in the development of the final regulations that will establish the new system.

Having learned from those experiences, we are now uniquely positioned to apply those lessons in a thoughtful and creative fashion throughout the civil service. Consistent with administration policy, we will be developing legislative proposals to modernize the systems and authorities available to the remaining Federal agencies. In a more specialized arena, we will be working to identify whether additional separate legislative proposals are needed for law enforcement officers (LEO's).

As with the new systems in DHS and DOD, implementation activities are a crucial part of OPM's role with regard to other recently-passed legislation. The Federal Workforce Flexibility Act made significant changes that will require complex adjustments in pay and leave administration practices. In addition, the new pay-for-performance system for the senior executive service (SES) requires certification of agency performance appraisal systems, as well as extensive guidance on issues relating to SES performance management and administration.

In addition, the intelligence reform legislation enacted last year authorized the director of the Federal Bureau of Investigation (FBI) to establish career positions for intelligence analysts within the FBI, to establish an FBI reserve service for the temporary reemployment of former FBI employees during periods of emergency, and to extend, for a limited period, the mandatory retirement age for FBI employees to 65. We will be working with the FBI to facilitate the implementation of those intelligence reforms.

The introduction of new dental and vision benefits for Federal employees and annuitants will require additional efforts this year.

Also, the acceptance of the transfer of personnel security investigations functions from the Defense Security Service constitutes an immensely important responsibility, creating in one place a single unit to conduct the vast majority of background investigations for the entire Federal Government. As a result, to carry out personnel investigations, an additional 1,686 employees were added to OPM's rolls to date as a result of the transfer of function, and the workload has drastically increased, as well.

We will also continue to engage agencies in implementing the human capital standards for success as they transform their human capital management practices, consistent with the merit system principles, veterans' preference, and other critical standards. The standards for success were developed jointly with the Office of Management and Budget and the Government Accountability Office. Through the compliance program, OPM will ensure that merit system principles are preserved and honored.

In addition, we will be working closely with agencies to strengthen their human capital accountability systems. As additional human resources flexibilities are being made available to agencies, there is a greater responsibility for accountability at the level within each agency where authorities are delegated and decisions are made. Strengthening accountability Government-wide helps ensure adherence to merit system principles and results in efficient, effective, and responsible administration of Government services.

Again in 2006, OPM will assess the effectiveness of its strategic human resources policy activities by administering the Federal human capital survey, and by continuing to track and report the extent to which agencies are using flexibilities such as direct hiring authority, teleworking, and student loan repayments.

Among our most extensive and forward-looking responsibilities is the implementation of a Human Resources Line-of-Business (HR–LOB) common solution. Transition of our current OPM-managed e-Government projects into a single framework will leverage economies of scale, while reducing costs and increasing the quality and consistency of service provided.

In fiscal year 2006, the request for resources for e-Government initiatives funded from salaries and expenses, including Enterprise Human Resources Integration (EHRI), and e-Payroll, is more than $4 million below the amount provided in fiscal year 2005, including no-year and 3-year funding.

For basic operating expenses, OPM's general fund request totals about $124.5 million, to support 998 full-time equivalent (FTE) employees. These overall resources will enable OPM to continue to support the transformation of agencies in more effectively managing human capital while increasing their accountability; to modernize HRM systems to streamline hiring, and link pay more closely to agency missions; and to improve both employee security and emergency response coordination. Included are nearly $114.2 million in annual funds and slightly more than $10.3 million in no-year funding for the e-Government initiatives described earlier, including EHRI, e-Payroll, e-Training, and HR–LOB.

In transfers from the benefits trust funds, OPM is requesting $100.0 million in annual funds to support 1,151 FTE engaged in the administration of the employee retirement and insurance programs.

Additionally, we will continue working to establish contracts to implement the major activities of the retirement systems modernization project. That strategic initiative will replace OPM's legacy systems with modern technology, moving from paper to electronic recordkeeping and reengineering business processes.

It should be noted, too, that the funding for the Office of the Inspector General (IG) is derived, in significant part, from transfers from trust funds. While the request for that office will be discussed in more detail in a separate statement, it bears mentioning that their overall request totals more than $17.9 million and 140 FTE. The bulk of that funding, $16.3 million, would represent transfers from trust funds, with $1.6 million coming from general funds.

Notwithstanding our independent relationship with the IG and his fine staff, we continue to work cooperatively on issues of mutual interest, including maintaining the integrity of our benefits trust funds and monitoring the Combined Federal Campaign. We strongly support and greatly appreciate the work of his office on such important matters.

OPM also provides a variety of ongoing services that are financed by other agencies through our revolving fund. These services include providing one-stop access to high-quality e-Training products and services; offering professional development and continuous learning for Federal managers and executives; providing employment information and assessment services; automating other agencies' staffing systems; providing examining services when requested by an agency; providing technical assistance and consulting services on all facets of HRM; testing potential military personnel for the Department of Defense where it is cost-effective for OPM to do so; managing the selection, coordination, and development of Presidential Management Fellows; and conducting investigations for all employees to determine whether they are suitable for employment, as well as more in-depth investigations for employees whose positions require a security. For those ongoing revolving fund responsibilities, the fiscal year 2006 budget includes an estimated $1.1 billion in obligations and 2,734 FTE to be financed through payments for OPM's services by other agencies.

Since OPM serves as the "employing agency" for Federal annuitants, the OPM budget request also includes, as always, mandatory appropriations to fund the Government contributions to the health benefits and life insurance programs for those individuals.

A "such sums as may be necessary" appropriation is requested for each of these accounts because of the mandatory nature of those payments. For the 1.9 million annuitants participating in the Federal Employees Health Benefits Program, we estimate that about $8.4 billion will be needed to pay the Government's share of the cost of coverage. That represents an increase of $570 million over fiscal year 2005. We estimate that, for the 500,000 annuitants under age 65 who elect post-employment life insurance coverage, an appropriation of $36 million will be required.

It is also worth noting that the President's budget proposes to use pension savings provided to the Postal Service by the Postal Civil Service Retirement System Funding Reform Act of 2003, Public Law 108–18, savings that would otherwise be held in escrow in 2006 and beyond, to begin funding the substantial Postal Service liabilities for its annuitants.

Under this plan, the Postal Service would make payments for its accruing actuarial costs of post-retirement health benefits coverage for its current employees, and amortization payments needed to liquidate its liability for the post-retirement health benefits coverage of its current retirees.

Also, as mandated by the financing system established in 1969 by Public Law 91–93, liabilities resulting from changes (principally pay raises) since that year that affect retirement benefits must be amortized over a 30-year period. For that purpose, we are requesting a "such sums as may be necessary" payment to the Civil Service Retirement and Disability Fund in the amount of $26.6 billion dollars. This represents an increase of $400 million to cover the service cost of the Civil Service Retirement System which is not funded by and for active employees.

Finally, the President's fiscal year 2006 budget proposes a pay increase for white-collar Federal employees of 2.3 percent, to be distributed between an across-the-board raise and locality pay, as determined by the President later in the year. Once again, the Government-wide general provisions in the budget include the appropriate legislative language to ensure that, if warranted by local private sector market rates, blue-collar Federal employees receive pay adjustments up to the amount received by their white-collar colleagues.

Thank you again for the opportunity to provide for the record a discussion of OPM's budget request. I would be pleased to provide any additional information the subcommittee may need.

PREPARED STATEMENT OF HONORABLE PATRICK E. MCFARLAND, INSPECTOR GENERAL

FISCAL YEAR 2006 APPROPRIATIONS REQUEST FOR THE OFFICE OF THE INSPECTOR GENERAL AT THE UNITED STATES OFFICE OF PERSONNEL MANAGEMENT

Mr. Chairman and members of the subcommittee, thank you for providing me with this opportunity to discuss the President's fiscal year 2006 request for appropriations for the Office of the Inspector General (OIG) at the Office of Personnel Management (OPM). The total request for the Office of the Inspector General is $17,943,000, which is the same amount enacted in fiscal year 2005. Of this amount, $1,614,000 is from the salaries and expenses/general fund and $16,329,000 is from the trust funds. These resources are requested to perform our core functions which include:

—Conducting audits of agency programs and operations, primarily carriers participating in the Federal Employees Health Benefits Program (FEHBP), associated information systems, and internal agency operations and financial systems.
—Providing investigative oversight of the OPM-administered employee benefit programs.
—Issuing administrative sanctions, including debarments, suspensions, and civil monetary penalties, to health care providers who pose a financial risk to the FEHBP itself or a health care risk to persons who receive health insurance coverage through the FEHBP.

The Office of the Inspector General recognizes that oversight of the retirement and health and life insurance trust funds administered by OPM is, and will remain, its most significant challenge. These trust funds are among the largest held by the United States Government. Their assets totaled $670.7 billion in fiscal year 2004, their receipts were $115.1 billion, and their annual outlays were $81.8 billion. The amounts of their balances are material to the integrity of the Government's financial position. I continue to allocate the vast majority of the Office of the Inspector General's efforts and resources to trust fund oversight, and we remain fully committed to trust fund activities.

OPM makes outlays from the retirement trust funds in the form of payments to millions of annuity recipients. The health benefits trust fund provides payments to approximately 260 health insurance plans nationwide. In turn, the health insurance carriers pay millions of claims for services filed by their enrollees and health care providers. We have shown through our investigations and audits that such health insurance payments may be at risk through improper, inaccurate or fraudulent claims.

We are obligated to Federal employees and annuitants to protect the integrity of their earned benefits. Our audit and criminal investigative work reduces losses due to fraud and improper payments and recovers misspent funds whenever possible. We have a special obligation to the Federal agencies and the American taxpayers who provide the majority of the funding.

The Office of the Inspector General has achieved an impressive record of cost effectiveness. Audits and criminal investigations of the OPM-administered trust fund programs have resulted in significant financial recoveries to the trust funds and commitments by program management to recover additional amounts. Since fiscal year 1992, these recoveries and commitments total $1.1 billion which is approximately $10 of positive financial impact for each direct program dollar spent. During fiscal year 2004, the positive financial impact exceeded $95 million, and current estimates for fiscal year 2005 and fiscal year 2006 are $135 million and $130 million respectively. In addition, we believe that audits and criminal investigations provide a significant deterrent against future instances of fraud, waste, and abuse.

With the additional resources received over the past few years, the Office of the Inspector General has established 21 investigative field offices. We have determined that the most effective deployment of investigative staff is to locate them in areas of the country where FEHBP and retirement benefits are more concentrated. Experience has shown that criminal investigators located in these areas often work in cooperation with other law enforcement entities similarly located resulting in additional criminal leads and better protection of OPM programs. In many instances, criminal investigators located outside of Washington, DC, work exclusively on cases referred to them by local authorities.

During fiscal year 2006, we will continue to conduct audits of pharmacy benefit managers (PBMs). It is estimated that approximately $6 billion was paid during 2004 in prescription drug premiums to experience-rated carriers by the Office of Personnel Management and Federal employees. This represents approximately 27 percent of experience-rated carrier premiums paid for health benefits coverage for Federal employees and annuitants. The premiums paid for prescription drug coverage have risen exponentially over the last 10 years. However, we did not begin to audit prescription drug benefits until late fiscal year 2004, because the FEHB Program historically had defined health care providers and suppliers as other than Federal subcontractors. Since PBMs were not subcontractors, they were not subject to our audits. In light of increasing expenditures on prescriptions and allegations against PBMs, the FEHB Program recently promulgated regulations that will bring PBMs under the umbrella of the FEHB Acquisition Regulation and subject them to audit requirements currently applicable to carriers and their subcontractors.

While we are still conducting the initial PBM audit, we believe that it will result in the FEHBP recovering inappropriate costs charged to it in previous years.

Also during fiscal year 2006, we will further our development of a data warehouse of health benefits claims. A data warehouse offers the best opportunity for detecting erroneous health benefit payment transactions by medical providers, insurance carriers and subscribers by accumulating all benefit claims for all fee-for-service insurance carriers in a single data repository. This effort will enhance our current claims reviews by enabling the auditors to target certain types of potential claim payment errors on a program-wide rather than on a plan-by-plan basis. This will provide a significant improvement in our audit efficiency and effectiveness by offering us the opportunity to address significant issues one time only, instead of multiple times per year and to recover overcharges to the program when appropriate.

The data warehouse will provide information enabling our criminal investigative staff to react quickly to criminal investigative leads. For example, the OIG investigators will be able to determine the potential program risks associated with an identified provider or subscriber fraud allegation, and take appropriate action in a matter of hours instead of the days or weeks currently required.

Our administrative sanctions program has continued to improve its effectiveness in protecting FEHBP and its enrollees against untrustworthy health care providers. This program enforces the FEHBP sanctions statute, which authorizes suspension or debarment of providers on the basis of 18 different categories of violations. The most frequently-encountered violations represent criminal convictions or loss of professional licensure. The highest priority sanctions cases involve providers who are the subject of investigation by our Office of Investigations. We have also developed a state-of-the-art capability to obtain sanctions-related information online and integrate it into our decision-making processes. With the nature and extent of electronically accessible information constantly growing, we are now able to identify violations involving providers nationwide who are directly associated with FEHBP as members of preferred provider organization networks and or who have actually submitted claims to FEHBP carriers. We select cases for action on the basis of the seriousness of the provider's violations and the risks that the provider poses to FEHBP and the persons who obtain their health coverage through it.

Thank you for this opportunity to present my resource request for fiscal year 2006.

UNITED STATES INTERAGENCY COUNCIL ON HOMELESSNESS

PREPARED STATEMENT OF PHILIP F. MANGANO, EXECUTIVE DIRECTOR

I appreciate the opportunity to present testimony on the work of the United States Interagency Council on Homelessness ("Council") and our budget request for fiscal year 2006.

The Council was authorized in 1987 in the McKinney-Vento Homeless Assistance Act but had been dormant for nearly 6 years before being revitalized by the administration in 2002 in accordance with the fiscal year 2001 VA/HUD/Independent Agencies Appropriations Act. That Act extended the Council's authorization to October 1, 2005. The administration is requesting that the authorization for the Council be extended and has included a $1.8 million budget request for the Council in fiscal year 2006.

The Council is taking an approach to homelessness that is based on partnerships, collaboration, accountability, and results. The full Council, comprised of 20 Cabinet Secretaries and Agency directors, has held six meetings. A seventh meeting is expected this summer at which time a new Chair will be elected. Over the past 3 years, chairmanship of the Council has rotated among the Secretaries of Housing and Urban Development, Health and Human Services, and Veterans Affairs. Rotating the chair among the members is in accordance with an amendment to our statute included in the fiscal year 2001 VA/HUD/Independent Agencies Appropriations Act and has had both substantive and symbolic meaning, reflecting the reality that homelessness has many causes and that solutions to homelessness are not fashioned through any one agency but only through collaborations by all.

The Council's work is supported by an Executive Director and seven professional and administrative staff in Washington. Our efforts are augmented by eight regional coordinators, who are programmatically supervised by the Council and administratively supported by the Department of Housing and Urban Development.

In his February 2 State of the Union Address, the President underscored the need to restrain spending in order to sustain economic prosperity. As part of this restraint, it is important that total discretionary and non security spending be held to levels proposed in the fiscal year 2006 budget. For fiscal year 2006, the President's budget requests $1.8 million for the Council, a $300,000 increase over fiscal year 2005 and the first proposed budget increase for the Council since fiscal year 2003. The new level of funding is largely accounted for by expenses the Council will incur in meeting a congressional directive to move into independent space from our temporary space at the Department of Housing and Urban Development headquarters building.

Through our work, the Council is seeking to establish a new standard of expectation around the issue of homelessness. That new measure requires that resource investments should do more than just "manage" the problem. We expect those investments to result in visible, measurable, quantifiable change in our communities, on our streets and in the lives of homeless people. Since enactment of the McKinney Act in 1987, billions of dollars have been spent by the Federal Government and other billions have been spent by State and local governments and philanthropy on this issue. But the fact is that despite the expenditure of these funds, there has continued to be tens of thousands of persons living long term on the streets, in encampments and in our shelters.

Now the administration has set a new marker on homelessness, the goal of working in partnership with States, localities, faith-based and community groups, as well as business to end chronic homelessness. The chronically homeless are the most vulnerable and disabled, those most visible and long term on our streets and in shelters. We also are now learning through research that they are some of the most expensive people to the public purse.

To meet our expectations of visible, measurable, quantifiable outcomes, our efforts are being guided by a management agenda, implemented in partnership across Federal agencies and with other levels of government and with the private sector, faith based organizations and homeless people. We are focusing resource investments on a strategy made whole that includes not only intervention activities but prevention initiatives. Our intent is to identify, create and invest in the most innovative initiatives that are research and data driven, performance based and results-oriented.

The administration's marker to end chronic homelessness calls for us to embrace the moral, spiritual and economic obligations we have to taxpayers and to those homeless people on the streets. Chronic homelessness is the most visible form of homelessness in our country, and is most often the result of individuals' disabilities. People experiencing chronic homelessness are the people we see in doorways or under bridges day after day, year after year. They populate homeless death lists across our country. Over the last few years, research has shown that those experiencing chronic homelessness are in fact a finite group representing only 10 percent of the adult homeless population. However, they consume over 50 percent of all emergency homeless shelter services and ricochet randomly around the acute side of very expensive primary and behavioral health care systems. As a result, persons experiencing chronic homelessness are some of the most expensive people to the public purse in communities across the country.

—In Seattle, 1,200 persons experiencing chronic homelessness were tracked for 1 year through emergency rooms and behavioral health care systems. Cost of those 1,200 for that 1 year: $12 million or $100,000 per person.

—In Asheville, Buncombe County, NC, 10-year planners analyzed the service use of 37 homeless men and women over a period of 3 years and found that these individuals cost the city and county more than $800,000 each year including 1,271 arrests generating $278,000 in jail costs, 280 episodes of EMS services for a cost of $120,000, and hospitalization costs of $425,000.

—The University of California at San Diego followed the service use of 15 chronically homeless people for 18 months. They reported 300 emergency room visits, taken by ambulance and accompanied by EMTs, using multiple day stays and they quantified behavioral health costs (substance abuse and mental health) and law enforcement. Total cost? $3 million over 18 months or an average of $200,000 per person.

—The Boston Health Care for the Homeless Program tracked 119 persons experiencing chronic homelessness over 5 years and discovered that they had over 18,000 emergency room visits at an average cost of $1,000 per visit.

—Two concerned Reno police officers tracked the services use of just two homeless persons they repeatedly encountered over 1 year. When the officers examined law enforcement, emergency room and other hospital costs, they found that each person cost over $100,000 a year.

Just as the cost-benefit analysis and research has been helpful in quantifying the costs associated with chronic homelessness, so too has the research been helpful in identifying interventions that are effective in ending chronic homelessness. Research shows that permanent supportive housing strategies in tandem with multidisciplinary, clinically based engagement strategies, and including employment counseling and job placement as appropriate, can be successful in sustaining tenancies for this population. These models of housing, which involve a rich array of supportive services, are effective in moving those experiencing chronic homelessness off the streets and out of long term shelter stays into sustainable tenancies and toward recovery and self sufficiency. That's the basis of the intervention in a growing number of cities across the country, including New York, San Francisco, Columbus, Ohio and Chattanooga, Tennessee.

The administration's goal of ending chronic homelessness is based on learning from—and acting on—that research. At the inaugural meeting of the revitalized Council, the Secretaries of HUD, HHS and VA announced an historic joint funding initiative, that now totals $55 million, as the first infusion of Federal resources targeted specifically toward the goal of ending chronic homelessness. More than 100 applications were received from communities across the country and awards were made to 11 community partnerships.

Along with the Federal funding partners, the Council has continued to monitor the results from this investment. To date, the 11 community partnerships have successfully housed over 600 persons. Cumulatively, the men and women housed under the Collaborative Initiative represent over 3,900 years of homelessness ended and tens of millions of dollars in ad hoc health care, corrections and other community costs incurred during their years of homelessness.

The administration submitted legislation for fiscal year 2005 for a $70 million Samaritan Initiative as a follow-on to the successful Collaborative Initiative effort. While it was disappointing that the Congress did not enact this legislation, the administration has a new proposal in the fiscal year 2006 budget for the Department of Housing and Urban Development that would provide up to $200 million for a new Samaritan Housing Initiative to provide new housing assistance paired with services. This proposal is included in the administration's proposed legislation to consolidate HUD's homeless assistance grants programs, which would provide grant recipients with greater local control, flexibility and streamlined requirements.

The HUD/HHS/VA Collaborative Initiative described above is just one of a number of Federal collaborations that demonstrate the continuing and deepening commitment of a wide array of Federal agencies to get the job done. HUD and DOL have collaborated in an effort to combine employment training with housing assistance in the Ending Chronic Homelessness through Employment and Housing Initiative. DOL and the VA are collaborating to target homeless veterans. HUD, Labor and the Justice Department are partners in the administration's Prisoner Re-entry Initiative. Through its Homeless Outreach Projects and Evaluation (HOPE), the Social Security Administration has funded 41 new projects across the country to increase access to Supplemental Security Income and Social Security disability benefits for persons experiencing chronic homelessness who are disabled by severe and persistent mental illness, HIV, cognitive impairments or co-occurring disorders. Receiving these benefits for which they were eligible by virtue of their disability has allowed these chronically homeless individuals to leave the streets and shelters, have a place to live, obtain medical care and move toward greater self sufficiency.

The additional resources and interagency collaborative efforts are evidence of the administration's ongoing commitment to ending chronic homelessness and are an important indicator of the Federal Government's good faith in the intergovernmental partnerships we are developing with cities and States. The administration's strategy is built on the recognition that no one Federal agency, no one level of government and no one sector of the community can prevent and end homelessness alone. That's why the Council is working to establish an expansive range of partnerships, public and private, between Federal agencies, statehouses, city halls and county executive offices, downtown associations, Chambers of Commerce, faith based and community organizations, the United Way, YMCAs, providers and advocates and homeless people themselves.

I am pleased to report that our efforts to establish intergovernmental partnerships to end chronic homelessness and reduce the incidence of all homelessness have been welcomed by Governors, Mayors and County Executives across the country who have committed to the creation of State Interagency Councils on Homelessness and to 10-Year Plans to End Chronic Homelessness.

Fifty-two Governors of States and territories have acted in response to our encouragement to create State interagency councils on homelessness. These State interagency councils mirror the work of our Council by providing a formal framework for State secretariats and agencies to examine resource allocations and ensure better coordination of State resources and Federal block grant funding in their States for the benefit of homeless people. The creation of these State interagency councils builds on the investment by several Federal agencies including HUD, HHS, VA and Labor in a series of Policy Academies that have been offered to States since 2001 on improving the access of homeless people to mainstream resources.

The Council's regional coordinators and staff have provided technical assistance to facilitate the creation of these State interagency councils. This technical assistance has included mentoring and peer models as well as producing and distributing a Step-by-Step Guide to Developing a State Interagency Council on Homelessness. In fiscal year 2005 the Council has been holding a series of regional colloquies for State policymakers.

In addition to our work in helping to foster State interagency councils on homelessness, the Council recognizes that communities are on the frontlines of homelessness and we are working with mayors and county executives to develop outcome-oriented 10-year plans to end chronic homelessness.

One hundred ninety-two mayors and county executives across the country, including 46 of the largest 50 cities, have heard and responded to the call to create these plans. These mayors and county executives are working with the Council, with their State officials, with their Chambers of Commerce and other downtown associations, with their faith based and community organizations, with providers and advocates and with homeless people to create business plans that quantify the problem, focus resources on permanent solutions that are evidence-based, and track the results. With technical assistance from the Council, the "legitimate larceny" of innovative ideas is seeding the best outcome oriented plans from coast to coast. Moreover, through these local planning processes, the private sector is being re-engaged. New resources from business and philanthropy are being invested in these plans. Nowhere is that more tangible than in Atlanta where Mayor Shirley Franklin's plan has attracted $16 million from private philanthropic giving in the past year and a half.

This jurisdictionally-based 10-year planning effort has been endorsed by the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties, the International Downtown Association, the United Way, and national homeless advocacy groups, all of whom have passed resolutions or offered direct assistance in support of the goal of ending chronic homelessness and encouraging communities to develop 10-year plans.

Just this past January, a Covenant of Partnership to End Chronic Homelessness, shaped by the Council to assist local plan implementation, was adopted during the Hunger and Homelessness Task Force meeting of the U.S. Conference of Mayors, led by Nashville Mayor Bill Purcell and Cedar Rapids Mayor Paul Pate. Mayors who sign the Covenant commit to collaborating with each other on an ongoing basis to exchange data to better quantify the number of chronically homeless persons, share best practices, try innovative solutions, and track their progress. Sixty-two mayors have signed the Covenant, representing communities as large as Philadelphia, San Diego and Dallas and as small as Henderson, North Carolina (population: 17,000) demonstrating that chronic homelessness is not solely an issue in a few urban areas.

The Council has produced and distributed a guide to facilitate the development of these plans, "The Ten Year Planning Process to End Chronic Homelessness in Your Community: Step by Step Guide" and Council staff are providing substantial direct technical assistance to communities. We are encouraging the use of the "Killer Bs" in the 10 year planning process—a business plan that is created around a management agenda that establishes baselines to quantify the problem, benchmarks to remedy and is attentive to budget. For fiscal year 2005 and 2006, the Council plans to increase the number of jurisdictions undertaking, and most importantly, completing and implementing results oriented 10-Year Plans to End Chronic Homelessness. Council staff will now support not only the creation of such plans, but will also work to insure that the implementation is results-oriented.

THE CONTINUING WORK OF THE COUNCIL

In fiscal year 2006, the Council will continue our efforts to end the national disgrace of chronic homelessness and to make homeless resource investments strategic and results oriented.

The Council will continue its statutory activities of Federal homeless program review, governmental and private programs evaluation, information distribution, and provision of technical assistance.

During the last year, the Council has launched a weekly e-newsletter that is being sent to over 7,000 Federal, State and local government, and non-profit, business and philanthropic decision makers. The e-newsletter provides rapid dissemination of timely information on Federal resource competitions, access to the latest Federal research and technical assistance reports, the weekly notice of Title V McKinney-Vento surplus properties, and information about replicable State and local government homeless prevention and intervention efforts.

The Council will continue to foster new collaborative prevention and intervention funding opportunities among Federal agencies as well as monitor those initiatives already underway to document outcomes and identify innovative and best practices.

The Council will continue to create national partnerships with communities and philanthropic organizations as it has with the International Downtown Association, the United Way, NAMI, and the Rockefeller Foundation.

The Council will continue working through its regional coordinators to bring together the regional representatives of the various Federal agencies as Federal Regional Interagency Councils to mirror the work of the Federal partners in Washington.

The Council will continue to strengthen the Federal partnership with State and local governments. Our goal is that every State and territory will develop a functioning State interagency council on homelessness and we are closing in on accomplishing this goal with 52 governors having already made the commitment. Our goal is to have more than 250 cities and counties create and implement 10-Year Plans to end chronic homelessness by the end of fiscal year 2006. We will continue to seek out the innovative and results oriented strategies and programs existing in this country and in other nations to disseminate to States and communities.

In these intergovernmental partnerships, our aim is to ensure jurisdictional accountability for outcomes and results in reducing the number of people experiencing chronic homelessness on our streets and long term in our shelters.

As is the case with myriad of other issues and problems facing States, counties and cities, the responsibility rests with elected and appointed jurisdictional CEOs and leaders to provide the planning and leadership to overcome the difficulties in partnership with community and faith based groups.

The Council will continue to develop the ICH website, www.ich.gov, as the central Federal website on homelessness and will work with member agencies to improve navigation to homelessness information on their sites. We have recently upgraded our website to include a special Innovations section that provides more detailed descriptions of innovative ideas and replicable efforts to eliminate homelessness. Among the subjects covered are successful innovative partnerships that incorporate a broadening base of stakeholders; permanent housing strategies; prevention and discharge planning; employment; and health care access strategies for homeless people. We also archive the weekly e-newsletter on the website.

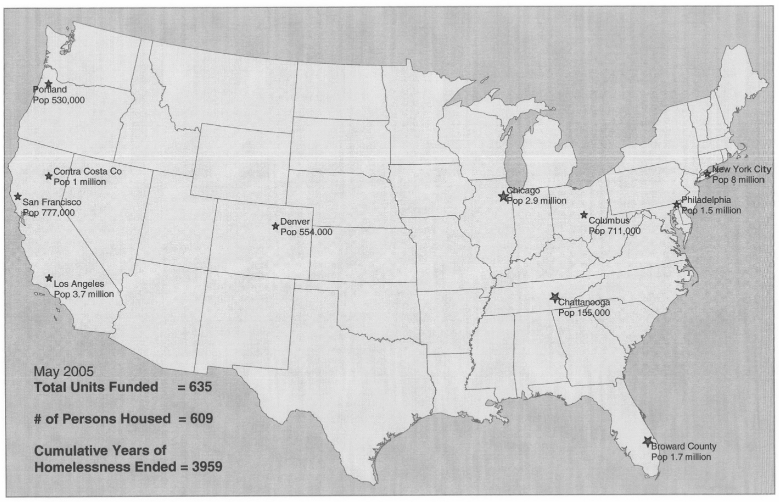
The Council will continue to support and monitor research underway by Federal agencies and others to ensure that Federal homelessness policies and activities are driven by the latest research findings.

Guided by a management agenda that incorporates a broad spectrum of partnerships, cost benefit analysis, outcome measurement data, sharing of evidence based practices, performance based investments, strengthened prevention, results oriented interventions, and targeted resource investments like the Samaritan Initiative, the partnership fostered by the Council's activities are providing a blend of Federal, State, county, city and private sector resources to accomplish the mission.

Our work together in the Council is to disrupt the status quo of homelessness—crisis interventions that are expensive and inefficient in reducing and ending chronic homelessness. Through a management agenda that prioritizes research, performance and results, and through interagency, intergovernmental, and intercommunity partnerships, ending chronic homelessness is achievable.

HUD/ HHS/ VA COLLABORATIVE INITIATIVE TO HELP END CHRONIC HOMELESSNESS

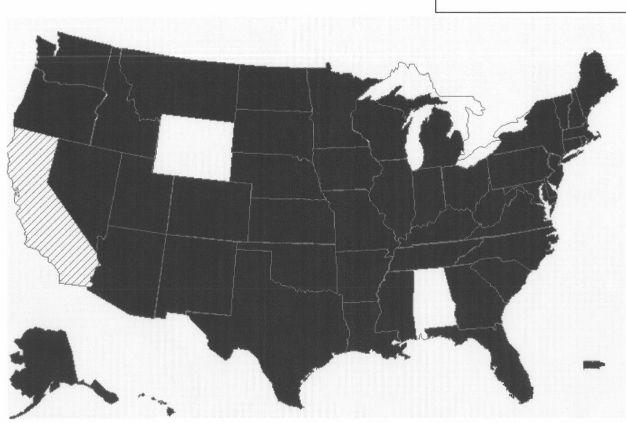
$55 Million Federal Investment: $20 Million Housing
$30 Million Behavioral Health and Other Services
$ 5 Million Veterans Case Management



UNITED STATES INTERAGENCY COUNCIL ON HOMELESSNESS

Status of State Interagency Councils on Homelessness (May 2005)

KEY:
States with State Interagency Councils
Pending



U.S. OFFICE OF SPECIAL COUNSEL

PREPARED STATEMENT OF HON. SCOTT J. BLOCH, SPECIAL COUNSEL

I am pleased to present testimony on behalf of the U.S. Office of Special Counsel (OSC) and our fiscal year 2006 budget request. I look forward to another productive year working with the U.S. Senate in my role as independent guardian of the merit system of civil service by protecting Federal employees from unfair workplace discrimination or mistreatment, including reprisal for whistleblowing, protecting returning service members' jobs, as well as imposing corrective action to protect those employees and bringing disciplinary action against negligent supervisors.

GOALS

My goals for the agency are: (1) To continue to strengthen the civil service merit system by vigorously enforcing the three statutes for which the Office of Special Counsel bears responsibility: the Civil Service Reform Act, the Whistleblower Protection Act, and the Hatch Act; (2) To provide an intense, more visible level of enforcement of the Uniformed Services in Employment and Reemployment Rights Act (USERRA).

GUIDING PRINCIPLES FOR ACHIEVING THESE GOALS

My top priorities have been an agency-wide focus on backlog reduction, swifter resolution of cases, and raising the visibility and enforcement of employee rights. Soon after taking office, I formed a Special Projects Unit (SPU) to begin to investigate the reasons for the chronic backlog of cases and to find solutions to the problem.

On May 17, 2005, we announced in a detailed response to the Government Accountability Office (GAO) report (GAO 04–36), that we reduced the overall Agency backlog by 82 percent, from 1,121 to 201 cases (in the Intake and Disclosure units) by the end of calendar year 2004. We have also eliminated our backlog of FOIA requests.

We were able to do this without sacrificing quality. We gave a full and fair resolution to all claims and we were able to provide even more justice to complainants. During the backlog resolution project, we doubled the historic percentages of internal referrals for Prohibited Personnel Practice (PPP) cases. This meant an even higher percentage of claims were investigated. For whistleblower disclosures, we nearly doubled the number of cases that were referred back to Agency heads or Inspectors General for further investigation. We also gave a more common sense interpretation of law and enforcement as Congress intended it. The credit for this Herculean effort goes to my career staff that worked long and hard to meet our goal.

We will build on this success by continuing to ask for great energy and focus of the current staff, and by bringing on new talent that is skilled at locating issues and understanding problem solving and keen on protecting rights. In all of this, we will be guided by the understanding that this is being done so that we can better service the merit system and protect whistleblowers. Reaching full authorized strength will enable the agency to operate in a way that prevents recurrent backlogs.

RELEVANT FUNDING FACTORS

For fiscal year 2006, the OSC requests $15,325,000—an amount equal to its net fiscal year 2005 appropriation after rescission—to fund approximately 113 full-time employees (FTE) and related non-personnel costs.

The primary purpose for this level of funding is to manage and process the agency's steadily increasing workload (since fiscal year 2000) of PPP complaints, whistleblower disclosures, Hatch Act matters, and new USERRA cases, and to further reduce remaining case processing backlogs.

I will discuss several specific areas that highlight the growing workload and the need for the agency to operate at its full authorized strength of 113 in order to ensure backlogs do not build up again.

—After a year of analysis of the existing processes and challenges of the agency, under my authority in 5 U.S.C. § 1211 and § 1212, I announced an Agency reorganization plan consistent with OSC's mission, in early January 2005, and utilizing concepts of strategic management of human capital. The reorganization was needed to ensure no future case backlogs would occur and to create internally consistent procedures and case handling. I consulted with all the senior management, career staff, as well as my immediate staff repeatedly throughout the past year.

—Besides implementing critical process improvements, this reorganization powered down decision-making to the well-qualified career staff of OSC. We strengthened the field offices by providing SES leadership and additional personnel to the existing offices. We created a team concept of cross-trained persons in smaller, more agile field offices. We also opened a Midwest field office in Detroit as one of many parts of the reorganization that will help OSC better meet our mission. In addition, we created a Washington, DC field office. We are implementing new standard operating procedures that cut out needless reviews and meetings and power down decision making to those employees in the best position to make decisions, including giving attorney's authority to sign routine letters. This effort is a large undertaking and can only be accomplished with strong SES leadership in the field to ensure that these changes actually occur and become the culture of OSC.

—We have implemented a vigorous new training unit that is starting to cross-train personnel to work in other areas of the law. In the past, the lack of cross-trained personnel was a major impediment to attacking backlogs. Without senior leadership in the field offices, the new standard operating procedures and cross-training would have little chance of success.

—A new customer service unit is being created to better serve the public and Federal employees. Having specific personnel assigned for this purpose will help OSC gain a reputation for better customer service within the Federal workforce.

—The Special Projects Unit will continue to handle the "silent" backlogs in the Investigation and Prosecution (IPD) Division, help prevent recurrent backlogs in other Units, and consider new methods for increasing the efficiency and effectiveness of all other aspects of the OSC. Several of the most experienced OSC attorneys will be assigned to the unit, as needed, to help with these issues. This includes a careful look at the agency's methods of electronic filing.

—Increased use of Alternative Dispute Resolution (ADR) will ensure a continued rate of success with resolving matters through mediation, which benefits employees and agencies and saves resources.

—*Increased cost factors*.—During fiscal year 2006, OSC anticipates incurring several continuing unfunded mandates: the new USERRA demonstration project, increased benefit costs (transit subsidy increases), new requirements for financial statements and audits, significant increase in costs under an interagency agreement for receipt of administrative services. Salaries and benefits make up approximately 84 percent of OSC's operating expenses, so the agency has little ability to reprogram funds when salaries and benefits for authorized FTE exceed appropriations. While these types of costs may be easily absorbed by most agencies' budgets that dwarf OSC's, these types of expenses can materially affect a small agency's ability to achieving goals and core missions.

—*Process automation*.—To be successful in meeting our goals of vigorously enforcing the statutes for which we are responsible, with the least possible headcount, we are moving to further automate several steps within our processes. These steps bear costs in equipment and development resources and significantly contribute to efficiency, and accomplishing our goals.

—*Enforcement litigation*.—The increased amount of litigation necessary to strongly enforce adherence to the statutes also has a cost in terms of employee resources.

—*Outreach*.—Outreach to other Federal agencies is critical to the mission of OSC. Success in outreach obviously generates a greater numbers of complaints, whistleblower disclosures, allegations and requests for assistance than in previous years. I believe our excellent professional staff will rise to the occasion, but agency resources must continually be redirected towards important outreach activities at other agencies.

UNITS' SUCCESS

Complaints Examining Unit (CEU).—The CEU or intake unit, is the foundation of OSC. It is responsible for screening approximately 1,700 PPP cases per year. The cases that have merit and within OSC's jurisdiction are referred to the Investigation and Prosecution Division (IPD). The cases without merit on their face or not within OSC's jurisdiction are closed. It is the largest undertaking of the agency and is where it all begins.

The CEU is a very well organized and efficient unit. The unit has a good mix of personnel between the lawyers and the human resource (HR) specialists. The lawyers bring analytical skills and the HR specialists bring their expertise in Federal human resources regulations.

In fiscal year 2004, OSC received 1,964 new PPP cases compared to 1,791 in fiscal year 2003. We processed 21 percent more in fiscal year 2004—2,093 complaints processed in fiscal year 2004, compared to only 1,732 in fiscal year 2003.

Disclosure Unit (DU).—This Unit had severe backlog issues, and with hundreds of cases sitting in backlog, sometimes for years, justice was not being given to Federal whistleblowers. Although we processed hundreds of disclosures in 2004, a majority of these were slated for closure by my predecessor as low priority cases as far as severity of potential harm and as probable closures that resulted in our giving them a second look and, in some cases, taking a closure and turning it into a referral to agencies. Many of these cases had languished in the Agency for several years, and were the focus of the initial backlog resolution efforts. Even so, we nearly doubled the number of referrals during the same time.

During fiscal year 2004, the Disclosure Unit received a 7 percent increase of disclosures over those received in fiscal year 2003. Many of these disclosures deal with national security issues (some involving complex and sensitive classified material) that have required the work of more than one DU staff attorney.

Management of the DU backlog remains a pressing concern for OSC, which has implemented several measures to improve upon its timeliness in processing whistleblower disclosures. For example, the Disclosure Unit has implemented a priority system for matters received; those priorities are tracked using the agency's automated case tracking system; employees have been detailed to Disclosure Unit work; one additional FTE was placed in the unit during fiscal year 2004 and two FTE have been added to the unit in fiscal year 2005; and, most importantly, the Special Project Unit spent nearly 2 months directly assisting the Disclosure Unit by working cases.

USERRA Investigations and Prosecutions.—Service members that believe that their Uniformed Services in Employment and Reemployment Rights Act (USERRA) rights have been violated can now come directly to OSC with their complaints. Before the new law (Public Law 108–454), members had to go through Department of Labor's investigative process and only after months and even years were then given the option to seek OSC's involvement. Under a 3-year pilot project, OSC will be responsible for investigating half of all Federal USERRA claims made. Partial funding for this will be reimbursed to OSC from DOL. The remainder is unfunded and the agency will have to absorb the costs. This function may require a higher number of staff focused on USERRA cases. OSC has filed two prosecutions before MSPB, the first-ever USERRA prosecutions in USERRA's history at OSC and successfully resolved those cases. OSC is aggressively pursuing the rights of returning service members in this historic time of mobilization and demobilization of Guard and Reserve units.

Hatch Act Unit.—In the past, Hatch Act complaints were in backlog, and investigations would take up to 3 years, during which candidates could already have assumed or left office. In one case, the subject died. Our Hatch Act Unit has reduced backlogs of older cases to a very manageable level, provided a record number of advisory opinions—some 600 more than the prior year, done extensive outreach during an election year and been a model of non partisan enforcement. Truly this unit has embodied principles of good government and deterred coercion and illegality at a time of harsh partisan rhetoric in the country.

In fiscal year 2004, the Unit experienced a 26 percent increase in Hatch Act complaints over the number of complaints received in fiscal year 2003. Likewise, there has been a corresponding increase in the number of alleged Hatch Act violations referred for field investigation.

Thirty corrective actions were taken by agencies as the result of warning letters from OSC. The Hatch Act Unit also generated lengthy MSPB litigation activity, and seven disciplinary actions complaints were filed by OSC in fiscal year 2004.

FOIA.—Freedom of Information Act (FOIA) processing, investigations, and enforcements are also increasing, with a corresponding increase in the labor required to handle them. OSC has eliminated a backlog of over 100 requests that were pending in the agency for too long.

SUMMARY

OSC stands in a good position already in fiscal year 2005—with greatly reduced backlogs but with a critical need to fill the remainder of its vacancies. With requested funding, the Agency will be able to meet the challenge of ever increasing case numbers, prevention of recurrent backlogs, and meeting new mandates such as the USERRA pilot program.

OSC requests $15,325,000 for fiscal year 2006, the same as its fiscal year 2005 appropriation. With this funding, OSC will manage and process the agency's steadily increasing workload. The items below highlight the areas in which this funding will be used:

—1. Increased costs for salaries and benefits;
—2. Staffing up to 113 FTE, with focus on adding critically needed clerical staff, replacing retired investigators, adding attorneys where needed, and freeing up resources to handle disclosure cases and USERRA enforcement cases;
—3. A document management system;
—4. Progress on several other information technology initiatives to comply with requirements for increased security and e-government (described above);
—5. Increased cost to investigate and prosecute a larger share of USERRA cases. A new law, Veterans Benefits Improvement Act of 2004 (Public Law 108–454), provides for a 3-year demonstration project that authorizes OSC to investigate about half of the Federal sector USERRA claims. This project began in February 2005.

The Office of Special Counsel exists to ensure good government. When people behave in ways that do not promote good government, or jeopardize safety and health in the Nation, we must take corrective and disciplinary action. We exist to promote good, efficient, fair government, and integrity for the Nation among the Federal workforce. The fiscal year 2006 budget request will enable OSC to reach its mission to promote good government in an expeditious way.

Thank you for your interest in the Office of Special Counsel.

NATIONAL HIGHWAY TRAFFIC SAFETY ADMINISTRATION

PREPARED STATEMENT OF HONORABLE JEFFREY W. RUNGE, M.D., ADMINISTRATOR

Mr. Chairman, I welcome this opportunity to testify about the Nation's highway and motor vehicle safety priorities, and to present the National Highway Traffic Safety Administration's (NHTSA) budget request for fiscal year 2006. The President has made his top priority the safety and security of the American people. Likewise, Secretary Mineta has made transportation safety his top priority in our Department. We at NHTSA have a constant sense of urgency to reduce fatalities and injuries on our Nation's streets and highways, and we appreciate the support you and your staff give our Agency to help us attack these problems.

Highway safety continues to be a major public health problem in the United States. Motor vehicle crashes account for 95 percent of U.S. transportation deaths and 99 percent of the transportation injuries. Even with the progress that has been made, motor vehicle crashes continue to be the leading cause of death for every age from 3 through 33 years old. I want to report to you on the status of traffic safety, and describe the progress being made, as well as the challenges ahead. I will also lay out NHTSA's priorities for fiscal year 2006, and discuss the resources we need to address these challenges.

We have seen tremendous progress in several areas this past year, but many challenges remain. In 2003, the last year for which we have complete data, the traffic fatality rate declined slightly to 1.48 deaths per 100 million miles of vehicle travel (VMT). In June 2004, safety belt usage reached 80 percent, an unprecedented high. Nonetheless, the number of Americans killed is still unacceptable. In 2003, 42,643 people were killed in motor vehicle crashes.

The Secretary has mandated an ambitious Department-wide goal—to reduce the traffic fatality rate to no more than 1.0 fatality per 100 million VMT by the end of 2008. Due in large part to increasing safety belt usage, we are making steady progress towards that goal. We must also focus on the problem areas that are driving up fatalities and represent major impediments to forcing the fatality rate down—alcohol impairment, vehicle rollover, motorcycle crashes and vehicle compatibility. If we fail to drive down the overall fatality rate, we will have 48,000 deaths a year by the end of this decade due to the increase in vehicle miles traveled. Simply put, we cannot be satisfied with our current progress.

Traffic crashes produce harsh economic consequences for the Nation. The cost to the economy in 2000 was $230.6 billion, or 2.3 percent of U.S. gross domestic product. The economic cost included $32.6 billion in medical expenses, over $50 billion related to impaired driving, and $20 billion (in 2003) for failure to wear safety belts. Only 25 percent of overall crash costs were paid by those involved in the crash.

To address this enormous public health issue, NHTSA is requesting $696.3 million for fiscal year 2006 to fund a balanced program of vehicle and human factors safety. NHTSA's work on our top five priorities—Safety Belts; Impaired Driving; Vehicle Rollover; Vehicle Compatibility; and Traffic Records and Data Improvements—will continue in fiscal year 2006. The fiscal year 2006 budget is consistent with the administration's reauthorization proposal, the Safe, Accountable, Flexible and Efficient Transportation Equity Act (SAFETEA). Furthermore, the budget is performance-based; our programs and funding are linked to clear, measurable safety goals. NHTSA's budget reflects our program priorities, and funds the countermeasures that will have the greatest yield in lives saved and injuries prevented.

Mr. Chairman, the balance of my statement describes the initiatives planned for all NHTSA programs in fiscal year 2006, including the strategies we will implement in each of the priority areas.

SAFETY BELT AND CHILD RESTRAINT USE

The fiscal year 2006 budget proposal for occupant protection is $11.774 million. The effectiveness of occupant restraints is well established. Wearing a safety belt cuts the risk of death in a crash almost in half. Our program for fiscal year 2006 continues support for evidence-based strategies to achieve higher safety belt and child safety seat usage.

The reason for our continued progress is clear. Click It or Ticket, NHTSA's priority safety belt campaign, is reaching new levels of national implementation. Click It or Ticket is not public education "in a vacuum." Our data show that non-users are unlikely to respond to public education alone, but will respond if they perceive a likelihood of a traffic citation. Click It or Ticket is built around high visibility law enforcement activity combined with public awareness. Awareness surveys show very high market penetration, due to the use of paid advertising and earned news media during a nationally coordinated mobilization period. In 2004, 47 States followed the Click It or Ticket model, with law enforcement officers writing citations to those not buckled up during a 2-week period beginning May 24 and ending on June 6. In addition, using funds provided by the Congress, NHTSA purchased $10 million of national advertising to supplement State purchases made with Section 157 funds, for a total of about $20 million in enforcement-related advertising during the mobilization period.

As a result, observed front safety belt use in passenger vehicles increased in 35 States compared with the same period in 2003. Four of these States (AZ, HI, MI, and NV) reduced non-use more than 30 percent. NHTSA estimates that the 2004 belt use increase will save about $900 million annually if the gains can be sustained.

NHTSA and our public/private partners will continue to support the national Click It or Ticket campaign. In 2005, 47 States qualified for grants to fund their Click It or Ticket campaigns. For the third year, Congress appropriated funds for NHTSA to purchase national advertising to support State and local enforcement campaigns. In addition, the 2005 Appropriations Act provided the Agency authority to distribute Section 157 innovative grants before awarding the incentive grants, thus providing States with funding for the May enforcement mobilization. We appreciate the flexibility granted by Congress to ensure funding for the mobilization.

Our data shows that a State's enforcement success is strongly related to the presence of a primary safety belt law. As of April 2005, 21 States have primary belt laws, which allow police to cite occupants solely for failing to buckle up. The remaining States (except New Hampshire which continues to have no adult law) have secondary laws, which allow belt law citations only if police stop motorists for another traffic infraction. States with primary laws can expect use rates 11 percentage points higher than those with secondary laws. Nearly every State that has achieved greater than 85 percent belt use has had the benefit of a primary law. Therefore, the continuing success of driving use rates upward is dependent on the enactment of more primary safety belt laws. We have thus revised our safety belt goal to reflect this reality, basing the goal on the proportion of the population covered by primary belt laws (based on VMT). For 2006, we have refined our forecasting model and set our goal at 82 percent.

If all States enacted primary laws, NHTSA estimates about 1,200 additional lives would be saved annually. To further this goal, the administration has proposed incentive grants, including a grant program offering States substantial benefits for enactment of primary laws or achieving usage rates of 90 percent. States receiving these incentives would have significant flexibility to apply the funds to any highway safety purpose, including infrastructure projects, according to their needs as defined within their Strategic Highway Safety Plan. If the United States were to achieve 90 percent belt use (which is commonplace in other industrialized nations), about 2,700 additional lives would be saved each year. A 90 percent rate for the United States is entirely possible, although unlikely to occur without most States adopting primary belt laws. In 2004, seven States and Territories achieved rates of greater than 90 percent (AZ, HI, WA, OR, MI, CA, and PR).

The occupant protection program also includes demonstrations of new approaches for increasing belt use among high-risk, low-use groups, such as pickup truck drivers, rural residents, teens and other high-risk populations. NHTSA will use the results of these demonstrations to create and refine strategies, programs and materials for use across the Nation. Working with many others in the automotive and safety communities, NHTSA has been successful in maintaining high rates of child restraint use among infants and toddlers. The 2004 National Occupant Protection Use Survey (NOPUS) reported 98 percent restraint use for infants (under 12 months), 93 percent for toddlers (1–3 years), and 73 percent for children ages 4–7. The Agency's child restraint goal has been expanded to include children through age 7, and the target for 2006 is 92 percent restraint use.

Unfortunately, the 2004 NOPUS survey indicates a decrease in restraint use among 4–7 year olds from 83 percent in 2002 to 73 percent in 2004, underscoring the need for continued attention to programs to increase booster seat use. The Agency plans a range of activities to address restraint use by the 4–7 age group, including consumer awareness of booster seat benefits, evaluation of booster seat laws, and a study of booster seat effectiveness. These activities support the goal stated in the Transportation Recall Enhancement, Accountability, and Documentation (TREAD) Act to reduce deaths and injuries by 25 percent among 4- to 8-year-olds by 2006.

IMPAIRED DRIVING

The fiscal year 2006 budget proposal for impaired driving is $11.617 million. The number of alcohol-related fatalities has generally held steady over the past decade. Demographic changes since the early 1990's, specifically a greater proportion of the overall population in age groups most at risk for alcohol-related crashes, have been a major challenge to progress. Fortunately, alcohol-related fatalities dropped significantly in 2003, the first such decline since 1999.

NHTSA is implementing a strategic plan to address the national impaired driving problem. The plan, developed by the Integrated Project Team (IPT) in 2003, is based on analysis of alcohol-related fatalities, information regarding program effectiveness, and input from a range of national impaired driving experts. The plan calls for a comprehensive approach to the problem, including public education, law enforcement, adjudication, legislation, as well as vehicle and roadway based technologies. In 2005 and 2006, NHTSA is focusing efforts on three key areas described in the IPT Report. One of these priorities, highly visible driving while impaired (DWI) law enforcement, will support State efforts to conduct such enforcement on a regular basis and secure law enforcement participation in a coordinated national enforcement mobilization crackdown, under the current theme of You Drink & Drive. You Lose. This effort is aimed toward encouraging people to make the choice to designate a sober driver.

The second priority area is to enhance State and local DWI prosecution and adjudication. Those who have not complied with the social norm of sober driving or responded to highly visible enforcement, require attention by the courts. NHTSA is facilitating the use of designated Traffic Safety Resource Prosecutors, who provide technical assistance to new and/or less experienced prosecutors in prosecuting DWI cases. To date, we have 38 Traffic Safety Resource Prosecutors and NHTSA will expand these efforts in 2006. The Agency will also continue to promote and facilitate widespread adoption of DWI Courts for repeat offenders. DWI Courts follow the Drug Court treatment model, using offender assessments to identify appropriate sentencing and treatment, and enhanced supervision and monitoring to reduce recidivism. We now have 177 DWI courts nationwide. In addition, we are continuing a pilot program utilizing Judicial Outreach Liaisons to improve linkages between judges and State traffic safety professionals. We have three Judicial Outreach Liaisons serving three Regions throughout the country and will expand this effort to two other regions this year. Finally, NHTSA will continue efforts to offer training and education to judges on the seriousness of DWI cases and DWI sentencing.

NHTSA is working with health care professionals across the Nation to implement the third impaired driving priority, medical screening and brief intervention for alcohol abuse problems. NHTSA encourages physicians, nurses, and other health care professionals across the country to practice screening and brief intervention in order to identify problem drinkers and direct them to appropriate treatment before they cause a traffic injury or death.

NHTSA conducted the second nationwide You Drink and Drive. You Lose. crackdown in August and September of 2004. This campaign included almost $25 million of combined Federal and State paid media. Congress provided $14 million in funding for NHTSA to purchase advertising to support the crackdown. NHTSA spent $9 million on airing a national advertisement and $5 million on additional purchases in 13 Strategic Evaluation States (SES). These States, all of which have high alcohol-related fatality numbers or rates, receive special assistance with program design, evaluation, and media support for the You Drink & Drive. You Lose. law enforcement crackdowns. The success of this campaign was evident in the data from 2003. Twelve of the 13 SES States had a decrease in alcohol-related fatalities, accounting for 75 percent of the total reduction in alcohol-related fatalities that year.

NHTSA's evaluations have shown that the use of paid advertisements is clearly effective in raising awareness of the You Drink and Drive. You Lose. impaired driving crackdown. Over 30 percent of drivers saw the advertisement and over 50 percent heard or saw the You Drink and Drive. You Lose. slogan during the 2003 crackdown. The advertising was targeted at age 18–34 males, and our surveys showed higher awareness in this target group than in any other age group, and even higher than among age 18–34 females.

NHTSA has expanded the SES program to include 15 States, from the 13 addressed in 2004. They will continue to be the focus for the 2005 and 2006 crackdowns scheduled for Labor Day holiday periods. NHTSA is supporting the Labor Day 2005 You Drink & Drive. You Lose. law enforcement crackdown through the use of $14 million in national paid media appropriated by this committee. The message and media buy will focus on those who are at highest risk, the 18- to 34-year-old males.

A component of our revised Section 402 grant program would focus significant resources on a small number of States with particularly severe impaired driving problems by creating a new $50-million-a-year impaired driving discretionary grant program. The grant program would include support for up to 10 States with an especially high number of alcohol-related fatalities and a high rate of alcohol-related fatalities relative to vehicle miles traveled and population. A team of outside experts would conduct detailed reviews of the impaired driving systems of these States to assist them in developing a strategic plan for improving programs and reducing impaired driving-related fatalities and injuries. Additional support would be provided for training, for technical assistance in the prosecution and adjudication of driving while intoxicated (DWI) cases, and to help licensing and criminal justice authorities close legal loopholes.

NHTSA believes that this targeted State grant program and supporting activities, together with continued nationwide use of high-visibility enforcement and paid and earned media campaigns, would lead to a continuation of the downward trend in alcohol-related fatalities. Also, through the comprehensive safety planning process, all States could elect to use a significant amount of their FHWA Highway Safety Infrastructure funding, in addition to their consolidated highway safety program funds, to address impaired driving.

NHTSA is continuing the demonstration of a comprehensive statewide repeat offender tracking system. This data system will facilitate tracking by allowing immediate transfer and access of information among relevant State agencies, including law enforcement, the court system, and the motor vehicle departments. Four States (Alabama, Iowa, Nebraska, and Wisconsin) began implementing such systems in 2002. One additional State, Connecticut, began implementation in 2004.

The Agency will continue demonstration projects to develop innovative strategies for reaching high-risk and hard-to-reach populations, especially Hispanics and 21- to 34-year-old males. Approaches such as responsible serving practices, behavior modification through social norming, and safe ride programs will be evaluated in a range of environments.

SPEEDING

The fiscal year 2006 budget request for the Enforcement and Justice Services program is $2.2 million. Of this amount, $500,000 will be allocated to speed management. In addition, $300,000, included in the highway safety research budget, will be spent on speeding-related issues. Over the past several years, NHTSA has focused significant resources and attention on addressing the two leading factors in motor vehicle fatalities and injuries—lack of occupant protection usage and impaired driving. We are now increasing our focus on the third major factor in crash-related fatalities and injuries—speeding. Speeding continues to be cited as a factor in approximately one-third of all crash-related fatalities and is estimated to extract over $40 billion in societal costs annually. Data analysis tells us that the major safety problem with speeding-related crashes does not occur on interstate highways, but on local roadways and collector roads.

The Department has an interdisciplinary Speed Management Team, comprised of members representing NHTSA, FHWA and FMCSA. The Administrators of the three sponsoring agencies directed the Team to develop specific objectives for addressing speed management. The focus of these efforts will be a multi-disciplinary approach addressing engineering, enforcement, and education. The Agency will work with communities to establish a process to set appropriate speed limits, advertise that those limits will be strictly enforced, and enforce them. This process will include assessing factors such as travel speeds, public attitudes, driver behavior, roadway characteristics, enforcement strategies, court sanctions, vehicle technologies, and speed zoning. The Agency will also provide technical assistance and guidance to States in ensuring that speed enforcement technology meets stringent performance standards and operational policies. Additionally, the three agencies are co-sponsoring a National Forum on Speeding in June 2005 to identify gaps in the data, needed research, and effective State strategies to reduce speeding.

MOTORCYCLE SAFETY

The budget request for fiscal year 2006 is $679,000. Even as NHTSA makes progress in reducing fatalities and injuries in passenger cars and light trucks, due in part to increased safety belt usage, there has been a rise in motorcyclist deaths each year since 1997. Our program is guided by recommendations contained in the National Agenda for Motorcycle Safety and our Agency action plan, and focuses countermeasure efforts on impaired riding, training, and licensure. NHTSA will continue to work with national motorcyclist organizations and the motorcycle industry to implement the recommendations in the National Agenda. In May, the Agency will host the first quarterly meeting with national motorcycle leaders and manufacturers to join together in a coordinated effort to improve motorcycle safety. NHTSA has also convened an agency-wide working group to focus on approaches to reduce motorcycle crashes, fatalities and injuries, update the Agency's action plan, and identify future research and data needs.

Critical research initiated in fiscal year 2005 will continue in fiscal year 2006. We are undertaking a pilot study on motorcycle crash causation to test the methodology for conducting a more in-depth study of motorcycle crashes. Our research office is also initiating a study to examine rider impairment at different BAC levels given that alcohol impaired riding remains a major problem. This initiative may shed light on potential strategies for addressing the problem.

Despite our efforts, the Agency faces a daunting task to reduce motorcycle crash fatalities and injuries in the face of continuing State actions to repeal motorcycle helmet laws. Riders who fail to wear approved helmets are 40 percent more likely to suffer a fatal head injury in a crash and three times more likely to suffer a brain injury than those wearing a helmet. Since 1997, six States have repealed their universal motorcycle helmet laws that cover riders of all ages (TX, AR, KY, LA, FL, and PA); many of these include a provision that a rider must carry at least $10,000 health insurance. Observed helmet use in these jurisdictions dropped from near 100 percent compliance to the 50 percent range within a few short months. In each of these States, motorcycle fatality and injury rates increased by far more that the national average. Since 1997, motorcyclist fatalities have increased 73 percent to 3,270 in 2003. According to our projections for 2004, motorcycle fatalities will account for over 9 percent of the U.S. total, increasing from 5 percent in 1997. Motorcyclists over the age of 40 have accounted for the largest increase.

EMERGENCY MEDICAL SERVICES

NHTSA has been a leader in EMS for over 40 years. NHTSA's involvement with EMS System development stems from recommendations made by the President's Committee on Highway Safety in 1960 and again by the National Academies in 1966, and the Highway Safety Act of 1966. For nearly four decades, NHTSA has fostered collaboration and consensus with an array of Federal and non-Federal partners. NHTSA has taken a broad approach in supporting EMS system development, to address the needs of all patients during an emergency—highway crashes, heart attacks, natural or man-made disasters and others. NHTSA has consistently demonstrated its national EMS leadership role including the: development of national training standards and training for all levels of EMS providers, from bystanders to paramedics; implementation of Wireless Enhanced 9–1–1; and a national EMS data base (National EMS Information System—NEMSIS).

The fiscal year 2006 budget request, in the amount of $2.305 million, will support State Emergency Medical Services (EMS) through the development of a voluntary national EMS Scope of Practice Model and national EMS Education standards, initial development of a National EMS Information System (NEMSIS) including a national EMS database to be housed at NHTSA, and facilitation of nationwide adoption of wireless Enhanced 9–1–1 (E9–1–1) deployment. The fiscal year 2006 Highway Traffic Safety grants budget proposes $10 million in EMS grants to State EMS offices to improve comprehensive EMS systems performance and improved care for EMS patients, implementation of EMS data collection, and improved access to wireless E9–1–1. The provision of prompt, high quality emergency medical care to persons injured in motor vehicle crashes is a critical injury control component resulting in a reduction of motor vehicle fatalities and in lessening of injury complications. Since the early 1970's, NHTSA has played a prominent role in improving the Nation's emergency medical services system including the development of national standards for the education of Emergency Medical Technicians. The consensus-based EMS Agenda for the Future, developed and being implemented by NHTSA, is guiding the EMS development efforts of Federal, State and local agencies and national organizations.

Wireless E9–1–1 will improve system performance in caring for injured and ill patients, including faster, more precise EMS response to vehicle crash victims. Nationwide implementation of a modern wireless E9–1–1 system will help provide more coordinated incident management, improve the timely sharing of essential public safety information among all responding agencies, and contribute substantially to the reduction of non-recurring traffic congestion. The national 9–1–1 Implementation Coordination Office, required by the ENHANCE 9–1–1 Act of 2004, will be housed at the NHTSA EMS Division.

Finally, SAFETEA establishes a new $10 million-a-year State formula grant program to support EMS systems development, including 9–1–1 nationwide, and provides for a Federal Interagency Committee on EMS to strengthen intergovernmental coordination of EMS with NHTSA. The States would administer the grant program through their State EMS offices and coordinate it with their highway safety offices. This grant program would result in comprehensive support for EMS systems, and improved emergency response capacity nationwide.

HIGHWAY TRAFFIC SAFETY GRANTS

The fiscal year 2006 budget request of $465 million reflects the administration's reauthorization proposal to streamline the highway safety grant program by collapsing the eight grant programs administered under TEA21 into four programs. The focus is to ease the administrative burden on States and provide maximum flexibility for States to use the funds according to each State's unique safety program requirements. In addition to providing States with great flexibility in the use of highway safety grant programs, the proposal emphasizes accountability. Beyond the basic formula grants, which would remain intact, the administration's fiscal year 2006 budget reflects the proposal to tie additional grants to each States' safety performance such as increasing safety belt use; reducing overall fatality rates; and reducing alcohol-related fatality rates. The proposal also provides financial incentives to States to allocate their highway safety resources based on the development of a multi-disciplinary, comprehensive highway safety plan.

VEHICLE SAFETY PRIORITIES

The Agency's vehicle safety efforts in fiscal year 2006 will be guided by the NHTSA Vehicle Safety Rulemaking and Supporting Research Plan, 2005–2009, January 2005 Update, which was delivered to Congress and posted on the NHTSA website in April, 2005. The Plan identifies the research and rulemaking actions that offer the greatest potential for saving lives and preventing injury. In the vehicle safety area, rollover and vehicle compatibility continue to be our top priorities. Other vehicle safety priorities include preventing crashes through advanced technologies, making large trucks safer, ensuring the safety of hydrogen, fuel cell, and alternative-fueled vehicles, improving child protection, and revising crash tests used for rating vehicles in our New Car Assessment Program. The initiatives in the plan were defined through extensive discussions within the Agency, taking into account the views we have heard via public meetings and comments submitted to the Agency on rulemaking notices and Requests for Comment. We will conduct an annual assessment of the plan. In addition, we review all of the Federal Motor Vehicle Safety Standards (FMVSS) on a 7-year cycle.

VEHICLE ROLLOVER

Rollover crashes are especially lethal; although they comprise only 2 percent of crashes, they accounted for almost one-third of passenger vehicle occupant fatalities (including 59 percent of SUV fatalities) in 2003. Since light trucks account for an increasing portion of total light vehicle sales, deaths and injuries in rollover crashes will become a greater safety problem unless something changes.

Since 2001, NHTSA has provided rollover propensity information on light vehicles to the public, through our New Car Assessment Program, based on the vehicle's static stability factor (SSF). In October, 2003 a dynamic rollover test was added and we began providing a combined rating. We believe this combined rollover rating provides the American public important safety information when choosing a new vehicle and will continue to influence manufacturers to design vehicles that have increased rollover resistance. In fact, since 2001 when the SSF ratings were first used, we have seen vehicle designs that are more rollover resistant. In 2003, 10,376 passenger vehicle occupants died in the United States in rollover crashes, down 3.3 percent from 10,729 in 2002.

New efforts at rollover prevention include investigation of Electronic Stability Control (ESC) devices that are now being introduced into vehicles, for prevention of single vehicle off road crashes that can result in rollover. A recent NHTSA study has shown this technology to have the potential to significantly reduce single vehicle run off the road crashes. Research is currently underway and a rulemaking decision on ESC is planned for 2005.

We estimate there are 225 fatalities and 800 serious head injuries annually resulting from roof intrusion during rollovers. NHTSA will issue a Notice of Proposed Rulemaking to upgrade the roof crush standard in 2005. In 2003, 8,582 occupants died when they were ejected from passenger vehicles and 70 percent of these occurred during rollovers. Occupants stand a much better chance of surviving a crash if they are not ejected from their vehicles. The upgrade to FMVSS No. 214 for side impact protection is expected to result in the fleet-wide installation of side curtain air bags, and represents the first phase of a three-phase approach the Agency is taking to reduce side window ejections. Under the second phase of ejection prevention, we are conducting research and investigating performance requirements for occupant containment for side windows. In the third phase, performance requirements for rollover sensors will be investigated, to ensure that the air bags will deploy in a rollover crash.

The first step to improving safety in rollovers is one that requires no changes to vehicles, the use of a safety belt. Most people killed in rollovers are totally or partially ejected from the vehicle. Safety belts can prevent nearly all of these ejections.

VEHICLE COMPATIBILITY

The vehicle fleet has changed dramatically in the last 20 years, and these changes have given rise to an unprecedented problem relating to vehicle mismatch in vehicle-to-vehicle crashes. The rising popularity of light trucks, vans, and SUVs has made the problem substantially more complex. In the last decade, for the first time, more vehicle occupants are being killed in crashes between passenger cars and light trucks than in crashes involving only passenger cars. In front-to-front or side crashes, where the light truck or van (LTV) strikes the passenger car, passenger car occupants are 3.3 times more likely to die than LTV occupants. While LTVs account for 37 percent of all registered vehicles, they are involved in approximately half of all fatal two-vehicle crashes involving passenger cars. In these collisions, nearly 80 percent of the fatalities are passenger car occupants. We need to address this problem now since LTVs constitute half of all new vehicle sales.

Reducing the hazards associated with vehicle incompatibility is one of NHTSA's top priorities. An IPT Report on Vehicle Compatibility was published in the Federal Register (68 FR 36534, Department of Transportation docket No. NHTSA–2003–14622). The Compatibility IPT made wide-ranging recommendations on ways to mitigate the compatibility problem, including several vehicle, behavioral, and roadway strategies (on which the Federal Highway Administration [FHWA] has the lead). Vehicle strategies include partner protection and self-protection. In addition, under the 1998 Global Agreement Program of Work, as well as under bilateral agreements with Canada, the European Commission and Japan, NHTSA is participating in an exchange of ideas on best regulatory approaches, including the possibility of conducting joint research and testing in support of potential solutions to vehicle incompatibility.

A key action in self-protection is the upgrade of FMVSS No. 214 to improve side impact protection. We published a NPRM in May 2004 and we plan to issue a final rule by 2006. NHTSA estimates that the proposed upgrade, which adds a new pole test to reflect real world collisions in which head injuries are prevalent, will save about 700 to 1,000 lives per year. To improve partner protection, NHTSA is conducting research in 2005 and 2006 to determine good measures of vehicle aggressivity, with a regulatory decision in 2007.

Several manufacturers have joined with the Insurance Institute for Highway Safety to form a technical working group to address this problem. They recently published their plan, which includes the voluntary addition of side air bags and the promise for improved geometric alignment and passenger car safety. We welcome the industry efforts to address vehicle compatibility and their recent voluntary commitments.

CRASH AVOIDANCE INITIATIVES

The NHTSA Vehicle Safety Rulemaking and Supporting Research Plan, 2005–2009, recognizes that the most significant vehicle-based initiatives will rest on advanced technologies that will help drivers avoid crashes, and also reduce severity when crashes do occur. We believe that many of the new technologies that are being introduced voluntarily by manufacturers have the potential to improve safety, such as electronic stability control, crash warning systems, pre-crash sensing systems, adaptive cruise control systems and driver assistance systems. These advanced technologies present a research challenge for the agency, in that the agency must develop proper test and evaluation procedures in order to establish their safety benefits and possible unintended consequences. This will require new, dedicated effort and allocation of resources. Accordingly, the Agency is requesting $500,000 to support a crash avoidance initiative.

NEW CAR ASSESSMENT PROGRAM

The fiscal year 2006 budget request for the New Car Assessment Program (NCAP) is $7.859 million. Providing the public with comparative safety information on new vehicles and child safety seats permits consumers to make more informed safety decisions and provides a market incentive to manufacturers to improve their products.

In fiscal year 2006, NCAP will continue to provide consumers with frontal and side crashworthiness information on approximately 80 percent of new vehicles. In addition, consumers will be provided with light vehicle rollover ratings and child safety seat Ease-of-Use ratings. The agency will also continue to investigate and implement improvements to NCAP tests and how it presents and disseminates the information to consumers. In particular, the agency will publish a final decision on what changes, if any, should occur to the frontal NCAP test to reflect recent upgrades to FMVSS No. 208. Concerted efforts will also be undertaken to promote the SaferCar.gov website and to work with safety partners and various media outlets to increase the awareness and accessibility of the NCAP information.

VEHICLE SAFETY ENFORCEMENT

The Defects Investigation budget proposal is $10.472 million. In 2004, the number of vehicles recalled was the largest in the history of NHTSA. There were 598 vehicle recalls involving 30.6 million motor vehicles, 77 equipment recalls involving 1.2 million items of motor vehicle equipment, three child safety seat recalls involving 357,000 child safety seats, and 16 tire recalls involving 571,000 tires.

With the routine submission of additional manufacturer data pursuant to the requirements of the TREAD Act, NHTSA now has access to a substantially increased amount of Early Warning Data (EWD) to help detect the existence of safety-related problems. The Early Warning Reporting (EWR) rule requires manufacturers to submit aggregate counts of production, warranty claims, consumer complaints, property damage claims, field reports, fatality and injury claims and notices, lists of substantially similar vehicles, foreign campaign information, and copies of non-dealer field reports. The system provides a secure, web-based environment that allows manufacturers to submit their data electronically, Intranet applications for NHTSA staff to monitor incoming data submissions, Intranet and Internet applications for data entry and query, and standard reports. One of the reports enables NHTSA to quickly identify manufacturers that fail to submit complete and timely EWR data. EWR data played a supporting role in identifying a safety defect trend that led to recent recalls of tires and side airbags.

ODI uses the EWD to spot potential defect trends and to provide a basis for requesting additional information from manufacturers. We will review the value of the various types of EWD to identify whether any changes are necessary in the reporting requirements. This study will start after eight quarters of field report data has been submitted (Summer 2006).

ODI keeps all Early Warning Reporting data, Auto Safety Hotline complaint data, investigation data and recall data in an electronic data base named ARTEMIS. ARTEMIS is a state-of-the-art, data management system with interfaces designed to meet the needs of government, industry, and the public. ARTEMIS allows owners of motor vehicles, child seats, and equipment to advise NHTSA of potential safety defects through an internet questionnaire. The public also uses ARTEMIS to find safety information related to recalls, investigations, and technical service bulletins.

Similarly, on a quarterly cycle, industry uses ARTEMIS to submit its early warning data to satisfy the reporting requirements of the Early Warning Rule. ODI staff uses ARTEMIS constantly to query its database of owner complaints and manufacturer data to search for potential safety defects, and to store investigation and recall information.

NHTSA is committed to enforcing compliance with the requirements of the FMVSS through identification and investigation of non-complying vehicles and vehicle equipment. We appreciate the support provided by Congress in fiscal year 2005 to add staff and improve processes for increased enforcement of vehicle lighting requirements. The Vehicle Safety Compliance program proposes funding of $7.727 million to ensure that new motor vehicles and motor vehicle equipment comply with the performance requirements of Federal motor vehicle safety standards and provide the safety benefits intended. The fiscal year 2006 budget request includes support for the Agency's compliance test program, including advanced air bag testing and support of our tire testing facility; development of new test procedures for fuel system integrity, side impact, head restraints and tires; and crash test dummy maintenance, for dummies used in crash testing.

FUEL ECONOMY PROGRAM

NHTSA is committed to enhancing energy security and maximizing fuel savings while ensuring safety and minimizing economic impacts. NHTSA is statutorily required to set new light truck standards for model year 2008 by April 1, 2006. It is possible that NHTSA will set standards for more than 1 model year. A NPRM is planned for Summer 2005. The fiscal year 2006 budget request of $1.3 million will be used to analyze data to determine appropriate light truck standards and possible reforms to the regulations. NHTSA published an Advance Notice of Proposed Rulemaking in December 2003, seeking comment on alternative approaches to reforming the Corporate Average Fuel Economy (CAFE) regulations that would facilitate further improvement in fuel economy without detrimental safety and economic impacts. NHTSA received over 65,000 comments and product plan data from eight manufacturers. Part of the CAFE reform effort includes collecting manufacturer data through model year 2012. These data will be used to set new light truck standards. Reforms to the system may or may not be applied to the 2008 light truck standards.

ALTERNATIVE FUEL VEHICLES—HYDROGEN SAFETY

NHTSA's program for hydrogen, fuel cell, and alternative fuel vehicles is focused on providing critical safety information on hydrogen-powered fuel cell and internal combustion engine vehicles. NHTSA's hydrogen-fueled vehicle safety research includes development of safety performance specifications, test procedures, new technologies, and harmonized safety requirements. Safety information is vital to support the President's FreedomCAR and Fuel Cell Initiative, announced in 2003. NHTSA's safety initiative will conduct risk assessment studies of hydrogen-fueled vehicles. The risk assessment studies will quantify potential failures that could indicate unsafe conditions.

NHTSA's 3-year research plan includes codes and standards, performance testing, emergency response, and rulemaking. The fiscal year 2006 request is $1.35 million. NHTSA created a working group to coordinate hydrogen activities with other DOT-wide initiatives, the Department of Energy, and the California Fuel Cell Partnership. NHTSA is also participating in the United Nation's Economic Commission for Europe (UNECE) World Forum for Harmonization of Vehicle Regulations (WP.29) for development of an action plan for the development of global technical regulations for hydrogen vehicles and is active in the DOE-led International Partnership for the Hydrogen Economy (IPHE), to leverage resources and share information among countries.

CRASH INJURY DATA COLLECTION

To reach DOT's goal of no more than 1.0 fatality per 100 million VMT by 2008, or any future goal, it is absolutely essential that the traffic safety community has better data and makes better use of these data. We must understand the causes of the fatalities, injuries and property damage costs that are occurring now. Accordingly, NHTSA has identified Traffic Records and Data Improvements as one of its five priority programs.

Improving the Federal data (FARS, NASS–GES, and State Data System) is dependent on improving State data. Therefore, NHTSA has requested $50 million for the new Traffic Records/Data Improvement program in fiscal year 2006. The new initiative will provide incentive grants to States to improve their traffic safety data to make them more timely, accurate, complete, uniform, integrated and accessible.

The fiscal year 2006 budget proposes $10 million to continue data collection and processing for a nationally representative Crash Causation Survey, which will provide detailed information urgently needed to identify the research needs for crash avoidance. This effort is critical to understanding the complex events that cause and contribute to highway crashes, the last one having been performed in the 1970's. NHTSA's fiscal year 2006 budget request also includes $469,000 to maintain the base FARS infrastructure and ensure that States will be able to provide continuity of data collection services. The FARS program collects a census data set of all fatal motor vehicle crashes that is used to define data driven highway safety initiatives that contribute to the goal of saving lives and reducing injuries.

Mr. Chairman, this concludes my statement. I thank the committee for its continued support of our safety programs. I look forward to working with you in developing an effective, results-oriented budget that will provide national leadership to solve the major problems of traffic safety.

FEDERAL ELECTION COMMISSION

PREPARED STATEMENT OF MICHAEL E. TONER, VICE CHAIRMAN

Mr. Chairman, Ranking Member Murray, and members of the committee, it is my privilege to present the Federal Election Commission's (FEC's) fiscal year 2006 appropriation request. To begin, on behalf of the agency, I thank you for last year's appropriation. Your bipartisan support of the FEC budget has enabled us to continue to implement the Bipartisan Campaign Reform Act of 2002 (BCRA), which amended the Federal Election Campaign Act of 1971.

Our fiscal year 2006 appropriation request is for $54,600,000, an increase of $2,858,272 or 5.52 percent over our enacted fiscal year 2005 appropriation, and for 391 FTE, the same as our fiscal year 2005 FTE level. This year, as last year, the FEC is seeking only a modest increase over the fiscal year 2005 budget of $51,741,728 ($52,159,000 less the fiscal year 2005 across-the-board rescission). I am pleased to report this request conforms to the President's fiscal year 2006 budget request for the FEC.

The fiscal year 2006 request represents a continuation of fiscal year 2005 funding levels, adjusted for inflation, and salary and benefit increases ($2,531,823 which represents a 6.77 percent increase). As such, it represents a Current Services request for fiscal year 2006, with no additional funds or staff for new programs or initiatives, and represents an overall increase of only 2.28 percent for non-personnel costs. These minimal increases are detailed in our fiscal year 2006 Budget Justification.

It is important to note this budget request does not include funds to implement new Homeland Security Presidential Directive 12, issued on August 27, 2004, calling for a mandatory, government-wide standard secure and reliable identification card. The FEC has estimated the first year cost to implement this program to be between $75,000–$100,000, with some continuing costs thereafter.

In its annual review of legislative recommendations, the Commission has submitted 16 recommendations for legislative action. Five of those were unanimously endorsed as priority recommendations; the remaining 11 as non-priority. The five priority recommendations, in brief, are that Congress: (1) add the Commission to the list of agencies authorized to issue immunity orders under Title 18; (2) increase the record retention period from 3 years to 5 years; (3) add a provision related to enforcement of the Act that makes it a violation for anyone to aid and abet another party violating the Act; (4) make permanent the Administrative Fine Program; and (5) require mandatory electronic filing of Senate reports. The remaining 11 recommendations, while placed in the non-priority category are, nonetheless, supported by the Commission as substantive or technical in nature. We are confident these legislative changes would result in efficiencies, not only for the FEC, but also for the regulated community.

Over the past few years, the FEC has achieved major successes, including meeting statutory and court deadlines for the BCRA implementation and legal challenges to the BCRA, as well as the expansion of the compliance program. These successes are the result of FEC efforts and support from our Congressional oversight committees. In addition, two programs have received accolades from the regulated community—the Administrative Fine Program and Alternative Dispute Resolution (ADR) Program. With the addition of these two programs, we have been able to successfully streamline the enforcement process. It is important to call to your attention that the

Administrative Fine Program will expire on December 31, 2005, unless Congress takes action to either make the program permanent or, at a minimum, extend the program through reporting periods ending on December 31, 2008. The Program has been in place since July 2000 and has worked extremely well, as testified to by many of the regulated community. The timeliness of reporting has improved with every election cycle since its implementation. If the program were made permanent, this would eliminate the need for the Commission to come back to Congress every 2 years seeking an extension.

I now will provide a brief overview of the FEC's three core program areas and relate those areas to the agency's fiscal year 2006 budget request.

DISCLOSURE PROGRAM

The FEC's disclosure program includes not only the review and placement of information on the public record, but also educational outreach, including campaign finance workshops and seminars, a toll-free line for requests on any topic, and automatic fax transmission of our publications 24 hours a day, 7 days a week. FEC meeting agendas and related documents also are available on our web site. Our disclosure program accounts for over a third of the agency's staffing (146.6 FTE), distributed among the Public Records Office, Information Technology Division, Reports Analysis Division, Press Office, Information Office and those sections of the Office of General Counsel (OGC) that formulate proposed regulations and draft responses to advisory opinion requests.

Improvements in productivity, aided by IT enhancements, have enabled the FEC to keep pace with the large increases in Federal campaign finance activity during recent election cycles. Campaign financing has skyrocketed since 1976, when the FEC regulated the disbursement by Federal candidates and committees of $310 million in the first publicly-funded presidential elections. For the 2004 Presidential and Congressional elections, it is estimated that the FEC regulated the disbursement of approximately $5 billion—an increase of more than 1,500 percent in just eight Presidential election cycles. The 2006 cycle, a congressional cycle, should be slightly lower in volume than the 2004 presidential cycle. Every election cycle since 1992 has seen a new record in total spending in Federal elections for Congressional and Presidential elections. With your help, we are building an impressive system capable of handling our Information Technology (IT) needs well into the future. This system offers the capability of instantly updating our campaign finance database and expanding the types of information collected. As you are aware, however, this system is expensive. The average annual cost is about $1 million to maintain the electronic filing system.

With the passage of legislation mandating electronic filing of campaign finance reports, we are seeing benefits of improved timeliness. Since the institution of electronic filing, the median time to process detailed information from all documents received has improved from 12 (2000 cycle) to 6 (2002 cycle) to 3 days (2004 cycle) from receipt of the disclosure reports by the Commission. Due to both the enhanced use of technology and management initiatives, the FEC is processing and reviewing disclosure reports more rapidly than ever, despite the huge increase in the amount of campaign finance funds and information to be processed and disclosed. This provides voters with more accurate and timely disclosure information prior to an election, enabling them to make an informed decision when it comes to the sources and uses of campaign funds by the candidate.

COMPLIANCE PROGRAM

Obtaining voluntary compliance is the foundation of the FEC's strategic and performance plans, and is at the core of our mission statement. A credible enforcement program, however, is necessary to provide sufficient incentive to the regulated community to achieve this voluntary compliance. In fiscal year 2006, we anticipate assigning 181.1 FTE to the compliance function, including enforcement, supervisory and support staff from OGC, Information Technology Division, Reports Analysis and the Audit Division. In the audit track of the compliance program, we are pleased to report sufficient resources have been provided to allow the Commission to initiate 40 to 45 audits "for cause" for the 2004 election cycle, as opposed to 25 in the 1998 cycle. Details on the compliance program are contained in the fiscal year 2006 Budget Justification.

The first major overhaul of the FEC's enforcement program occurred in May 1993. Faced with a large number of complex cases, the Commission developed the Enforcement Priority System (EPS), to prioritize cases for substantive enforcement action. This system is designed to provide a consistent and impartial ranking of cases based on the relative seriousness of the alleged violations, and gives us a tool to match the seriousness of a particular case to the resources available to undertake the investigation. We use the EPS in conjunction with the Case Management System, which enables the Commission to measure performance with regard to the substantive resolution of cases by issue and to measure timeliness of enforcement actions. Under the EPS, the Commission has activated more cases, closed more cases with substantive action, and resolved some cases that would otherwise have been dismissed.

The EPS has enabled the Commission to focus limited OGC enforcement resources on the more important enforcement uses. The increased level of civil penalties assessed by the Commission following implementation of the EPS has demonstrated the benefits of pursuing this course. In fiscal year 1995, there were 229 OGC cases closed and a total of $1,966,600 in civil penalties. By fiscal year 2004, there were 72 OGC cases closed, and civil penalties totaled $3,024,595.

Prior to 2000, the FEC's enforcement program was administered solely by the Office of General Counsel. Since that time, the Staff Director has been responsible for administering two new components of the Commission's enforcement efforts—the Administrative Fine Program and the ADR program. The goal of the ADR Program is to resolve matters quickly and effectively through bilateral negotiations. Both the ADR and Administrative Fine programs are designed to expand the FEC's enforcement presence and resolve certain types of cases without resorting to the more lengthy traditional OGC enforcement process. Today, the Commission focuses its OGC resources on the more complex enforcement matters, while using administrative processes to handle less complex matters. For example, from fiscal year 1995 through fiscal year 2000, the FEC closed an average of 197 cases each fiscal year. In fiscal year 2001, with the addition of the Administrative Fine and ADR Programs, the FEC closed 516 cases, a 163 percent increase over the fiscal year 1995–2000 annual average of 197 cases. In fiscal year 2002, the FEC closed 226 cases, including enforcement, ADR and Administrative Fine cases. (The number of administrative fine case closings is smaller in even-numbered fiscal years.) The total in fiscal year 2003 was 529, and in fiscal year 2004 it was 250 closed cases. We are confident the figure for fiscal year 2005 will be higher than the fiscal year 2003 number.

Since fiscal year 2001, the Administrative Fine Program has resolved 1,009 cases of late and non-filed reports. During this time period the Commission has assessed administrative fines totaling $1,891,148. This program, when viewed in combination with reporting violations resolved through the traditional enforcement process, has resulted in a six-fold increase in the number of reporting violation actions resolved by the FEC.

The ADR program seeks to resolve certain types of matters in a collaborative and expeditious manner. While the potential exists for civil penalties, the focus of ADR is to correct behavior. As a consequence, ADR employs non-financial solutions such as training, adoption by the reporting entity of additional or revised policies and procedures, and audits to reduce the likelihood of future violations.

PUBLIC FUNDING PROGRAM

The Commission also administers the program providing a public subsidy to Presidential election campaigns. During fiscal year 2006, approximately 63.3 FTE from the Audit Division, Office of General Counsel, and Information Technology Division, will be directly involved in this program, which will entail audits of the eight candidates receiving matching funds for the 2004 election. In addition, two general election candidate committees are to be audited, as will two host committees and two convention committees, for a total of 14 Presidential audits. This program began processing matching fund requests for eligible primary candidates in 2003. The first payments occurred on January 2, 2004.

On a related matter, we believe it is appropriate to bring to your attention the potential shortfall in the Presidential Public Funding Program. There was a brief shortfall with the February primary matching payments for the 2004 Presidential election, which was restored the following month with the February deposits to the Fund. This was the only shortfall for the 2004 cycle. We did not experience a major shortfall for the 2004 Presidential election because several major candidates decided not to take Federal matching funds for the 2004 primaries; this may change, however, in future elections. The Treasury Department maintains the matching fund account, which is comprised of money derived from a taxpayer check-off system. Shortfalls in 1996, 2000 and 2004 occurred for several reasons. First, the Treasury Department does not consider expected election-year check-off proceeds to be available for calculating payout resources. Second, while payouts under the program have been adjusted upward, due to inflation, the $3 check-off amount has not been increased since 1993. Third, the number of taxpayers participating in the check-off has been declining. Fourth, the "front-loading" of primaries and caucuses, which puts a premium on early fundraising, has resulted in a high demand for matching payments early in the election year. Finally, the eligibility requirements for matching funds have not been adjusted since 1974, and many candidates can qualify for public funding as a result. Absent legislative action, the shortfall problem will recur in future elections.

The foregoing summarizes the FEC's fiscal year 2006 budget request. For a more detailed review of this request, I would urge members of the committee to consult our more detailed Budget Justification, which includes charts delineating how our budget request would be allocated and how it compares to previous years. It also demonstrates how the FEC has developed and used strategic and performance planning.

Again, I thank you, Mr. Chairman and the committee, for your continued support and the opportunity to present our fiscal year 2006 budget request.

FEDERAL DEPOSIT INSURANCE CORPORATION

PREPARED STATEMENT OF PATRICIA M. BLACK, ACTING INSPECTOR GENERAL

Mr. Chairman and members of the subcommittee, I am pleased to present the fiscal year 2006 budget request totaling $29.9 million for the Office of Inspector General (OIG) at the Federal Deposit Insurance Corporation (FDIC). This OIG budget reflects a decrease for the tenth consecutive year, after adjusting for inflation. This budget has been possible because of the improved health of the banking industry since the early 1990's, the major staff downsizing at the FDIC and within the OIG, and our internal efforts to improve our performance and productivity even with reduced budgets.

As you know, the FDIC was established by the Congress in 1933, during the Great Depression, to maintain stability and public confidence in the Nation's banking system. Our Nation has weathered several economic downturns since that era without the severe panic and loss of life savings unfortunately experienced in those times. The Federal deposit insurance offered by the FDIC is designed to protect depositors from losses due to failures of insured commercial banks and thrifts. The FDIC insures individual deposits of up to $100,000. As of December 31, 2004, the FDIC insured $3.623 trillion in deposits for 8,988 institutions, of which the FDIC supervised 5,263. The FDIC also promotes the safety and soundness of these institutions by identifying, monitoring, and addressing risks to which they are exposed.

The Corporation reports that financial institutions have recently had record earnings. The rate of bank and thrift failures has remained at a relatively low level over the past 10 years, and the Corporation has substantially reduced its estimates of future losses from failures. Assets held in receiverships following bank failures are at comparatively low levels, and significant progress has been made in closing older receiverships. The insurance funds are now comfortably above the designated reserve ratio that could otherwise trigger increases in premiums assessed on insured depository institutions. These are important indicators of a healthy banking system, and the Corporation can take pride in its positive contributions in each of these areas.

The FDIC OIG was established in 1989 in accordance with amendments added to the Inspector General Act. The OIG's program of independent audits, investigations, and other reviews assists and augments the FDIC's mission. Our efforts promote economy, efficiency, and effectiveness of FDIC programs and operations and protect against fraud, waste, and abuse.

In December 2004, Gaston L. Gianni, Jr. retired after serving for over 8 years as the FDIC Inspector General. Since then, I have been the Acting FDIC Inspector General and will continue to dedicate myself to carrying out the mission of the OIG until the President appoints an Inspector General. In this capacity, I look forward to supporting the Congress, the FDIC Chairman, and other corporate management in meeting current and future challenges facing the FDIC and the banking industry.

This statement discusses OIG accomplishments during fiscal year 2004, our contributions to assist FDIC management, internal initiatives to improve the OIG, and management and performance challenges facing the FDIC. I am also providing additional details about our fiscal year 2006 budget and how it will be spent.

A REVIEW OF THE FDIC OIG'S FISCAL YEAR 2004 ACCOMPLISHMENTS

The OIG's fiscal year 2004 achievements include the following:

—$95.8 million in actual and potential monetary benefits;

—137 non-monetary recommendations to FDIC management;
—32 referrals to the Department of Justice;
—24 indictments;
—24 convictions; and,
—4 employee/disciplinary actions.

More specifically, our accomplishments included 56 completed investigations that led to the above indictments and convictions as well as fines, court-ordered restitution, and recoveries that constitute slightly over $40 million from our work. Also, we issued a total of 48 audit and evaluation reports, which included about $4.4 million in questioned costs and $51.1 million in recommendations that funds be put to better use. The nonmonetary recommendations in these reports aim to improve the internal controls and operational effectiveness in diverse aspects of the Corporation's operations, including automated systems, contracting, bank supervision, financial management, and asset disposition.

Further, the OIG accomplished many of its organizational goals during the fiscal year as outlined in our annual performance plan. Our 2004 Performance Report shows that we met or substantially met 31 of our 41 goals, or 76 percent. In a measurable way, this achievement shows the progress we continue to make in adding value to the Corporation with our audits, investigations, and evaluations in terms of impact, quality, productivity, and timeliness.

Audits, Investigations, and Evaluations

Examples of the OIG's audit, investigation, and evaluation work that contributed to these accomplishments follow.

Investigation into Fraud at Hamilton Bancorp and Hamilton Bank, N.A. (Hamilton Bank)

In 2004, a Federal grand jury in Miami, Florida, returned a 42-count indictment for conspiracy, wire fraud, securities fraud, false filings with the Securities and Exchange Commission, false statements to accountants, obstruction of an examination of a financial institution, and making false statements to the Office of the Comptroller of the Currency (OCC). Named in the indictment were three former senior executive officers of Hamilton Bancorp and Hamilton Bank, N.A. and the former Managing Director, Deutsche Morgan Grenfell, and the advisor to Hamilton Bancorp Board of Directors. The indictment alleges that, in 1998 and 1999, the defendants fraudulently inflated the reported results of operations and financial condition of Hamilton Bancorp and defrauded the investing public and the bank and securities regulators, so that the accused would unjustly enrich and benefit themselves through higher salaries, bonuses, and stock options, and would facilitate an upcoming registered securities offering to the investing public.

In February 2005, the former President of Hamilton Bank pleaded guilty of two counts of securities fraud and could get 10 years for each count, a maximum fine of $1 million, and restitution. The three other defendants are scheduled for trial on June 27, 2005. This case is being investigated by the FDIC OIG and prosecuted by the U.S. Attorney's Office for the Southern District of Florida.

Investigation into the Failure of Sinclair National Bank

In August 2004, a Federal jury returned guilty verdicts against a former owner who was also a board member of Sinclair National Bank and the former Chief Executive Officer of Stevens Financial Group. The jury found the former owner guilty of conspiracy to submit a false statement and making a false statement to the OCC during her application for the purchase of a predecessor bank. On September 7, 2001, after only 18 months under new ownership, the OCC closed the bank, and the FDIC was named receiver. Sinclair's failure caused a loss of approximately $4.5 million to the Bank Insurance Fund. The former owner was sentenced to 2 years' probation, fined $5,000, and ordered to surrender her passport.

The former Chief Executive Officer of Stevens Financial Group was found guilty of conspiring to commit bank fraud. Through his company, he sold over $15 million in sub-prime loans to Sinclair National Bank. He was found guilty of conspiracy to defraud Sinclair in the purchase of these sub-prime loans and making false and misleading statements to the Missouri Division of Securities. The Chief Executive Officer was sentenced to 5 years in prison and ordered to pay $4.2 million in restitution.

In November 2004, the former in-house counsel for Sinclair National Bank and Stevens Financial Group was sentenced both in State and Federal court to 5 years' probation and was ordered to surrender his law license.

The Federal case was investigated by the FDIC OIG, Treasury OIG, FBI, and the Missouri Attorney General's Office. The case was prosecuted by the U.S. Department of Justice, Washington, DC.

Audits of FDIC's Allocation of Records Storage Costs and Records Management and Storage

The OIG issued two reports dealing with records management and storage costs that resulted in $51.1 million in funds put to better use. The audit of the FDIC's allocation of records storage costs determined that records storage costs were not correctly charged to the appropriate insurance and resolution funds.

In another audit, we concluded that the FDIC's contract with Iron Mountain Records Management, Inc. for records storage could be more cost-effective. We reported that the FDIC could avoid costs of $5.1 to $5.5 million by moving records from climate-controlled storage, renegotiating certain contract terms, and obtaining permission to destroy thrift records not associated with goodwill litigation. We made recommendations to the FDIC to make the contract with Iron Mountain more cost effective and to improve contract oversight. We also recommended that the General Counsel and Division of Administration expedite efforts related to the destruction of records for thrifts not involved in the goodwill litigation.

Audit Report on Observations from FDIC OIG Material Loss Reviews Conducted 1993 Through 2003

In January 2004, we issued an audit report that discussed the recurring and root causes of failure for the 10 FDIC-supervised institutions that caused material losses to the Bank Insurance Fund (BIF) during the past 10 years. Estimated losses to the BIF from these 10 failures total over $584 million. We concluded that the major causes of failure were inadequate corporate governance, poor risk management, and lack of risk diversification.

Our semiannual reports to the Congress provide many other examples of OIG accomplishments. These reports can be found on our Web page at http://fdicig.gov/reports.shtml or by contacting our office.

Assistance to FDIC Management

In addition to 2004 audits, investigations, and evaluations, the OIG made contributions to the FDIC in several other ways. We strive to work in partnership with Corporation management to share our expertise and perspective in certain areas where management is seeking to make improvements. Among these contributions were the following activities:

—Reviewed 43 proposed corporate policies and 3 draft regulations and offered comments and suggestions when appropriate.

—Provided advisory comments on the FDIC's 2004 Annual Performance Plan and 2003 Annual Report.

—Participated in division-level conferences and meetings to communicate about our audit and investigation work and processes.

—Provided technical assistance and advice to several FDIC groups working on information technology issues, including participating at the FDIC's information technology security meetings. We also participated in an advisory capacity on the Information Technology Subcommittee of the Audit Committee.

—Coordinated with the FDIC's Division of Information Technology and agency officials to establish appropriate processes in addressing cyber crimes.

OIG Management and Operational Initiatives

An important part of our stewardship over the funding we receive includes our continuous efforts to improve OIG operations.

The OIG has continued to downsize with the Corporation. In this environment, the OIG has had to emphasize aligning our human resources to achieve the OIG mission. The OIG will carry out several key initiatives to implement our human capital strategic plan and ensure that the OIG is a results oriented high-performance organization. Many of the planned initiatives relate to staff development and include: creating a mentoring program; providing training and development related to the OIG core competencies and business knowledge needs; and creating a strategy to improve the supervisor-staff feedback process.

During the past year, the OIG published its first comprehensive Employee Survey Report. The survey collected information on how employees who work for the OIG view and appraise their work and workplace. The survey was designed to provide information comparable to certain major benchmark surveys of other government employees.

Other internal initiatives include our hosting an interagency symposium on the Federal Information Security Management Act (FISMA) of 2002. Representatives from more than 40 Federal agencies attended the symposium to share information, ideas, and best practices related to the implementation of FISMA. We also co-sponsored a third Emerging Issues in Banking Symposium with the Offices of Inspector

General of the Department of the Treasury and the Board of Governors of the Federal Reserve System, bringing together distinguished speakers who shared their perspectives on the banking and financial services community with Inspector General staff in the interest of enhancing the value that OIGs can add to their agencies by successfully addressing risk areas. We sponsored the annual conference of the Federal Audit Executive Council, a working group comprised of the heads of Federal audit organizations. This forum helps ensure that Federal audit organizations keep current with auditing standards, practices, priorities, and issues of concern. We also conducted our sixth external customer survey regarding satisfaction with OIG operations.

The OIG's Office of Audits received an unqualified opinion on a peer review of the system of quality control for the audit function of the FDIC OIG. According to the Department of Energy OIG, the system of quality control for the audit function in effect for the year ended March 31, 2004, was designed in accordance with quality standards established by the President's Council on Integrity and Efficiency and provided the OIG with reasonable assurance of material compliance with professional auditing standards in the conduct of the FDIC OIG's audits.

MANAGEMENT AND PERFORMANCE CHALLENGES FACING THE FDIC

In the spirit of the Reports Consolidation Act of 2000, the OIG annually identifies the top management and performance challenges facing the FDIC. We have worked with the FDIC to prepare our annual assessment. The challenges set forth below capture the risks and opportunities we see before the Corporation in the coming year or more. In addition, these challenges serve as a guide for our work.

Corporate Governance in Insured Depository Institutions

Corporate governance is generally defined as the fulfillment of the broad stewardship responsibilities entrusted to the Board of Directors, officers, and external and internal auditors of a corporation. A number of well-publicized announcements of business and accountability failings, including those of financial institutions, have raised questions about the credibility of management oversight and accounting practices in the United States. In certain cases, board members and senior management engaged in high-risk activities without proper risk management processes, did not maintain adequate loan policies and procedures, and circumvented or disregarded various laws and banking regulations. The FDIC's effort in to achieve sound corporate governance without undue regulatory burden remains a management challenge.

Several of our audits focused on issues relating to external governance. One audit focused on the process that the FDIC uses to assess bank management and controls during examinations of FDIC-supervised financial institutions. We concluded that the process is adequate. However, based on our review of six open banks with high-risk composite ratings, we found opportunities for improvement pertaining to banks that have a dominant official with significant influence in bank operations. We made recommendations to address these concerns, and the corrective actions that FDIC management proposed were responsive. We also conducted an audit to examine the FDIC's issuance of implementing guidelines to financial institutions and examiners for applicable provisions of the Sarbanes-Oxley Act. We concluded that the FDIC took adequate steps to issue implementing guidance for applicable provisions of the Act both to FDIC-supervised institutions and to FDIC examiners. In addition, the Act did not have a major impact on FDIC-supervised financial institutions because of pre-existing audit committee and internal control reporting requirements imposed by the FDIC Improvement Act of 1991.

Likewise, our investigative work also addresses corporate governance issues. In a number of cases, financial institution fraud is a principal contributing factor to an institution's failure. Our Office of Investigations plays a critical role in investigating such cases and has been very successful in identifying bank fraud cases involving corporate governance weaknesses.

Management and Analysis of Risks to the Insurance Funds

A primary goal of the FDIC under its insurance program is to ensure that its deposit insurance funds do not require augmentation by the U.S. Treasury. Achieving this goal is a considerable challenge that requires effective communication and coordination with the other Federal banking agencies. The FDIC engages in an ongoing process of proactively identifying risks to the deposit insurance funds and adjusting the risk-based deposit insurance premiums charged to the institutions.

We completed an evaluation of the FDIC's supervisory approach for examining limited-charter depository institutions, which include industrial loan companies. This evaluation was completed in September 2004 and contained eight recommendations for strengthening the quality of the Division of Supervision and Consumer Protection's program for supervising industrial loan companies. In addition, we completed an audit of the Maximum Efficiency, Risk-focused, Institution Targeted (MERIT) Examination Program to assess the adequacy of processes, reports, and other data that the FDIC uses in monitoring MERIT examination coverage of financial institutions.

Security Management

The FDIC relies heavily upon automated information systems to collect, process, and store vast amounts of banking information. This information is used by financial regulators, academia, and the public to assess market and institution conditions, develop regulatory policy, and conduct research and analysis on important banking issues. Ensuring the confidentiality, integrity, and availability of this information in an environment of increasingly sophisticated security threats requires a strong, enterprise-wide information security program at the FDIC and insured depository institutions.

As a result of focused efforts over the past several years, the FDIC has made significant progress in improving its information security controls and practices and addressing current and emerging information security requirements mandated by FISMA. The OIG has completed its fourth annual security evaluation pursuant to FISMA and its predecessor legislation. Also, the FDIC's external auditor, the Government Accountability Office, for the first time in several years did not cite information systems security as a reportable condition in its audit of the Corporation's financial statements. However, the FDIC recognizes that continued improvements in its information security program and practices are needed. The FDIC Annual Report 2004 identified information security as a high vulnerability issue within the Corporation. The FDIC also identified improvements in its information security program as a major corporate priority in its 2004 Annual Performance Plan.

The OIG recently completed an audit of security controls over the FDIC's e-mail infrastructure. In addition, we have completed one audit and a follow-up review of the Virtual Supervisory Information on the Net application. This is a major application that provides access to financial, examination, and supervisory information on financial institutions. FISMA 2005 work is ongoing.

Money Laundering and Terrorist Financing

In today's global banking environment, where funds are transferred instantly and communication systems make services available internationally, a lapse at even a small financial institution outside of a major metropolitan area can have significant implications across the Nation. The reality today is that all institutions are at risk of being used to facilitate criminal activities, including terrorist financing.

On June 3, 2004, the OIG testified before the Senate Committee on Banking, Housing, and Urban Affairs, on Bank Secrecy Act (BSA) compliance and enforcement. Also, in March 2005, we completed an audit that addressed the FDIC's supervision of one institution's compliance with the BSA. This audit determined that responsibilities to ensure compliance with the BSA were not adequately fulfilled by either institution management or the FDIC. Corporate governance at the financial institution and two former institutions was not sufficient to ensure that the institutions met BSA requirements. The FDIC's examinations identified significant BSA violations and deficiencies, but the examinations generally lacked sufficient follow-up on corrective measures promised but not implemented by institution management. Consequently, weak BSA compliance programs persisted for extended periods. In addition, the FDIC should have more thoroughly considered the impact of BSA compliance violation and deficiency histories in connection with its decision to qualify the potential acquirers of a failed institution. The FDIC concurred with our findings and recommendations and is making significant improvements in its supervision of institution BSA compliance programs in response to our recommendations and its own initiatives.

The FDIC anti-money laundering supervision program is a matter for continued monitoring in the FDIC Annual Report 2004. The OIG has additional audits and investigations planned in this area to help ensure that financial institutions, through efficient and effective supervision by the FDIC, will remain vigilant in implementing BSA programs that assist in preventing money laundering and terrorism.

Protection of Consumer Interests

In addition to its mission of maintaining public confidence in the Nation's financial system, the FDIC also protects the interests of consumers through its oversight of a variety of statutory and regulatory requirements aimed at protecting consumers from unfair and unscrupulous banking practices. The FDIC is legislatively mandated to enforce various statutes and regulations regarding consumer protection and civil rights with respect to State-chartered, non-member banks and to encourage community investment initiatives by these institutions.

The OIG's recent coverage in this area includes reviews of compliance with the Gramm-Leach-Bliley Act, Community Reinvestment Act, and the Fair Lending Act. In 2004, we examined the FDIC's Supervision and Appeals Review Committee's decision regarding a financial institution's appeal of a fair lending violation. In addition, we have an ongoing audit on predatory lending.

The OIG's involvement with consumer protection matters includes our investigative cases regarding misrepresentations of FDIC insurance or affiliation to unsuspecting consumers. Additionally, our Office of Investigations' Electronic Crimes Team has been involved in investigating "phishing" identity theft schemes that have used the FDIC name in an attempt to obtain personal data from unsuspecting consumers who receive the e-mails. Our investigations have also uncovered multiple schemes to defraud depositors by offering them misleading rates of return on deposits. These abuses are effected through the misuse of the FDIC's name, logo, abbreviation, or other indicators suggesting that the products are fully insured deposits. Our experience with such cases prompted us to submit a legislative proposal to prevent misuse of the Corporation's guarantee of insurance. This proposal was incorporated in H.R. 1375: Financial Services Regulatory Relief Act of 2003. On March 24, 2004, it was passed by the House of Representatives and referred to the U.S. Senate.

Corporate Governance in the FDIC

Corporate governance within the FDIC is the responsibility of the Board of Directors, officers, and operating managers in fulfilling the Corporation's broad mission functions. It also provides the structure for setting goals and objectives, the means to attaining those goals and objectives, and ways of monitoring performance. Management of the FDIC's corporate resources is essential for efficiently achieving the FDIC's program goals and objectives.

Management of Human Capital

The FDIC, like other organizations, continues to be affected by changing technology, market conditions, initiatives designed to improve its business processes, an aging workforce, and the changing financial environment. Such events impact needed staffing levels and required skills going forward. Workforce management is a matter for continued monitoring in the FDIC Annual Report 2004. Recent OIG work in this area includes an evaluation of the effectiveness of the FDIC's Division of Supervision and Consumer Protection workforce planning and an evaluation of the FDIC Corporate University.

Competitive Sourcing

The FDIC has awarded long-term contracts to consolidate outsourced information technology activities. While these contracts permitted the FDIC to solicit among well-qualified sources under task orders, the FDIC's ability to compete was generally limited to a small number of firms. We recently completed a pre-award audit of these consolidated contracts. We have ongoing work to determine whether the FDIC achieves adequate price competition and complies with the Acquisition Policy Manual's bid solicitation and evaluation requirements.

Improved Financial Management

The FDIC has begun to field a new financial management system in 2005 that will consolidate the operations of multiple systems. Named the New Financial Environment (NFE), this initiative will modernize the FDIC's financial reporting capabilities and cost about $58 million. Implementing NFE and interfacing other systems with NFE will require significant efforts and poses major challenges. We have reported on several NFE matters in the past and are currently monitoring the Corporation's ongoing NFE efforts. We plan to provide audit coverage of NFE implementation after the system is deployed.

E-Government

The FDIC's E-Government Strategy is a component of the enterprise architecture that focuses on service delivery for the external customers of the FDIC. The FDIC issued Version One of its E-Government Strategy in November 2002 and established a task force to update the strategy. The FDIC has initiated a number of projects that will enable the Corporation to improve internal operations, communications, and service to members of the public, businesses, and other government offices. The projects include: Call Report Modernization, Virtual Supervisory Information on the Net, Asset Servicing Technology Enhancement Project, New Financial Environment, Corporate Human Resources Information System, and FDIConnect. We have an audit in process that will determine if the FDIC is adequately implementing E-Government principles in its operations and in its information exchange with insured financial institutions.

Risk Management and Assessment of Corporate Performance

Within the business community, there is a heightened awareness of the need for a robust risk management program. Enterprise risk management is a process designed to: identify potential events that may affect the entity, manage identified risks, and provide reasonable assurance regarding how identified risks will affect the achievement of entity objectives. The migration from internal control to enterprise risk management perspectives and activities presents challenges and opportunities for the FDIC. We recently completed an audit on strategies for enhancing corporate governance and we have two evaluations planned that will assess the FDIC's approach to enterprise risk management and the FDIC's use of performance measures. We also provide input to the FDIC's annual performance plans.

Security of Critical Infrastructure

To effectively protect critical infrastructure, the FDIC's challenge in this area is to implement measures to mitigate risks, plan for and manage emergencies through effective contingency and continuity planning, coordinate protective measures with other agencies, determine resource and organization requirements, and engage in education and awareness activities.

The OIG has performed several evaluations to assess the FDIC's physical security program and information technology (IT) contingency planning. A follow-up to two prior OIG evaluations to assess the FDIC physical security program and implementation of physical security concluded that the FDIC had implemented our recommended improvements to security policies for FDIC-owned and leased space in the Washington, DC area and in the regional and field offices.

With respect to IT contingency planning, the FDIC has continued capability to recover its mainframe and server platforms necessary to restore operations in the event of a disaster. However, testing for data restoration is an area needing continuous attention. The FDIC's Business Continuity Plan addresses critical business functions in key divisions and offices. The Corporation has updated its business impact analysis and updated the plan accordingly. Continued testing and updates of the plan must be part of a sound business continuity planning process. The OIG has further work planned in this area.

Management of Major Projects

Project management involves defining, planning, scheduling, and controlling the tasks that must be completed to reach a goal and allocating resources to perform those tasks. The FDIC has engaged in several multi-million dollar projects, such as the New Financial Environment discussed earlier, Central Data Repository, and Virginia Square Phase II Construction.

We have done several reviews of these projects and identified the need for improved defining, planning, scheduling, and controlling of resources and tasks to reach goals and milestones. Project management is a matter for continued monitoring in the FDIC Annual Report 2004. Also, the Corporation included a project management initiative in its 2004 performance goals and established a Program Management Office to address the risks and challenges that these kinds of projects pose.

Cost Containment and Procurement Integrity

As steward for the BIF, the Savings Association Insurance Fund (SAIF), and the FSLIC Resolution Fund (FRF), the FDIC strives to identify and implement measures to contain and reduce costs, either through more careful spending or by assessing and making changes in business processes to increase efficiency. A key challenge to containing costs relates to the contracting area.

The OIG has performed several audits and evaluations that have addressed procurement issues, all in the interest of enhancing the effectiveness of contracting and reducing costs of contracted goods and services. These audits and evaluations addressed local telecommunications, price reduction on laptop computers, procurement of administrative goods and services, and the FDIC's use of consultants. These audits and evaluations resulted in questioned costs, funds put to better use, or cost savings for the Corporation.

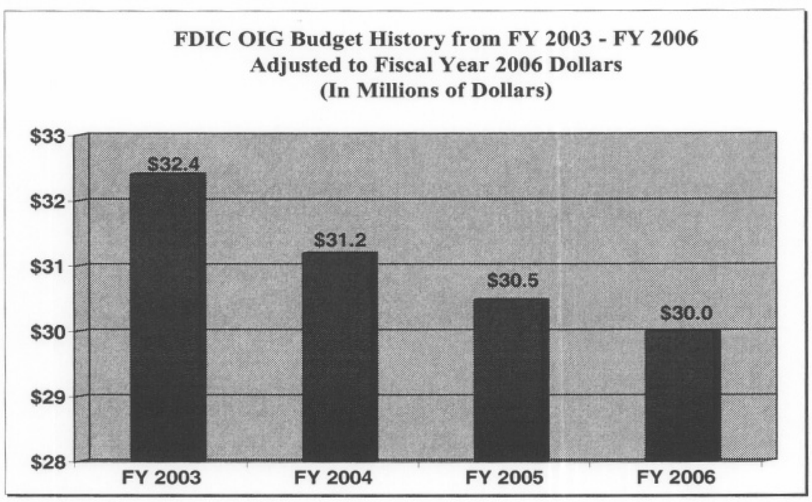
Resolution and Receivership Activities

One of the FDIC's primary responsibilities includes planning and efficiently handling the resolutions of failing FDIC-insured institutions and providing prompt, responsive, and efficient resolution of failed financial institutions. These activities maintain confidence and stability in our financial system. Three of our recent audit reports addressed resolution and receivership activities. These audits addressed internal loan servicing, receivership dividend payments, and asset write-offs and each made recommendations for improvement.

The OIG's Office of Investigations coordinates closely with the FDIC's Division of Resolutions and Receiverships and with the Legal Division regarding ongoing investigations involving fraud at failed institutions, fraud by FDIC debtors, and fraud in the sale or management of FDIC assets. In particular, investigators address issues arising in connection with the prosecution of individuals who have illegally concealed assets in an attempt to avoid payment of criminal restitution to the FDIC. As of September 30, 2004, the FDIC was owed approximately $1.7 billion in criminal restitution. In most cases, the individuals subject to restitution orders do not have the means to pay. We focus our investigations on those who do have the means to pay but hide their assets from and/or lie about their ability to pay.

THE OIG'S FISCAL YEAR 2006 BUDGET REQUEST

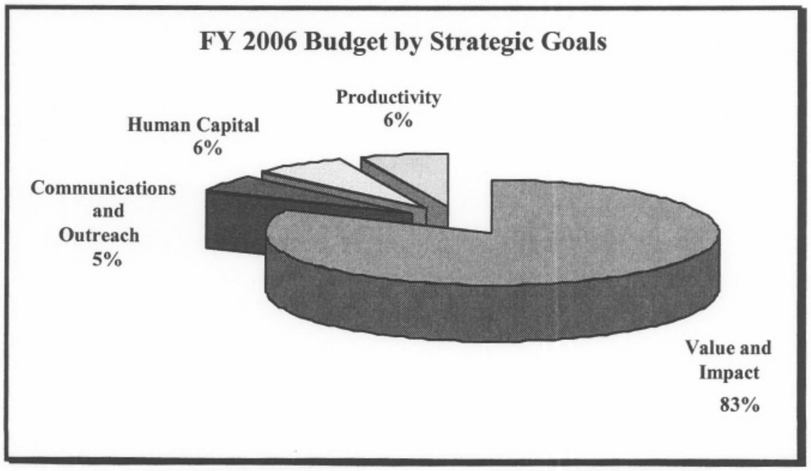
The proposed fiscal year 2006 OIG budget includes funding in the amount of $29,965,000 or $160,000 less than fiscal year 2005. This budget will support an authorized staffing level of 160. Since this budget is less than the fiscal year 2005 budget and will fund the same staffing level, the budget absorbs higher projected expenses for salaries, employee benefits, and other costs that will increase by reducing funds for travel, contracts, and equipment purchases. The graph below shows the OIG's budget history from fiscal year 2003 through fiscal year 2006.



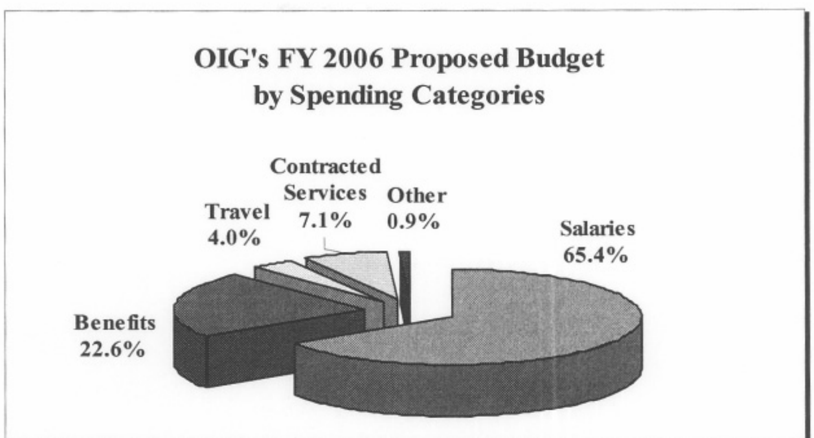
The FDIC OIG has been operating under an appropriated budget since fiscal year 1998 in accordance with Section 1105(a) of Title 31, United States Code, which provides for "a separate appropriation account for appropriations for each Office of Inspector General of an establishment defined under Section 11(2) of the Inspector General Act of 1978." This funding approach is part of the statutory protection of the OIG's independence. The FDIC OIG is the only appropriated entity in the FDIC. The OIG's appropriation would be derived from the BIF, SAIF, and FRF. These funds are the ones used to pay for other FDIC operating expenses.

Budget by Strategic Goals and Major Spending Categories

For fiscal year 2006, the OIG developed the budget based on the four strategic goals outlined in our Strategic Plan found on our Web page at http://fdicig.gov/gpra/StratFY04-08.pdf. The four strategic goals, along with their associated percent of budget dollars follow:



The following chart shows the distribution of the OIG's budget by major spending categories. Mostly, the OIG budget is comprised of salaries and benefits for its employees and the necessary funding for travel and training expenses.



As I discussed earlier, the OIG has continued to downsize during the last few years. The OIG has decreased its authorized level of 190 staff for fiscal year 2003 to 160 for fiscal year 2006—about a 16 percent reduction. Years 2005 and 2006 are critical periods of change for the FDIC, and the OIG resources will be needed to ensure an efficient and effective rollout. However, OIG resource requirements may realize benefits from the FDIC's restructuring and downsizing, which could mean fewer OIG staff and smaller budgets, and we will be reviewing that issue.

CONCLUDING REMARKS

Mr. Chairman and members of the subcommittee, I appreciate the support and resources we have received through the collaboration of the President, the Congress, and the FDIC. As a result, the OIG has been able to make a real difference in FDIC operations in terms of financial benefits and improvements, and by strengthening our own operations and efficiency. I look forward to working with this subcommittee beginning with this budget. Like many governmental organizations, we are faced with downsizing and succession planning challenges for which the OIG will assess whether further downsizing may be necessary. We seek your support so that we will be able to effectively and efficiently conduct our work on behalf of the Congress, the FDIC Chairman, and the American public.

NATIONAL TRANSPORTATION SAFETY BOARD

PREPARED STATEMENT OF MARK V. ROSENKER, ACTING CHAIRMAN

Thank you, Chairman Bond and members of the subcommittee for allowing me the opportunity to present testimony on behalf of the National Transportation Safety Board (NTSB) regarding the agency's appropriation needs for fiscal year 2006. It is truly an honor and a pleasure to represent an agency dedicated to the care and safety of our Nation and it's citizens.

The NTSB is an independent Federal agency charged by Congress with investigating every civil aviation accident in the United States and significant accidents in other modes of transportation—railroad, highway, marine and pipeline—and issuing safety recommendations aimed at preventing future accidents. The Safety Board is responsible for maintaining the government's database of civil aviation accidents; serves as the "court of appeals" for any airman, mechanic or mariner whenever certificate action is taken by the Federal Aviation Administration (FAA) or the U.S. Coast Guard (USCG) Commandant, or when civil penalties are assessed by the FAA; and is tasked with ensuring that transportation disaster survivors and victims' families receive timely, effective, complete and compassionate assistance from the operator, other government agencies, and community service organizations. In addition, the NTSB Academy, now in its second year of operation, provides quality training for accident investigations. The Academy also provides a platform for accident reconstruction and evaluation and uses its training resources to facilitate family assistance and first responder training programs.

Since its inception in 1967, the NTSB has investigated more than 124,000 aviation accidents and over 10,000 surface transportation accidents. In addition, the Safety Board has issued more than 12,000 safety recommendations in all modes of transportation with an 82 percent adoption rate for recommendations made. In fiscal year 2004, the Safety Board issued 151 new safety recommendations and closed 308 recommendations. For the first time since 1975, the number of open safety recommendations is under 800.

ACCOMPLISHMENTS

I would like to begin by highlighting just some of the NTSB's accomplishments in 2004–2005.

—The Office of the Chief Financial Officer achieved an unqualified clean opinion on our audited Consolidated Financial Statements. This is the second year in a row the Board received a clean audit.

—Nearly 2,000 aviation accident investigations were completed by the Office of Aviation Safety, including Air Sunshine flight 527, which ditched into the Atlantic Ocean near Great Abaco Island, Bahamas, causing three minor injuries and two fatalities; two non-fatal crashes involving FedEx freighters—flight 1478, which crashed near Tallahassee, Florida and flight 647, which crashed while landing at the Memphis International Airport in Tennessee; American Airlines flight 587, which crashed into a residential area near Belle Harbor, New York—with 265 fatalities; and Air Midwest flight 5481, which crashed shortly after takeoff at Charlotte, North Carolina with 21 fatalities.

—Six major investigations were completed by the Office of Highway Safety, including a vehicle intrusion into a farmers market in Santa Monica, California resulting in 10 fatalities and 63 injuries; a school bus run-off-bridge accident near Omaha, Nebraska resulting in 4 fatalities; a motorcoach accident and rollover near Victor, New York with 5 passengers killed; the towboat Robert Y. Love allision that collapsed a highway bridge near Webbers Falls, Oklahoma resulting in 14 fatalities and a 15-passenger child care van accident near Memphis, Tennessee with the driver and 4 children sustaining fatal injuries.

—The Office of Marine Safety completed four marine investigations including a fire aboard the passenger ferry, Columbia, in Alaska; the grounding and sinking of a small passenger vessel, Safari Spirit, also in Alaska; the sinking of the small passenger vessel Panther near Everglades City, Florida; and the allision of the Staten Island Ferry, Andrew J. Barberi, off St. George, Staten Island, New York.

—The Office of Railroad, Pipeline and Hazardous Materials Investigations completed over 18 accident investigations.

- —Some of the rail investigations completed included the derailment of runaway railcars near the City of Commerce, California; a CSX freight train derailment and subsequent fire in the Howard Street Tunnel in Baltimore, Maryland; the derailment of an Amtrak train near Kensington, Maryland; the derailment of a Canadian Pacific Railway freight train near Minot, North Dakota; and the derailment of a Canadian National freight train in Tamaroa, Illinois.
- —Major pipeline investigations completed included the release of crude oil and the rupture of a pipeline near Cohasset, Minnesota; and a storage tank explosion and fire in Glenpool, Oklahoma.
- —Major hazardous materials investigations completed included a nurse tank failure and release of anhydrous ammonia near Calamus, Iowa; and the rupture of a rail tank car containing hazardous waste near Freeport, Texas.

—The Office of Research and Engineering supported 292 accident and incident investigations in all modes of transportation; developed four safety studies in issues pertaining to aviation and pipeline transportation; examined over 150 items in the laboratory; and read out more than 160 vehicle recorders and responded to over 2,500 information requests and over 500 FOIA requests.

—The Board, in conjunction with the Office of Safety Recommendations and Communications, testified 32 times in 14 States in 2004 and has already testified 16 times in 9 States in 2005.

—Our SWAT (Safety With A Team) teams held 33 meetings with 7 Federal agencies and 6 industry groups, discussed over 350 recommendations, closing 49 of them.

—The Academy hosted 3 public forums in 2004–2005—Air Cargo Safety, Personal Flotation Devices in Recreational Boating (2004) and Positive Train Control (2005). In 2004, during its second year of operation, the NTSB Academy delivered 15 courses with over 1,000 individuals, including 65 students from 35 foreign countries, in attendance.

MOST WANTED

The Office of Safety Recommendations and Communications is responsible for coordinating strategies for implementing safety recommendations, supporting victims of transportation disasters, keeping the media apprised of important safety developments and ensuring that Congressional, Federal and State government leaders are provided with timely and accurate information. The office also manages the most critical open safety recommendations on the NTSB's list of Most Wanted Transportation Safety Improvements.

The NTSB's Most Wanted list was established in 1990 to increase the public's awareness of, and support for, recommendations having the greatest potential for preventing accidents and saving lives. The Most Wanted list also focuses attention on recommendations that may have become stalled, but if accomplished, would significantly reduce deaths and injuries.

In 2003, the Safety Board separated Federal and State issues on the Most Wanted list to maximize its utility and to allow the Board to focus on a more manageable number of recommendations. In September 2004, the Board Meeting on the Most Wanted List of State issues, the Board reviewed 319 actions emanating from 10 safety recommendations and 197 recommendation classifications, including 173 safety improvements that were completed. Further action, however, still needed by the States includes improving child occupant protection, enacting primary seat belt laws, eliminating hard-core drinking driving, enhancing recreational boating safety and, added to the list during the meeting, improving school bus/grade crossing safety.

The meeting on the Most Wanted List of Federal issues was held in November 2004. Two items were removed from that list: the recommendation for marine voyage data recorders, which was almost complete and the recommendation to enhance the safety of locomotive cab voice recorders, which the Federal Railroad Administration refuses to adopt. The Board also revised the classifications of two FAA responses on runway incursions and aircraft icing from "Open-Acceptable Response" to "Open-Unacceptable Response" because of lack of progress by the FAA. In addition to reducing dangers to aircraft flying in icing conditions and stopping runway incursions, improvements still need to be made by Federal agencies include eliminating flammable fuel/air vapors in aircraft fuel tanks, implementing positive train control, and preventing medically unqualified drivers from operating commercial vehicles.

The Board will review its Most Wanted State issues list in September 2005 and Federal issues list in November 2005. We will keep the subcommittee informed of any changes made during those reviews.

ADVOCACY PROGRAM

The goal of NTSB's advocacy program is to implement safety recommendations. The expeditious implementation of recommended safety improvements remains a priority at the Board. Paramount in our efforts to achieve this goal is our work with the modal administrations of the Department of Transportation to focus on open recommendations, particularly those from our Most Wanted List. The Board's persistence in this endeavor has yielded significant safety benefits. For example, following a series of Safety With A Team (SWAT) meetings, the FAA took positive actions and 7 aviation recommendations were reclassified from open-unacceptable to closed-acceptable or closed-acceptable-alternate. Two examples include A–00–39, which recommended that Air Traffic Control facilities retain recorded voice communications and radar data for 45 days whenever equipment for properly archiving the data is available, was classified closed-acceptable; and A–01–54, which required the use of automatic brakes, if available and operative, on aircraft for landings during wet, slippery, or high crosswind conditions, was classified closed-alternative action. SWAT is a communication plan that seeks to implement open safety recommendations so that they can be closed-acceptable. Safety Board staff meets with appropriate Federal agencies, some of whom staff has never met with before, such as the American Association of State Highway and Transportation Officials, to discuss open recommendations and focus on what causes the delays, objections and issues that are holding up implementation of the recommendations.

With all five Board Members and NTSB staff working as a team, we have seen significant progress in State legislatures advancing the adoption of our recommendations. Each Board Member focuses on advocacy activities in 10 States. Board Members meet with State officials, departments and public advocacy groups to encourage support for our recommendations. From January 2004 to date, Board Members and staff have testified 48 times in 23 different States. During the same time period, 47 States have enacted 14 booster seat laws, 3 primary seat belt enforcement laws, 11 teen driving laws, 8 laws addressing hard core drunk driving, 5 laws to require personal flotation devices for children on boats and 6 laws for mandatory boater education. Since 1993 in response to our safety recommendations, 40 States and the District of Columbia have enacted graduated driver licensing laws, revolutionizing the way States license young drivers. In addition, the Board has provided leadership to several national coalitions promoting recreational boating safety, highway safety and the reduction of hard-core drunk driving.

MAJOR INVESTIGATIONS

Office of Aviation Safety (OAS)

The NTSB is required by law to investigate and determine the probable cause of all of the nearly 2,000 civil aviation accidents and certain public-use aircraft accidents that occur each year.

Earlier I mentioned the accident investigations closed by OAS last year. I would like to briefly discuss two of those accidents—American Airlines flight 587, in Belle Harbor, New York, and Air Midwest flight 5481 in Charlotte, North Carolina.

On November 12, 2001, American Airlines flight 587, an Airbus A300–605R (N14053) crashed in Belle Harbor, New York shortly after taking off from John F. Kennedy International Airport on a flight to Santo Domingo. All 260 people aboard the plane died, as did five persons on the ground. It was the second deadliest aviation accident in American history. On October 26, 2004, the Safety Board determined that flight 587 crashed because the plane's vertical stabilizer separated in flight as a result of aerodynamic loads that were created by the first officer's unnecessary and excessive rudder pedal inputs after the aircraft encountered wake turbulence. The Board said that contributing to the crash were characteristics of the airplane's rudder system design and elements of the airline's pilot training program. As a result of the investigation, the Safety Board issued 13 safety recommendations.

On January 3, 2003, an Air Midwest (U.S. Airways Express) flight 5481, a Raytheon (Beechcraft) 1900D (N233YV) crashed on takeoff at Charlotte-Douglas International Airport. Two crewmembers and 19 passengers aboard the airplane were killed and one person on the ground received minor injuries. Impact forces and a post-crash fire destroyed the airplane. On February 26, 2004, the Safety Board determined that the probable cause of the accident was the airplane's loss of pitch control during takeoff. The loss of pitch control was the result of incorrect rigging of the elevator control system compounded by the airplane's center of gravity, which was substantially aft of the certified aft limit. As a result of the investigation, the Safety Board issued 21 safety recommendations.

Currently, the Safety Board has 8 ongoing major investigations including a Canadair crash near Montrose, Colorado, a Gulfstream jet crash at Houston, Texas, and the Platinum Airlines Challenger jet crash at Teterboro Airport, New Jersey.

The NTSB also assisted in several foreign investigations in the past year. These include the China Northern CRJ, which crashed on takeoff from Baotou, China; the Flash Airlines B737–300, which crashed on take-off near Sharm-el-Sheikh, Egypt; and the Air Transat charter flight 961, an Airbus A–310–308, en route from Varadero, Cuba to Quebec City, Canada, which lost a rudder and returned to Cuba.

Office of Highway Safety (OHS)

OHS investigates highway accidents involving issues with wide-ranging safety significance, such as bridge collapses, multiple fatalities on public transportation vehicles, heavy trucks and at grade crossings. The office also examines the safety programs of the Federal Highway Administration, Federal Motor Carrier Safety Administration and the National Highway Traffic Safety Administration.

Highway fatalities account for about 95 percent of all transportation deaths in the United States per year, causing about 120 fatalities a day. As I mentioned earlier, OHS completed six major accident investigations in 2004, including a school bus run-off-bridge accident in Omaha, Nebraska which resulted in four fatalities; a daycare van run-off-road accident near Memphis, Tennessee with five fatalities; a fatigued driver in a motorcoach near Victor, New York resulting in five fatalities; an elderly driver who crashed into a farmer's market near Santa Monica, California, which resulted in 10 fatalities and 63 injuries; a barge/bridge collapse with 14 fatalities near Webbers Falls, Oklahoma; and six accidents involving drivers' seizures and medical issues that resulted in 8 fatalities, and 27 injuries.

Each of these accident investigations yielded significant safety improvements as a result of our recommendations. The accident near Memphis, Tennessee involved a 15-passenger van, operated by a childcare center, which ran off the road, killing the driver and 4 children. The Board's report made recommendations for improved oversight of child care transportation, improved vehicle crashworthiness standards, improved vehicle inspections, better driver qualifications and medical exams, the use of age-appropriate child restraints, and improved guard rail anchorages.

Two similar accidents near North Hudson, New York occurring 7 months apart, involved a motorcoach and a tractor semi-trailer that collided with stopped traffic on a congested interstate. The congestion was created by a U.S. Border Patrol checkpoint. Four persons were killed and 56 people were injured in these two accidents. The Board made urgent recommendations to immediately develop comprehensive traffic control guidelines specifically tailored to U.S. Border Patrol checkpoints located on highways. These urgent recommendations were issued approximately 1 month after the second accident.

The Office of Highway Safety has 17 on-going investigations, including a motorcoach collision with an SUV near Hewitt, Texas, a truck that rear-ended a bus near Hampshire, Illinois and two school bus accidents, one in Arlington, Virginia and another in Liberty, Missouri.

Office of Railroad, Pipeline and Hazardous Materials Investigations (ORPH)

Since January 2004, ORPH completed 18 accident investigations, including 12 railroad, 3 pipeline and 3 hazardous materials reports.

By law, the Safety Board determines the probable cause of railroad accidents involving passenger trains or any train accident that results in at least one fatality or major property damage.

I'd like to discuss two railroad accident investigations by the Safety Board: the derailment of a Canadian Pacific Railway freight train near Minot, North Dakota and the derailment of a Norfolk Southern Railway freight train in Graniteville, South Carolina.

On January 18, 2002, an eastbound Canadian Pacific Railway freight train traveling about 41 miles an hour derailed 31 cars about ½ mile west of the city limits of Minot, North Dakota. Five tank cars carrying anhydrous ammonia catastrophically ruptured and a vapor plume covered the derailment site and surrounding area. The plume affected about 11,600 people who occupied the area. One resident was fatally injured and 60–65 residents of the neighborhood nearest the derailment site were rescued. As a result of the accident, 11 people sustained serious injuries and 322 people sustained minor injuries. The probable cause of the derailment was an ineffective inspection and maintenance program that did not identify and replace cracked joint bars before they completely fractured and led to the breaking of the rail at the joint. Contributing to the severity of the accident was the catastrophic failure of five tank cars and the instantaneous release of about 146,700 gallons of anhydrous ammonia. The Safety Board made 8 safety recommendations to improve track inspections and tank car performance.

On January 6, 2005, a northbound Norfolk Southern Railway freight train collided with a locomotive that was parked on an industrial siding in Graniteville, South Carolina. Hours before the accident, another Norfolk Southern Railway train had used the same main track to enter the industrial siding. The local train crew secured their train and departed the area. About 8 hours later, the accident train proceeded toward Graniteville with authority to use the main track without restrictions. The engineer of the accident train initiated an emergency application of the brakes as the train neared the switch. The train was diverted onto the sidetrack and struck the lead locomotive of the parked local train. The two locomotives and 16 head cars derailed. Included in the derailment were three pressure tank cars filled with chlorine. One chlorine tank car was breached, which prompted an evacuation of about 5,400 people for an extended period. The engineer and eight other people died from inhalation injuries due to the chlorine gas release. The conductor and 72 other people were hospitalized. The investigation is on-going.

In addition to launching on 17 investigations and completing 18 major reports, ORPH held a symposium in March 2005 on Positive Train Control at the NTSB Academy and held a public hearing on April 26–27, 2005 regarding a Union Pacific train derailment near Macdona, Texas.

Currently, the Office of Railroad, Pipeline and Hazardous Materials Investigations has 18 railroad, 2 pipeline and 3 hazardous materials accident investigations ongoing.

Office of Marine Safety (OMS)

OMS investigates marine accidents on navigable waters and territorial seas of the United States and accidents involving U.S. merchant vessels worldwide. Recently, the NTSB and the USCG reached an agreement making the Board responsible for the investigation of accidents that risked high loss of life to innocent third parties such as passenger vessel accidents and accidents that involve significant safety issues related to USCG safety functions.

Passenger vessel accidents have constituted 80 percent of the 21 marine accidents investigated by the Board in the past 4 years. Since March 2003, four of the Board's major accident investigation launches have been marine accidents, all of which were of major consequence: the boiler explosion aboard the Bahamian Flag cruise ship, Norway, in Miami, Florida, the allision of the Staten Island Ferry near St. George, Staten Island, New York and the Taki-Tooo which capsized while transiting Tillamook Bar near Garibaldi, Oregon.

At approximately 6:48 A.M. on May 25, 2003, a boiler room explosion aboard the S/S Norway, docked in the port of Miami-Dade, killed 4 and injured at least 20 crewmembers. Nearly 50 fire-rescue units from Miami-Dade County, the City of Miami, and Miami Beach responded to the explosion in the boiler room. An additional 4 crewmembers died of injuries over the next 3 weeks after the accident. The investigation is on going.

On October 15, 2003, the Staten Island Ferry Andrew J. Barberi was at the end of its regularly scheduled trip from Manhattan to Staten Island when it allided with a maintenance pier at the Staten Island Ferry terminal. Fifteen crewmembers and an estimated 1,500 passengers were on board. Ten passengers died and 70 were injured in the accident. An eleventh passenger died 2 months later as a result of injuries sustained in the accident. Damages totaled over $8 million, with repair costs of $7 million for the Barberi and $1.4 million for the pier. The probable cause of this accident was the assistant captain's unexplained incapacitation and failure of the New York City Department of Transportation to implement and oversee safe, effective operating procedures for its ferries. As a result of its investigation, the Safety Board made eight safety recommendations.

On June 14, 2003, at about 7:15 A.M., the small passenger vessel Taki-Tooo capsized while transiting Tillamook Bar near Garibaldi, Oregon. The Taki-Tooo was one of four U.S. Coast Guard-inspected small passenger vessels leaving the bay at the same time for charter fishing excursions. Rough bar warnings were posted and had prohibited recreational and uninspected commercial vessels from transiting the bar that morning. One of the rescue units could not launch because conditions were too rough. The Taki-Tooo's course took her close to the North Jetty as the vessel turned to the north. The Taki-Tooo capsized after being struck on its port side by a large wave. Of the 19 persons aboard, 9 died and 2 are missing and presumed drowned. The Board will be considering this report in June.

In addition to investigating 21 accidents and completing 5 marine reports, OMS completed a major reconsideration of the collision between the U.S. Coast Guard

Cutter, Cowslip, and the foreign flag vessel, EverGrade, and issued two early recommendations related to the availability of children's lifejackets aboard small passenger vessels and small passenger vessel stability.

The OMS currently has 10 on-going accident investigations.

CRITICAL NEEDS

The increasing demands of a growing transportation environment and advancements in transportation technologies, coupled with our needs to adjust mission resources to accommodate inflation, salary increases, and the strain of a static budget, create significant challenges for the NTSB to investigate the accidents that Congress requires us to investigate under our mandate.

For example, there is a 24 percent staffing shortage in the Office of Aviation Safety (OAS) alone. With a forecasted activity growth of between 4 and 5 percent in world aircraft by the year 2015, OAS will be overloaded and it will be increasingly difficult to keep on schedule with current investigations and reports. Additionally, without additional resources, the Safety Board will struggle to maintain its currency with emerging technologies, and the Board's focus on incidents that, if investigated, may prevent major accidents.

Similarly, our Office of Highway Safety (OHS), due to shrinking resources, is unable to fully staff all three major highway investigation teams. Without sufficient personnel in key technical areas, our highway office can only select a limited number of accidents and incidents to investigate. These investigations can yield significant life-saving lessons learned; consequently, fewer investigations will reduce our prospects for identifying these life-saving lessons. The opportunities to improve highway safety in our Nation with over 42,000 deaths per year are significant. However, resources are necessary to ensure that the NTSB can continue to focus on those highway issues that will make meaningful improvements for our citizens. Likewise, resource limitations impact our Office of Railroad, Pipeline and Hazardous Materials Investigations and our Office of Marine Safety. In both of these modal offices, managers have had to either curtail some investigations or repeatedly launch the same investigators to multiple accidents. In the end, the timeliness of our recommendations may suffer.

The Board appreciated the support of the committee in providing approximately $3.7 million above the fiscal year 2004 appropriation level. However, the Board had to absorb $3.9 million, which included a government-wide pay increase, an inflationary increase and a fiscal year 2005 across-the-board rescission. Consequently, the increase only allowed us to maintain our fiscal year 2003 staffing level.

TRAINING ACADEMY

The NTSB Academy is in its second year of operation in Ashburn, Virginia, with a record number of individuals (over 1,500) attending classes, training sessions, symposiums, forums and other programs. This number far exceeded all expectations. During the year, 15 courses were taught on topics such as the sciences involved in accident investigations and techniques used to assist survivors and victims' families following a transportation disaster. Sixty-five students, from 35 foreign countries, attended Academy courses in 2004, more than doubling the 16 countries represented in 2003. Additionally, 9 new courses and partnership programs are currently scheduled for the 2005 calendar year; more will be added as they are identified. Yet, the Academy has only 6 staff to develop and deliver these programs.

In addition, the Academy has formed alliances and partnerships with other Federal agencies and private organizations to meet the training needs of other government agencies and the transportation and emergency response communities including Airports Council International of North America, the Air Transport Association, the Aviation Safety Alliance, the Civil Aviation Administration of China, the Federal Bureau of Investigation, the National Association of State Boating Laws Administrators, the National Aeronautics and Space Administration, Transportation Safety Institute and the Society of Automotive Engineers.

As a developing center of excellence for accident and transportation safety training, the Academy has been sought out as a venue for other organizations' training and outreach use. Recently, the Society of Automotive Engineers conducted its forum on developing transportation-related technologies and the Armed Forces Institute of Pathology taught its annual course for medical examiners at the Academy. NTSB, as the chair of the International Transportation Safety Alliance, hosted the Chairman's meeting with 10 countries that have independent safety boards at the Academy in March of this year.

TRANSPORTATION DISASTER ASSISTANCE (TDA)

In 1996, Congress passed the Aviation Disaster Family Assistance Act that gave the NTSB the responsibility of assisting the victims of aviation disasters and their families. The Board's primary responsibility involves coordination between Federal agencies, commercial airlines, State and local authorities and the families of victims. Additionally, in 1997, Congress enacted the Foreign Air Carrier Support Act to ensure foreign air carriers operating to the United States meet the same standards for victim assistance as their domestic U.S. counterparts. The TDA team's mandatory responsibilities include assistance at all major aviation accidents as well as accidents in other modes of transportation. TDA staff launched on 16 major accidents providing support to all modes and responded to approximately 1,500 inquiries from family members. In one instance, a TDA staff member launched to three major investigations within a 10-day period.

In addition, the TDA provides comprehensive courses at the NTSB Academy for professionals who support families of major transportation accident victims following a tragedy. These courses bring together leading experts in the field and cover a wide range of topics including initial accident notification, grief and trauma, forensic procedures, multi-cultural memorial services and effective family briefings.

APPROPRIATION REQUEST

The President's budget for fiscal year 2006 requests $76.7 million for the National Transportation Safety Board. This level is the same as the amount appropriated for the Board's Salaries and Expenses account for the current year. This level will fund 401 full-time equivalent (FTE) positions, requiring a reduction of 15 FTEs. As other expenses are relatively fixed, the Board must reduce staff to offset salary increases and inflation.

SURFACE TRANSPORTATION BOARD

PREPARED STATEMENT OF ROGER NOBER, CHAIRMAN

Mr. Chairman, members of the subcommittee, thank you for the opportunity to submit for the record this testimony on the Surface Transportation Board's (Board) fiscal year 2006 budget request.

BACKGROUND ON THE BOARD

As all of you know, the Surface Transportation Board was created 8 years ago by this committee in the ICC Termination Act of 1995. It has three members and is bipartisan. Structurally, the Congress determined that the Board should be decisionally independent but administratively affiliated with DOT.

The Board provides an efficient and effective forum for the resolution of disputes arising from surface transportation regulation. It serves as both an adjudicatory and a regulatory body. The Board has jurisdiction over railroad rate and service issues and rail restructuring transactions (mergers, line sales, line construction, and line abandonments); certain trucking company, moving van, and non-contiguous ocean shipping company rate matters; certain intercity passenger bus company structure, financial, and operational matters; and certain pipeline matters not regulated by the Federal Energy Regulatory Commission.

The Board's Section of Environmental Analysis performs environmental reviews on the Board's construction, abandonment, and merger matters as required by the National Environmental Protection Act. These reviews have become more complex and require significant resources.

THE BOARD'S FISCAL YEAR 2006 BUDGET REQUEST

The Board requests budget resources of $26,622,000 and authority to continue to operate at 150 full time equivalents (FTEs). The Board's budget request for fiscal year 2006 reflects its fiscal year 2005 budget, adjusted for the fiscal year 2006 pay raise and increased to the extent necessary for the Board to physical relocate due to the expiration of its current building space lease. The 150 FTEs is the level approved by Congress for fiscal year 2005. Unlike many agencies, there is little room at the Board's current budget level to absorb a pay increase without the additional resources, because fixed costs, including salary and rent, comprise about 95 percent of the agency's expenses. Absorbing even a small amount of the pay increase impairs the Board's ability to perform its statutory mission.

Of the requested $26,622,000, 81 percent of the increase in budget resources requested would be used to cover the Board's relocation expenses. The Board is requesting $4,500,000 for services related to the agency's relocation by the General Services Administration (GSA) from its current physical site. The Board has been at its current site for the duration of its 10-year lease, which expires early in 2007. The Board cannot remain in its current building and will be forced to find new space because the building owners intend to vacate the building to provide for extensive renovation and modernization. GSA had the replacement lease prospectus approved by Congress during 2004. GSA expects to advertise the lease solicitation during the summer of 2005 and award the lease by the fall of 2005. GSA will then begin the design and interior construction beginning in 2006 with an anticipated move-in date of January 2007. The requested funds will provide GSA with the resources to schedule the network and telecommunication connections and interfaces and perform needed structural changes to the leased space to support the Board's mission. The Board will request funds in fiscal year 2007 for the physical relocation of its furniture, equipment, and files to the new space, as well as an amount to pay for the new level of rent.

The requested authorization for 150 FTEs also will provide the Board with the discretion to hire staff to replace tenured, retirement-eligible staff prior to their anticipated retirement date. Currently, 75 employees, or 57 percent, of the Board staff are retirement eligible. Several retirements can be expected in the near future, and having the flexibility to hire qualified people when they are available is particularly important for a high-rated agency that must hire economic and technical expertise when they are available in the labor market. Consistent with appropriation acts for past fiscal years, the Board requests a provision allowing user fee collections to be credited to the appropriation as offsetting collections and used for necessary and authorized expenses, to the extent that they are collected.

The overall budget request reflects the workload that is expected and the statutory and regulatory deadlines associated with the resolution of the cases filed.

OVERALL GOALS OF THE BOARD

In the performance of its functions, the objective of the Board is to ensure that, where regulatory oversight is necessary, it is exercised efficiently and effectively. In doing so, the Board strives to integrate market forces into the overall regulatory model, where possible.

In particular, the Board seeks to resolve matters brought before it fairly and expeditiously. The Board seeks to facilitate commerce by providing an effective forum for efficient dispute resolution and facilitation of appropriate business transactions. It does so by using of its regulatory exemption authority, streamlining of its decisional process and the regulations applicable thereto, and consistently applying legal and equitable principles. Through rulemakings and case disposition, the Board continues to work to develop new and better ways to analyze unique and complex problems, to reach fully justified decisions more quickly, and to reduce the costs associated with regulatory oversight.

To be more responsive to the surface transportation community by fostering governmental efficiency, innovation in dispute resolution, private-sector solutions to problems, and competition in the provision of transportation services, the Board will:

—Continue to strive for a more streamlined process for the expeditious handling of rail rate reasonableness and other complaint cases, in an effort to provide additional regulatory predictability to shippers and carriers;

—Continue to process diligently cases before the Board and to ensure that appropriate market-based transactions in the public interest are facilitated;

—Continue to develop new opportunities for the various sectors of the transportation community to work cooperatively with the Board and with one another to find creative solutions to persistent industry and/or regulatory problems involving carriers, shippers, employees, and local communities; and

—Continue to work to ensure the provision of rail service that is responsive to the needs of customers.

SIGNIFICANT WORKLOAD THAT IMPACTS THE BOARD'S BUDGET REQUEST

Under the Interstate Commerce Act, the Board must authorize the construction of new rail lines that are part of the national rail system. The Board has been named a cooperating agency in the environmental review associated with building a rail line to the repository at Yucca Mountain, in Nye County, Nevada. The Department of Energy (DOE) has been working for years on a program to use Yucca Mountain as a repository for spent nuclear fuel and high-level radioactive waste that would be transported there from throughout the United States.

In April 2004, DOE announced that its preferred mode to transport the radioactive materials from throughout the United States to Yucca Mountain was "mostly rail," and it selected as its preferred corridor for a new rail line to Yucca Mountain one beginning near Caliente, Nevada. DOE announced its intent to prepare an Environmental Impact Statement (EIS), as required by the National Environmental Policy Act, for construction and operation of this rail line.

In May 2004, DOE formally requested that the Board, along with two other agencies, become a cooperating agency on the environmental review of the Caliente Corridor leading to the Yucca Mountain facility. DOE made this request due to the Board's statutory authority to review certain rail construction projects and its expertise in doing so. Our responsibilities as a cooperating agency have been ongoing since 2004. The Board's Section of Environmental Analysis has had numerous meetings this year and throughout the EIS process, which the DOE expects to last at least 2 years.

DOE has not yet determined whether it will structure the line in a way that would trigger Board review. While the Board receives many applications to build new rail lines that are subject to the Board's jurisdiction, not every rail line construction project requires Board approval. The Board has jurisdiction over and must approve the construction of any common carrier rail line—a rail line on which the railroad must provide service to any shipper who requests it. However, the Board does not license the construction of a private rail line—a line over service is not available to the general public.

When the Board receives an application to build and operate a new rail line, it conducts the required environmental review of these projects and, unless the project is not in the public convenience and necessity, licenses the project. In the typical case, the Board is the lead agency for any necessary environmental review, but an environmental review that meets the Board's standards could be used if the Board were a cooperating agency.

In conducting the environmental review, the Board is usually able to accept certain services that are paid for by the project proponent. For example, to complete the environmental review of a rail construction project, the applicant selects a third-party contractor from the Board's list of pre-approved contractors and retains it. Although the contractor works at the direction of the Board's Section of Environmental Analysis, the project proponent pays the contractor. The Board is not reimbursed for its staff time or travel.

In discharging our duties as a cooperating agency, the Board will require a third party contractor who will assist the Board by attending meetings regarding the EIS, evaluating the environmental concerns, and providing the specialized, technical expertise concerning issues affecting the rail line construction that would supplement the work of the Board's Section of Environmental Analysis. The Board has received funding from DOE to reimburse the Board for the costs associated with this contractor. The Board's review of such a proposal must be independent. Otherwise, if the Board issued a license, that issuance could be subject to challenge in court on grounds that the agency's independence was jeopardized by its acceptance of reimbursements beyond those reimbursements that are ordinarily permissible in any rail construction case. A successful challenge could be costly to the taxpayers and delay the project.

The Board's participation in the Yucca Mountain EIS will require 25 percent of the Board's current environmental staff, which could adversely affect the Board's ability to conduct the environmental reviews required for abandonment and rail line construction cases currently pending before the Board and those that may be in the pipeline awaiting formal filing.

Another significant construction case is The Alaska Railroad Corporation's proceeding. In that case, The Alaska Railroad Corporation seeks authority from the Board to construct and operate approximately 80 miles of new rail line that would connect Eielson Air Force Base near North Pole, Alaska, to a point at, or near, Fort Greely and the Donnelly Training Area near Delta Junction, Alaska. The proposed project would include a 15-mile spur from Flag Hill to the Blair Lakes Military Training Area. The project area is located in a sub-arctic region with diverse environmental, geological and geotechnical conditions. The proposed rail line would cross several rivers and numerous streams and wetland areas. The project area also provides habitat to moose, caribou, black and brown bears, raptors and numerous other wildlife. The Board's Section of Environmental Analysis is in the early stages of the environmental review process for the project.

AMTRAK DIRECTED SERVICE PROVISION

The fiscal year 2005 Transportation Appropriations Act directed the Secretary of Transportation to reserve $60 million of Amtrak's fiscal year 2005 appropriation to fund directed service of commuter and freight operations in the event of a cessation of service by Amtrak. The fiscal year 2006 President's budget request proposes to provide the Board with $360 million to support commuter rail service along the northeast corridor should Amtrak cease commuter rail operations. These funds would allow the Board to direct service of commuter and freight rail operations that fail as a result of a cessation of service by Amtrak.

The Board has taken a number of steps since Congress' action last year. Among other things, the Board set up a joint working group with the FRA to coordinate issues. That group has met with all major stakeholders—including Amtrak, the affected commuter and freight railroads, and representatives of labor—to identify issues. We have compiled all of the services Amtrak provides to commuter and freight railroads, and we have examined legal issues that might arise. However, these planning efforts would need to be significantly supplemented were the need to implement directed service imminent.

While matters brought before the Board are often lengthy, in directed service proceedings the law does alter some administrative procedures to allow the Board to act cooperatively and quickly. Of course, because the Board may be called on to consider these issues, I cannot say how the Board would resolve them. I can only identify those issues which we currently know would have to be resolved. Nevertheless, the Board and its staff would work to the best of our abilities to carry out these responsibilities in a fair and impartial manner.

FISCAL YEAR 2005 AND 2006 ACTIVITIES OF THE BOARD

Building upon the Board's success in fiscal year 2004—including issuing 1,108 decisions in fiscal year 2004, developing regulations to expedite processing for small rate cases[1] and informally resolving disputes between railroads and between railroads and their customers—the Board will continue to look for ways to streamline and to improve applicable regulations and the regulatory process and to promote private-sector resolution of problems. In this regard, the Board is open to proposals filed by parties and independently will look for ways to shorten and streamline its procedures and processes.

The workload involving rail rates and services is expected to remain stable through fiscal year 2006, particularly given the likely continuing expiration of long-term coal transportation contracts. Currently, the Board's rail rate docket is as follows:

—4 coal rate complaint cases that are at various stages of adjudication under the stand-alone cost constraint of the Board's Coal Rate Guidelines;

—3 complaint cases that have already been decided under the stand-alone cost constraint and are now being tested at the request of the complaining shippers under the alternative "phasing" constraint; and

—4 additional coal rate complaints that are currently being contested by the parties and defended by the Board in court.

These proceedings will require significant staff attention, given the complex nature of the cases, the numerous steps such as motions and discovery resolution, and the tight 9-month statutory timeframes for completion once the record is closed. Indeed, the bulge in rate cases is already producing a strain on our resources, which have historically been geared to handle two rate cases at a time.

Additionally, the Board will continue to handle rail cases involving questions of whether certain rail activity cannot be regulated at the State or local level because such regulation is preempted by Federal law.

The Board continues to have success in resolving scheduling and operational issues between freight railroads and between those railroads and their customers. The Board's Rail Consumer Assistance Program is an informal mechanism for resolving disputes that has proven very effective, by having a special toll-free telephone number and a specific website connection, to assist rail customers and others with concerns involving railroads and has resolved 123 rail consumer issues during 2004. Board staff expeditiously handles and brings to a successful conclusion on an informal basis rail consumer inquiries and complaints concerning matters related to rates and other charges, car supply and other service issues, claims for damages, and service-related problems, employee concerns, and community issues.

[1] Ex Parte No. 646, Rail Rate Challenges in Small Cases.

The Board has also worked to facilitate better communications between railroads and shippers regarding service issues and plans to resolve them. The Board participated in forums between railroads and their customers in Kansas City, San Francisco, and Atlanta. And the Board continues to assist parties in devising private-sector solutions to their disputes outside of the Board's formal processes.

With respect to rail carrier consolidations, we are not aware of any major rail mergers in the immediate future. Therefore, the workload in this category is expected to remain somewhat stable through fiscal year 2006 because this category includes a broad array of control transactions among larger railroads and smaller railroads. Of course, it is impossible to know whether a major merger may be proposed during fiscal year 2006. As noted, the Board continues to resolve issues related to past Class I rail mergers. Also, the Board will continue to handle other rail consolidations involving smaller railroads that are filed with it.

With the notable exception of the Yucca Mountain rail line construction project, the Board projects that its line construction docket will remain constant through fiscal year 2006. The Board has an unprecedented number of railroad line construction proposals, along with the associated environmental review work currently under review. These 12 proposals currently under review varied in size and scope, ranging from less than a mile to 260 miles of new rail line. The Board has been working on environmental issues raised by the U.S. Court of Appeals for the 8th Circuit in STB Docket No. 33407, Dakota, Minnesota & Eastern Railroad Corporation Construction Into The Powder River Basin. The Board has issued a draft supplemental addressing the issues remanded by the Court and is awaiting public comments on the Board's analysis. We emphasize that demands on the Board to conduct environmental reviews for such transactions continue to grow, and that such activities require a significant number of resources to complete.

Other line transaction activity is expected to increase slightly through fiscal year 2006 as more carriers continue to sell unprofitable or marginally profitable lines as an alternative to service abandonment. In the past few years, the Board has seen a number of line acquisitions by both small carriers and noncarriers as rail carriers restructure their rail systems.

SUMMARY

The Board's budget request would ensure the resources needed for the Board to continue to implement its responsibilities expeditiously and effectively as Congress intends. I appreciate the opportunity to submit this statement about the Board's fiscal year 2006 budget request and would be happy to answer any other questions that the committee may have.

MORRIS K. UDALL FOUNDATION

PREPARED STATEMENT OF TERRENCE L. BRACY, CHAIR

Mr. Chairman, members of the subcommittee, thank you for the opportunity to present testimony regarding the fiscal year 2006 budget of the Morris K. Udall Foundation. We have previously submitted our Congressional Justification and met with the subcommittee's staff to answer their questions regarding our programs and budget.

I am enormously proud of the accomplishments of the Foundation, produced by a small, dedicated staff working with a budget based on a combination of appropriations, fees and interest.

There are two major program areas, supported by two distinct appropriations funds: the U.S. Institute for Environmental Conflict Resolution (the Institute), supported by a combination of annual appropriations and fees charged for services, and the Education Programs, supported by the annual interest from a Trust Fund (invested solely in Treasury obligations). In fiscal year 2006, the Institute will generate an estimated $3.6 million in gross revenues, of which an estimated $2.7 million will fund extramural mediation services and $900,000 will be applied to intramural costs. The Trust Fund will earn an estimated $1.5 million in interest. In consideration of these projections the President's Budget requests no new appropriation for the Trust Fund and $700,000 for the Institute. This funding is expected to allow the Foundation to maintain current programs in fiscal year 2006. In this testimony, I would like to address some of the new developments at the Udall Foundation over the last year.

The U.S. Institute for Environmental Conflict Resolution has become established as a national resource for assistance in resolving and preventing environmental conflicts involving Federal agencies. For example, the U.S. Institute has assisted the

Federal Highway Administration's Environmental Streamlining and Stewardship Program by conducting 11 regionally customized workshops to strengthen Federal and State agencies' efforts to successfully meet agency coordination and cooperation mandates of the Transportation Equity Act for the 21st Century (TEA–21), Section 1309: Environmental Streamlining and Executive Order 13274: Environmental Stewardship and Transportation Infrastructure Project Reviews. Similar workshops featuring State-specific topics, co-funded by FHWA and a local sponsor, are continuing through fiscal year 2005. The Institute also has provided conflict resolution services on 2 of the 13 high priority transportation cases identified by the interagency task force on Environmental Stewardship and Transportation Infrastructure Project Reviews (St. Croix River Crossing and the Community Environmental Transportation Acceptability Project).

The U.S. Institute has recently been retained to provide conflict resolution services in two projects in the Missouri River Basin (affecting Kansas, Missouri, Montana, Nebraska, North Dakota, South Dakota and Wyoming)—the first is facilitating an intergovernmental process to develop agreement on a "spring rise" proposal, and the second is an assessment for development of a Missouri River Recovery Implementation Committee. Other major projects under way in fiscal year 2004–2005 included the Grand Canyon overflight noise controversy, the impact of endangered species issues on flight training at the Barry M. Goldwater Range, Everglades collaborative water use planning, and the Upper Klamath Basin Watershed recovery planning effort.

Also in fiscal year 2004, President Bush signed into law the Environmental Policy and Conflict Resolution Advancement Act of 2003 (Public Law 108–160), authorizing $3 million a year in operating appropriations for the U.S. Institute and $1 million a year for grants to assist non-Federal stakeholders to participate in Federal conflict resolution processes.

Because of the increase in the number and size of its cases, the U.S. Institute's gross revenues from services tripled in fiscal year 2004 over fiscal year 2003. About 25 percent of gross revenue is used by the U.S. Institute to fund intramural costs, and the rest is paid out to contracted private sector mediators with whom the Institute partners on projects. (The U.S. Institute's enabling legislation directs that it use mediators located in geographic proximity to the dispute whenever practicable.) Ultimately, the net revenues from services are equal to about one-third of the Institute's basic operating budget.

The Education Programs of the Udall Foundation are also thriving. The Foundation continues to draw the highest quality applicants for its scholarships, fellowships, and internships. A total of 756 college scholarships have been awarded through fiscal year 2005 to students from all 50 States and 255 colleges. The Native American Congressional Internship Program has placed 114 interns from 30 States and 73 tribes in Congressional offices, the Executive Office of the President, and high-placed offices at the Departments of Interior, Education and Defense.

Native Nations Institute, a joint project of the Udall Foundation and the University of Arizona, has conducted executive education sessions for more than 1,000 councilors, presidents and senior managers from more than 100 Indian nations over the last 4 years and has reached many more through conference presentations. In partnership with the Harvard Project on American Indian Economic Development, NNI has developed the leading research on tribal economic development, leadership and self-determination. NNI will have sufficient carryover funds in fiscal year 2006 to maintain current program levels; the President's Budget has not requested an fiscal year 2006 appropriation.

I am pleased to report to the subcommittee that, in its first full audit, as required by the Accountability of Tax Dollars Act of 2002, the Foundation received an unqualified "clean" opinion for fiscal year 2004, and no material inadequacies were identified by the independent auditor, Clifton, Gunderson, LLP. In addition, the Foundation met all programmatic goals and nearly all management goals for fiscal year 2004, as reported in its Performance and Accountability Report to Congress.

I want to assure the Chairman and members of the subcommittee that the Foundation has taken extraordinary steps to keep down administrative expenses and get the best value out of its limited funds. We will continue to operate in that spirit, recognizing that we have a responsibility to Congress to make the best use of each dollar.

Thank you again for the opportunity to submit testimony. I look forward to working closely with you and your staff as you consider fiscal year 2006 appropriations.

NATIONAL CREDIT UNION ADMINISTRATION

PREPARED STATEMENT OF HONORABLE JOANN JOHNSON, CHAIRMAN

Chairman Bond, Ranking Member Murray, members of the subcommittee, I am pleased to submit this testimony that presents NCUA's request for fiscal year 2006 funding of $950,000 for the Community Development Revolving Loan Fund (CDRLF) and to request $1.5 billion in fiscal year 2006 borrowing authority for the Central Liquidity Facility (CLF), and an administrative limitation of $323,000 in CLF operational expenses for the year.

NATIONAL CREDIT UNION ADMINISTRATION COMMUNITY DEVELOPMENT REVOLVING LOAN FUND

NCUA remains committed in our efforts to promote and facilitate the extension of affordable financial services to individuals and communities throughout America. "Low-income" designated credit unions use the loans to further community development by providing funding for member loan demand, additional member services, and increased credit union capacity to serve members and the community. The grants are used for verifiable and need-based technical assistance purposes by low-income designated credit unions.

Congress established the CDRLF in 1979 to provide low-interest loans to credit unions that have been designated low-income by NCUA. NCUA has administered the CDRLF for 15 years. By year-end 2004, the CDRLF had provided 244 loans totaling $35 million to low-income designated credit unions. In 1992, NCUA initiated a technical assistance grant (TAG) program in conjunction with the CDRLF which funded grants from the interest generated from outstanding CDRLF loans. To date, NCUA has disbursed 1,510 TAGs totaling $3.4 million.

NCUA views the CDRLF as a resource for incubation monies for low-income designated credit unions to initiate or develop services for members, thereby providing further opportunities to self-fund or obtain more substantial funding. Low-income designated credit unions use CDRLF loans to further community development efforts by funding member loan demand, provide additional member services, increase capacity to service members and improve the financial condition of low-income credit union members. TAGs support many of the services low-income designated credit unions provide to their members, including member financial literacy programs and electronic delivery systems.

Background

The CDRLF was established by Congress (Public Law 96–124, Nov. 20, 1979) through an initial $6 million appropriation to stimulate economic development in low-income communities. In 1990 the sole administration of the CDRLF was transferred to NCUA after having been administered by various Federal agencies.

Congress did not provide additional appropriations for the CDRLF from 1979 to 1996. For fiscal year 1997, Congress appropriated an additional $1 million for the loan program with subsequent appropriations as follows:

Fiscal Year 1997	$1,000,000	Loans
Fiscal Year 1998	1,000,000	Loans
Fiscal Year 1999	2,000,000	Loans
Fiscal Year 2000	1,000,000	Loans
Fiscal Year 2001	350,000	TAG
	650,000	Loans
Fiscal Year 2002	350,000	TAG
	650,000	Loans
Fiscal Year 2003	300,000	TAG
	700,000	Loans
Fiscal Year 2004	1,000,000	TAG
	200,000	Loans
Fiscal Year 2005	800,000	TAG
	200,000	Loans

Administrative expenses related to the CDRLF are fully absorbed by NCUA. All appropriations, as well as any earnings generated from the CDRLF's assets, are provided to the intended low-income designated credit unions after any necessary adjustments to recognize potential losses in the loan portfolio.

Qualifying Applicants

In order to qualify for participation in the CDRLF, credit union applicants must have a low-income designation and must serve predominantly low-income members. NCUA regulations define low-income members as those persons either earning less than 80 percent of the average for all wage earners as established by the Bureau of Labor Statistics or those whose annual income falls at or below 80 percent of the median household income for the Nation. The NCUA standard for 2004 income for a household was $35,080 and $21,389 for an individual.

Revolving Loan Component

The revolving loan component of the CDRLF is designed to assist as many qualifying credit unions as possible. Therefore, loans are limited to $300,000 and no credit union may have more than two separate loans at any one time. Loans must be repaid within 5 years, although a shorter repayment period may be considered.

Generally, loans are required to be paid in semiannual installments with no principal balance repayment due during the first year. To combat the potential misuse of funds, NCUA regulations require that recipient credit unions must match the loan with funding from member share deposits or non-member deposits within the first year.

Interest rates are set annually by the NCUA Board at a rate between 1 and 3 percent. Due to the current interest rate environment, the NCUA Board has set a 1 percent interest rate for 2005.

NCUA has authorized an open application period for participation in the loan program. This unrestricted application period enables low-income credit unions—most of which have very few employees and limited resources—to develop and present a viable plan for better serving their fields of membership. The open application period also allows credit unions to implement projects and services on a timelier basis.

During 2002, NCUA revised the loan program in an effort to achieve greater flexibility and mitigate risk. Although loan repayments accelerated during this period of time, the revised program offset the anticipated loss of loans with increased interest and applications for the loan program. During 2004, twenty-three credit union loan applications were received.

To help ensure equality in loan approvals, a scoring system judges the purpose of the proposed use of funds, the financial condition of the credit union and management's capability of achieving the stated objective and operating the credit union in a safe and sound manner. As a regulator, NCUA has the added advantage of using credit union examinations to ensure the financial stability of loan grantees.

Technical Assistance Grants (TAGs)

TAGs are generally awarded in amounts less than $5,000 and are made directly to low-income designated credit unions requiring assistance to further their outreach into the communities they serve. The grants assist these credit unions, generally less than $18 million in assets, in their efforts to improve service to their members by providing training opportunities to credit union staff; supplying funds for operational upgrades in recordkeeping; offering stipends to credit unions for summer student intern programs; promoting credit union services; developing training and consulting services for members and other worthwhile programs. With assistance provided through the TAG program, credit unions have also realized improved service in the delivery of financial products and services through enhanced technology. In 2004, 106 credit unions received more than $448,000 specifically designated for technology improvements which includes upgrades in hardware and software, debit card programs and automated response systems.

To ensure the funds are used solely for the purpose approved, grants are issued as reimbursements for goods or services previously approved by NCUA and much like the loan component of the CDRLF, various TAG initiatives are available to low-income designated credit unions throughout the year.

Beginning in 2001, Congress specifically designated a portion of its annual appropriations for TAGs. Prior to 2001, the grant program was funded solely through earnings from outstanding CDRLF loans and never exceeded $250,000.

Grant requests continue to exceed all available resources. In 2004, NCUA received requests for more than $3.4 million. Due to limited resources, NCUA was forced to decline requests for more than $2.2 million that could have been used to provide much needed services in low-income areas. Congress, recognizing the high demand for technical assistance, specifically designated $800,000 of the $1 million total appropriation for the grant component of the CDRLF for fiscal year 2005. From its inception in 1992, the CDRLF has disbursed 1,510 technical assistance grants totaling $3.4 million to low-income designated credit unions. In 2004, NCUA disbursed grants totaling over $600,000.

Student Intern Program

In 1996, NCUA established a student intern program funded entirely by the grant component of the CDRLF. The program is designed to provide low-income designated credit unions the opportunity for college students to contribute to the operations of the credit union while learning about the credit union community. In 2004, the program approved grants totaling $63,000, with 26 low-income designated credit unions and their 26 credit union partners participating. Student interns participating in the program work at both the low-income designated credit unions and their partnering credit unions, affording them with the opportunity to share best practices between the institutions. Response from student and credit union participants has been extremely positive. The program is reevaluated annually to assess its ongoing impact and feasibility.

VITA Program

In 2004, NCUA designated funds for low-income designated credit unions establishing VITA (Volunteer Income Tax Assistance) sites. The VITA program is administered by the Internal Revenue Service to assist low-income and elderly taxpayers with income tax preparation, and to encourage low-wage earners to file for the Earned Income Tax Credit (EITC). Last year, NCUA granted 12 credit unions a total of $56,322 dollars to offset some of the administrative burden associated with setting up these taxpayer clinics. Due to the success of last year's program, NCUA designated $60,000 for credit unions to set up VITA programs for 2005.

Financial Education Program

A new initiative offered last year was the Financial Education Program. Last year, NCUA granted 19 credit unions, a total of $80,683 to offset some of the costs associated with initiating and/or maintaining a financial education program. Grants provided under this initiative were granted to facilitate credit unions in providing members and potential members with practical money-management skills and an introduction to financial planning through course work that covers the fundamentals of money management.

Other TAG Programs

In addition to the above three programs and the Enhanced Technology Program, NCUA offered a Home Ownership Program, Individual Development Account Program, International Remittance Program, Officials and Staff Training Program, Mentoring Program, and Service to Underserved Areas Program in 2004.

2005 TAG Programs

In 2005, there will be five specific grant initiatives made available to low-income designated credit unions, entitled as follows: Urgent Needs Grant, Student Internship Initiative, Volunteer Income Tax Assistance (VITA) Initiative, Building Internal Capacity (Infrastructure) Initiative, and Enhancing Member Services (Outreach) Initiative.

NCUA plans to use both appropriated funds and funds derived from income from assets to cover the costs of these initiatives. These specialized TAG programs emphasize initiatives that help communities develop self-sufficiency.

Credit unions receiving funds through the Student Internship Initiative are provided an opportunity to introduce college students to credit unions and credit union operations. The purpose of the VITA Initiative is to provide financial assistance to credit unions wishing to help existing and potential members prepare their tax returns, especially those eligible for the Earned Income Tax Credit. The Building Internal Capacity Initiative grants will cover the costs of projects which improve the overall operations or financial condition of the credit union and ultimately enable the credit union to better deliver services to its members. Grant awarded under this initiative may include enhancing and improving technologies; preparing emergency and business resumption strategies or training and developing management. Credit unions receiving funds through the Enhancing Member Services Initiative are provided an opportunity to provide new or better services to existing members and those projects which will extend services to potential members and the community. Grant awarded under this initiative may include financial education, homeownership opportunities and developing marketing and outreach programs.

The CDRLF continues to provide low-income designated credit unions—particularly those of smaller asset size—the opportunity to obtain loans and technical assistance grants to improve and enhance services to their members. Though a small program, it provides valuable aid and assistance for those credit unions benefiting from this support while striving for self-sufficiency. Credit unions, through their cooperative structure, are funded through the share deposits of their members. The CDRLF provides needed assistance to further growth and viability of participating credit unions serving low-income fields of membership. Access to affordable financial services can provide underserved communities with a much needed alternative to high-cost lenders, allowing the residents to keep more of their money in their communities.

NATIONAL CREDIT UNION ADMINISTRATION CENTRAL LIQUIDITY FACILITY

The National Credit Union Administration Central Liquidity Facility (CLF) was created by the National Credit Union Administration Central Liquidity Facility Act (Public Law 95–630, Title XVIII, 12 U.S.C. 1795, et seq.). The CLF is a mixed ownership government corporation managed by the National Credit Union Administration Board. It is owned by its member credit unions who contribute all of the capital by the purchase of stock. The CLF became operational on October 1, 1979.

The purpose of the CLF is to improve general financial stability by meeting the liquidity needs of credit unions and thereby encourage savings, support consumer and mortgage lending and provide basic financial resources to all segments of the economy. To accomplish this purpose, member credit unions invest in CLF stock which is used for investment purposes and the funding of some lending activity. The proceeds of borrowed funds from the Federal Financing Bank are used to match fund significant loan requests from member credit unions.

In addition to serving its direct members, the CLF works through agents to serve substantially all natural person credit unions. CLF agents are a private financial network of 29 State and federally chartered corporate credit unions with approximately $69.6 billion in assets. The corporate credit union network provides operational and correspondent services, investment products and advice and short-term loans to its approximately 9,324 natural person credit unions. The CLF provides this network with funds to meet abnormal savings outflows if temporary liquidity shortages or public confidence issues arise. As a specialized lender housed within NCUA, the CLF has the ability to draw upon the supervisory and insurance resources of the agency. However, CLF assistance is generally a secondary source of funds after the corporate system or other sources of credit have been utilized.

The borrowings of the CLF have the "full faith and credit" of the United States government. The Federal Financing Bank of the U.S. Treasury is available as a source for the CLF to fund its lending programs. The CLF is financially self-supporting and does not use government funds to support any of its administrative and operational expenses.

Lending Activities

Loans are available to credit unions directly from the CLF or through its agent corporate credit union members. Credit unions rely on market sources to meet their demands for funds. The CLF normally is not an active participant in the on-going daily operations of this system. Rather, its role is to be available when unexpected, unusual or extreme events cause temporary shortages of funds. If not handled immediately, these shortages could lead to a larger crisis in individual credit unions or even the system as a whole. With its knowledge of credit unions and its immediate access to the supervisory information of NCUA, the CLF plays a vital role in maintaining member and public confidence in the health of the U.S. credit union financial system.

During 2004, the CLF did not receive any requests for loans. Credit union liquidity remained strong in 2004. Although credit union member loan demand moderately exceeded share growth in 2004, share growth exceeded loan growth in the 3 prior years. However, the CLF remains ready and able to meet the liquidity needs of the credit union system when unusual, unexpected or extreme events occur.

Factors Influencing Credit Union Borrowing Demand

Under the Federal Credit Union Act, the CLF is intended to address unusual or unpredictable events that may impact the liquidity needs of credit unions. Since these events are not generally foreseen, it is extremely difficult to forecast potential loan demand. Throughout the history of the CLF, loan demand has widely fluctuated in both volume and dollar amount.

The CLF is authorized by statute to borrow from any source up to 12 times its subscribed capital stock and surplus. Since fiscal year 2001, a borrowing limit of $1.5 billion has been approved by Congress. The continuation of the $1.5 billion cap for fiscal year 2006 will further assure that the CLF continues as a reliable, efficient backup liquidity source in times of need.

It is important to note that CLF loans are not used to increase loan or investment volumes because by statute the proceeds from CLF loans cannot be used to expand credit union portfolios. Rather, the funds are advanced strictly to support the purpose stated in the Federal Credit Union Act—credit union liquidity needs—and in response to circumstances dictated by market events.

Administrative Expenses

Total operating expenses for fiscal year 2004 were $214,000, below the budget limitation of $310,000. Expenses were under budget in 2004 due to a vacancy in the NCUA/CLF Board in the third and fourth quarters and travel expenses were not incurred as anticipated.

Total operating expenses for fiscal year 2005 are projected to be within our budget limitation of $309,000. In fiscal year 2005, pay and related benefits are higher than 2004 due to salary increases.

For fiscal year 2006, the CLF is requesting an administrative expense limitation of $323,000 and borrowing authority not to exceed $1,500,000,000.

Additional Background

Credit unions manage liquidity through a dynamic asset and liability management process. When on-hand liquidity is low, credit unions must increasingly utilize borrowed funds from third-party providers to maintain an appropriate balance between liquidity and sound asset/liability positions. The CLF provides a measure of stability in times of limited liquidity by ensuring a back-up source of funds for institutions that experience a sudden or unexpected shortage that cannot adequately be met by advances from primary funding sources. Two ratios that provide information about relative liquidity are the loan-to-share ratio and the liquid asset ratio. Liquid assets are defined as all investments less than 1 year plus all cash on hand. Managing liquidity risk is a major priority for credit unions and has become an increasingly important risk issue in the past decade as the charts below indicate.

Chart 1
Loans/Shares (%)

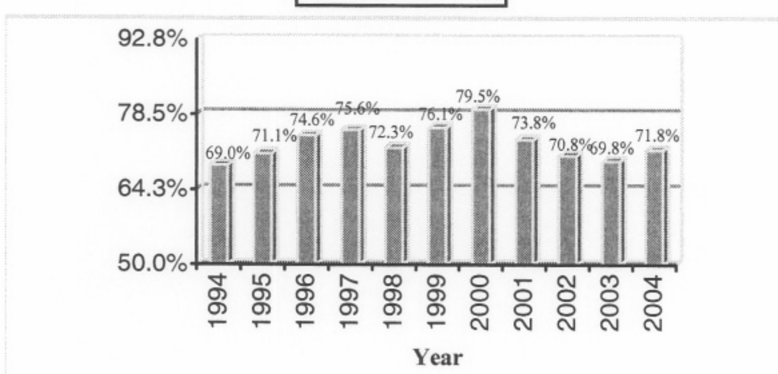


Chart 1 shows the ratio of loans to shares in all federally insured credit unions. As the ratio of loans to shares increases, the amount of funds maintained in short-term liquid investments declines. Liquidity risk has increased on average in the past decade as on-hand liquidity in federally insured credit unions gradually declined due to increased lending. Weak share growth during 2004 increased the ratio from the year-end 2003 low of 69.8 percent to a mid-year 2004 level of 71.8 percent. Liquidity risk management remains a significant obligation for credit unions.

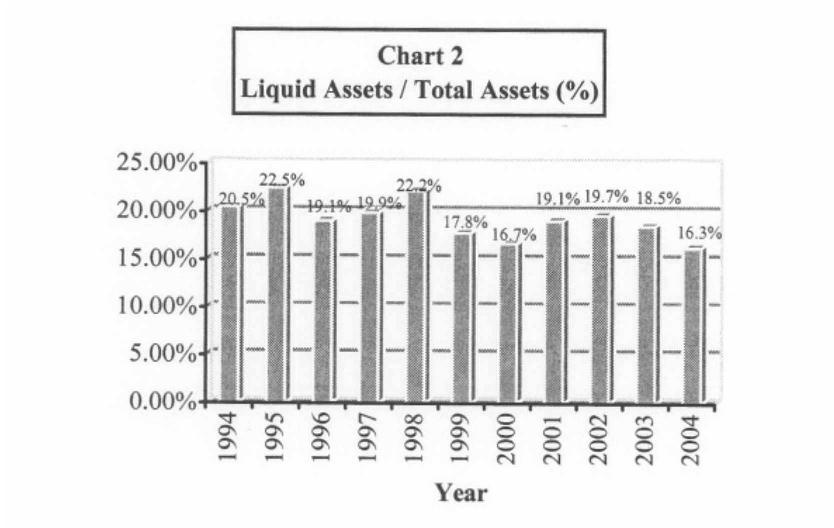


Chart 2 shows the ratio of liquid assets to total assets in all federally insured credit unions (using mid-year data for 2004). As this ratio decreases, liquidity risk and the potential need for borrowed funds conversely increases. Credit unions utilize various market sources for funding needs including the repurchase market, correspondent relationships with corporate credit unions and other financial institutions, and, to a growing extent, membership in the Federal Home Loan Bank system. CLF serves as a back-up source of liquidity when an unexpected need for funds arises and primary sources are not available.

SUMMARY

NCUA greatly appreciates the subcommittee's continued support of NCUA's efforts to keep credit unions safe and sound, enhance credit union liquidity and provide needed assistance through loans and grants to low-income credit unions.

NEIGHBORHOOD REINVESTMENT CORPORATION

PREPARED STATEMENT OF KENNETH D. WADE, CHIEF EXECUTIVE OFFICER

Neighborhood Reinvestment Corporation, now doing business as NeighborWorks® America, is pleased to submit this testimony for the record, on behalf of the NeighborWorks® system. This system includes NeighborWorks® America and 235 nonprofit, community-based organizations that comprise the NeighborWorks® network. In fiscal year 2004, we served over 2,700 communities and generated over $2 billion in direct investment.

OVERVIEW OF THE NEIGHBORWORKS® SYSTEM

To help more Americans seize opportunities to build wealth, strengthen their communities and realize the dream of homeownership, we work on three basic fronts:

—NeighborWorks® America headquarters and training agency;

—Our national NeighborWorks® network of nonprofit community development organizations; and

—Financial backing through Neighborhood Housing Services of America.

For nearly 30 years, the NeighborWorks® System has proven to be an increasingly effective and efficient vehicle for generating significant private-sector resources for community revitalization and affordable-housing. The NeighborWorks® System relies on public-private partnerships, the leveraging of Federal funding, and flexible revolving loan funds to achieve results. Innovations that are generated in response to community needs are a hallmark of the NeighborWorks® System. We were borne out of a real and present community need for more private sector investment in decaying urban areas in the 1970's and continue to nimbly address real and present community needs today.

NeighborWorks® America

NeighborWorks® America evolved from a 1972 effort by the Federal Home Loan Bank Board to increase thrift-industry lending in declining neighborhoods. Recognizing the model's effectiveness in community development and turning around urban blight, Congress chartered NeighborWorks® America as a public nonprofit organization in the Housing and Community Development Amendments of 1978 (Public Law 95–557).

Today NeighborWorks® America:

—As the Nation's largest certifier of high-quality homeownership education counselors, creates a national force of homeownership and financial literacy education counselors that have educated and empowered 500,000 Americans nationwide.

—Fuels local innovation with a powerful battery of community development training, research, managerial advice, turnaround specialists and an aggressive brokering of business and government partnerships.

—Maintains high performance standards for its NeighborWorks® member organizations through rigorous and thorough audits to ensure accountability and results.

—Empowers underserved populations and regions of the Nation. When comparing total lending activity, the NeighborWorks® network serves four times as many minorities as conventional lenders and twice as many as served by government agencies (as a percentage of the total clients served).

—Ensures continued responsiveness to local needs through sound dependable capital loan funds that have invested $2.5 billion in communities in the last 5 years alone.

—Challenges predatory lending with the twin tools of education and customized, responsible lending.

The NeighborWorks® Network

In the early 1970's, NeighborWorks® America founded the NeighborWorks® network, a group of community-based nonprofits that has evolved from a few organizations to more than 235 members active in more than 2,700 communities across the country. NeighborWorks® organizations operate in our Nation's largest cities, suburban neighborhoods and rural areas across 49 States as well as Puerto Rico and the District of Columbia. No matter what their location, NeighborWorks® organizations are responsive and effective, because they function as partnerships of local residents, lenders and other business leaders, and representatives from local government. NeighborWorks® network results include:

—forging private-sector partnerships that revitalize blighted communities to create an infusion of job retention and economic development strategies to local economies;

—providing full-service affordable rental housing that provides citizens with much more than a roof over their heads;

—creating homeownership incentives that help individuals realize the American dream and build wealth for their families and communities;

—educating communities about strategies that improve safety and attract wealth-building opportunities.

Neighborhood Housing Services of America (NHSA)

Flexible financing enables NeighborWorks® organizations to be nimble, competitive and effective. Neighborhood Housing Services of America works in partnership with NeighborWorks® America to meet special secondary market needs of NeighborWorks® organizations and their clients. The primary mission of NHSA is to operate a specialized secondary market created to replenish the revolving loan funds and capital pools of local NeighborWorks® organizations. As such, it has become an important tool for challenging predatory lenders.

PROJECTED OUTCOMES FOR FISCAL YEAR 2006

This is a time of unprecedented challenges and opportunities in housing and community development. NeighborWorks® America is in a prime position to deliver results.

An appropriation of $118 million will allow the NeighborWorks® system to:

—Triple the number of certified homeownership educators and counselors to serve 2 million people each year by 2007 to ensure that the largest investment of an individual's life is successful.

—Generate $19.60 in other investment for every dollar appropriated to NeighborWorks® America, for a total reinvestment of over $2.3 billion in American communities.
—Establish a national foreclosure prevention center (the NeighborWorks® Center for Foreclosure Solutions) to identify the most common causes of foreclosure and deploy effective prevention and intervention strategies.
—Train thousands of community leaders across the country in community development and housing; homeownership and community lending; home-ownership education and counseling; construction, production, real estate and housing management; nonprofit management and leadership; and economic development, revitalization and community building to become preeminent practitioners.
—Increase financial fitness education in underserved markets to build better money management skills that position families to build assets and achieve financial independence.
—Work with government and private sector partners to provide affordable loans, rental housing and community development that improve job retention and buoys local economies.

For fiscal year 2005, NeighborWorks® America received an appropriation of $115 (minus an across-the-board rescission). The proposed increase for fiscal year 2006 will further NeighborWorks® America's work to create and sustain minority homeownership through grants to NeighborWorks® organizations, as well as continue to allow NeighborWorks® America to attract and retain qualified and competent staff in community development.

PRIORITIES FOR FISCAL YEAR 2006

In developing the Corporation's fiscal year 2006 budget, NeighborWorks® America is setting more aggressive expectations for the NeighborWorks® system. NeighborWorks® America has always worked to be good stewards of the funds that Congress has entrusted to us, and the Corporation continues to diligently work to maximize our efficiency and effectiveness. In order to meet these expectations, NeighborWorks® America and the NeighborWorks® system will:
—Leverage strategic partners and resources to stay on the forward edge of housing and community development needs.
—Monitor the efficiency and results of the NeighborWorks® network through financial and performance reviews.
—Fuel network innovation that can be applied across the Nation.
—Build skills and performance in the housing and community development field.

Leverage Strategic Partners and Resources

Historically, the success of the NeighborWorks® System has far exceeded its visibility. In fiscal year 2005, NeighborWorks® America is taking a major step forward in enhancing visibility of NeighborWorks® by launching a public awareness and branding campaign: "NeighborWorks® America—Transforming Lives and Strengthening Communities." The campaign will unite the corporation with the national network it supports—235 NeighborWorks® organizations across 49 States. Neighborhood Reinvestment is adopting the name "NeighborWorks® America" as its public trade name. A resolution of the Board of Directors directing the Corporation to launch this public awareness and branding campaign passed unanimously on September 20, 2004.

More awareness of NeighborWorks® America will help us serve more communities, creating a force of empowered consumers and engaged communities. NeighborWorks® America will promote several tools to empower neighbors to maximize their financial position, to become informed homebuyers and savvy homeowners whose home values grow and provide equity. As NeighborWorks® America, united with our national network under one name and a singleness of purpose, we will become a more visible and powerful national force for change.

Increase the Efficiency and Results of the NeighborWorks® Network

Our scale and history allows NeighborWorks® America and its affiliated NeighborWorks® network to be responsive and innovative, successfully navigating the rocky terrain of the current housing and community development landscape. To keep pace with the breakneck and challenging changes in the current environment, we will:

Demand Accountability and Results

NeighborWorks® America is committed to promoting and maintaining a network of productive, well-managed, nonprofit housing and community-development corporations that deliver high quality services responsive to local needs and have a measurable impact on the communities they serve.

Conduct Rigorous and Thorough Audits and Reviews of NeighborWorks® System

As part of its responsibility to be a strong steward of Federal funding and protect the investment of other partners and the reputation of the NeighborWorks® network as a whole, NeighborWorks® America uses a rigorous and thorough audit and review of all NeighborWorks® programs and organizations. Those who don't measure up are given a defined time period to turnaround or leave the network. We demand high-performance and results.

Through a system of continuous monitoring, we assess the risks faced by each NeighborWorks® organization with a thorough collection and analysis of programmatic and financial data.

Measure the Success of the Community Development Field

As stewards of taxpayer money and advocates for our most needy neighbors, we must make sure our investments are working in ways that truly make a difference. It's not good enough to talk about simple counts of housing units produced or dollars leveraged. We must be willing to hold ourselves accountable for results. If banks and actuaries can refine their investment and insurance packages with increasing accuracy and sophistication, we also must find new ways to measure the impact of our work. This year NeighborWorks® America will begin using the Success Measures Data System as one important tool to help answer the question: are we making a difference? This state-of-the-art program can measure dividends such as changes in safety, property values, levels of civic engagement and the quality and performance of schools and healthcare, helping us to work smarter in serving the real and present needs in our communities.

The development of this index has been encouraged by OMB through its Program Assessment Rating Tool (PART) process. Federal Reserve Chairman Alan Greenspan recently cited Success Measures as a model tool for providing "objective and quantifiable standards to assess community development programs."

Improve Efficiency and Coverage of Underserved Areas

The efficacy of the NeighborWorks® system is measured in productivity, more efficient use of resources and more responsive service delivery. In many underserved areas, the most effective growth strategy is to expand the reach and/or programmatic services of an existing network member or to facilitate a merger of two organizations to create one powerful organization with greater impact and efficiency.

We receive far more applicants to become NeighborWorks® members than we charter. Through a careful affiliation process, NeighborWorks® America ensures that before any organization is chartered as a NeighborWorks® entity, it is sound and productive; led by a board of directors reflective of the community it serves; and committed to a mission with goals, values, programs and accomplishments compatible with the focus and priorities of the NeighborWorks® network.

Invest in What Works

Responsible, responsive real-estate development and lending requires dependable equity capital grants. NeighborWorks® America provides our network with this critical gap funding and equity, allowing NeighborWorks® organizations to make loans for home purchase, property rehabilitation and small business loans.

NeighborWorks® America also provides grants to NeighborWorks® organizations to address a range of community needs, such as financial fitness education, homeownership counseling and education, development of affordable rental property, loans for improving safety, and much more.

Fuel an Engine of Innovation

The structure of the NeighborWorks® network facilitates collaborative learning to harness all the practical knowledge picked up on the ground and in our research. Initiatives that allow NeighborWorks® organizations to learn directly from each other include: the NeighborWorks® Campaign for Home Ownership, the NeighborWorks® Multifamily Initiative, the NeighborWorks® Rural Initiative, and the NeighborWorks® Insurance Initiative and its National Insurance Task Force. To help organizations stay on the forward edge of business practices and community development, we deploy several strategies:

Topflight Expertise and Coaching

NeighborWorks® America deploys a team of experts to provide NeighborWorks® organizations with the expertise and coaching needed to continue to serve resident needs.

This on-call team provides help in six areas:

—Organizational development;
—Resource development and marketing;
—Community revitalization and business planning;
—Management systems (including technology and financial management);
—Single-family housing and lending; and
—Real-estate development and management.

The NeighborWorks® Campaign for Home Ownership

The NeighborWorks® Campaign for Home Ownership is a joint effort of government, banks, the insurance industry, secondary markets, the real-estate community and others, coordinated by NeighborWorks® America in conjunction with more than 154 community-based NeighborWorks® organizations. Since 1993, the combined efforts of the Campaign have created more than 90,000 new homeowners (the majority of whom are low- and moderate-income minority families) and provided counseling to more than 500,000 individuals. As a result, $8.5 billion has been invested in many of America's distressed communities. The campaign provides resources and education for homeowners and empowers those for whom the American dream is thought out of reach.

HomeOwnership Centers

NeighborWorks® HomeOwnership Centers throughout the Nation offer one-stop shops for a broad range of homeownership services available to low- and moderate-income families including unbiased advice, counseling, training, referrals to partners such as lenders, real-estate agents, inspectors, contractors, and special financial assistance to income-qualified buyers. The Centers can also help existing homeowners with housing rehabilitation advice and assistance along with maintenance training. Financial counseling to avoid credit problems, loan delinquencies and foreclosures is also available.

NeighborWorks® America expects to add at least 10 percent more HomeOwnership Centers in fiscal year 2006. On average, after becoming fully operational, each HomeOwnership Center will produce over 100 new homeowners per year.

Between 2003 and 2007 the Campaign for Home Ownership set a goal to reach 30,000 minority homeowners. This goal also helps support the White House's Minority Homeownership Initiative. We are making great strides in achieving this goal.

—67 percent of those assisted by the NeighborWorks® Campaign for Home Ownership are low- or very low-income households. Only 25 percent of the clients of conventional mortgage lenders have low or very low incomes.
—51 percent of the households assisted by the NeighborWorks® Campaign for Home Ownership are ethnic minorities, compared to only 25 percent of the clients served by conventional mortgage lenders are minorities.
—46 percent of the buyers assisted by the NeighborWorks® Campaign for Home Ownership are female, compared to only 21 percent of the clients of conventional mortgage lenders.

NeighborWorks® Homeownership Activities for Fiscal Year 2006

In fiscal year 2006, the NeighborWorks® System will continue to focus attention on helping qualified lower-income families and individuals purchase, maintain and stay in their homes for the long term. Our plans include:

—Delivering new training classes on "Reaching Underserved Homebuyers" that will continue to be offered regularly at the NeighborWorks® Training Institutes;
—Designing a new "minority marketing toolbox" in 2005 that will include templates, tools and marketing materials to help local NeighborWorks® organizations implement enhanced marketing efforts to attract more minority customers as potential homebuyers;
—Promoting expansion of financial education and homeownership-education programs with new partners such as churches, schools and employers.

Financial Literacy and Education to Help Avoid Predatory Lending

Predatory lending tactics are at an all time high, particularly those preying on minority families, immigrants, and financially less-sophisticated borrowers. Too often bad actors encourage homeowners to pursue inappropriate debt consolidation, refinancing schemes, home improvement, or home equity loans that threaten the assets that the NeighborWorks® System has worked so hard to help them acquire. NeighborWorks® America just added a new course to its training curriculum to help combat predatory lending. The class filled up immediately and given this ballooning need, we are working to accommodate more.

Other strategies we use to combat predatory lending include:

—A Financial Fitness Program that prepares families to build sound finances and be aware of predatory tactics. The Corporation developed standards, adapted and created training materials, trained trainers to initiate this comprehensive program, and supports its growth;

—The addition of 10 Financial Fitness sites in fiscal year 2006 to expand the reach of financial education efforts across the network;

—A new consumer training curriculum for "Refinancing Your Home" that can be offered to assist existing homeowners in making smarter choices when considering the multitude of options in refinancing their home;

—A new consumer training curriculum on "Buying a Manufactured Home" to help consumers who are considering buying manufactured homes; and

—A study on the cost/benefit of providing pre-purchase counseling to consumers.

Center for Foreclosure Solutions

We need to prevent foreclosures earlier—before a family even thinks of buying a home. NeighborWorks® America's approach is to provide education and counseling at every stage—pre- and post-ownership. We want to empower individuals, their families, their communities and their economies to be on a path of continued wealth creation. Informed consumers can leverage better service, lower costs and a more transparent, accountable lending and real estate industry.

Over the past 10 years, there have been dramatic increases in high-risk lending, growing job instability and excess consumer debt obligations that are all trademarks of susceptibility to foreclosures. NeighborWorks® America has established the Center for Foreclosure Solutions (CFS) to research and test homeownership preservation efforts.

Our NeighborWorks® affiliate—Chicago Neighborhood Housing Services—is blazing trails for other organizations across the Nation. Chicago NHS teamed up with city officials and 20-plus lenders to reduce geographically concentrated foreclosures that leave neighborhood blocks riddled with vacant homes. The Home Ownership Preservation Initiative (HOPI) provides counseling to financially strapped owners and assistance in working with lenders to discuss refinancing, lowering interest rates and modifying payment plans. In the past 18 months, the HOPI campaign prevented 650 foreclosures through innovative outreach and counseling efforts.

The Center for Foreclosure Solutions seeks to expand successful initiatives to reduce foreclosures and its many negative impacts on borrowers and communities.

Housing Choice Voucher Homeownership

Through June 2004, almost 3,000 Section 8 households have completed homeownership education training through local NeighborWorks® organizations and 555 have purchased homes through this program.

This is the result of NeighborWorks® organizations forging partnerships with 75 local public housing authorities to develop and implement comprehensive local and regional Housing Choice Voucher Homeownership programs, formerly known as the Section 8 to Homeownership program. These partnerships are built upon the NeighborWorks® network's solid experience in pre- and post-purchase counseling, innovative mortgage financing and in leveraging public resources with private investment.

In addition to national funding, the NeighborWorks® America is assisting local Section 8 administrators and NeighborWorks® organizations to develop Housing Choice Voucher Homeownership Programs through national and regional training, technical assistance, ongoing evaluation and publication of lessons learned. With support from the U.S. Department of Housing and Urban Development, NeighborWorks® America has hosted numerous training sessions at its NeighborWorks® Training Institutes and other venues to help build capacity in the Housing Choice Voucher Homeownership Program.

Rural Development

The NeighborWorks® network has become increasingly active in rural communities around the country. Today, 70 out of 230 chartered NeighborWorks® organizations—about 30 percent of the network—serves rural populations. The needs of rural homeowners and renters differ in many aspects from those in urban or suburban areas. In many States, rural areas have the highest rate of substandard housing, the highest poverty rate, and median incomes often 35 percent or less than the median incomes of urban residents. Unfortunately, rural areas traditionally have lacked the financial resources for home financing.

During fiscal year 2006, direct investments by NeighborWorks® organizations serving low-, very low- and moderate-income residents in rural communities across America are again expected to surpass $500 million. At this rate of leveraged direct investments, NeighborWorks® America expects to achieve the benchmark goal of providing $1 billion into underserved rural markets over the 2-year period ending December 31, 2005. The Corporation will continue to support the needs of NeighborWorks® organizations serving rural populations (74 as of December 2004) by implementing a plan for at least one pilot expansion into a perennially underserved rural region not currently being served by a chartered NeighborWorks® organization.

Affordable Rental Opportunities

The desire to own a home is strong across all socioeconomic groups, but not everyone is adequately prepared, and the strongest communities offer multiple housing options. Therefore it remains important to have viable rental housing—especially units that allow a safe, stable environment—with rents affordable enough for occupants to accumulate savings. Tomorrow's first-time buyers are renters today.

A major focus of NeighborWorks® Multifamily Initiative, which provides affordable rental housing, has been on strengthening aging property portfolios that may be suffering a weakness in cash flow. Our expert coaches and analysts suggest operational improvements, and explore creative ways to restructure financing, with an eye to improving cash flow across the entire portfolio.

NeighborWorks® America also promotes more opportunities to increase the supply of affordable rental homes. In 2004, the Corporation was able to use the special set-aside of $5 million for multifamily housing to promote mixed income rental homes that truly serve their communities by providing more than just sound housing.

NeighborWorks® organizations in our Learning Center Consortium provide afterschool care, job training, health care, parenting classes and much more. NeighborWorks® America has commissioned a study to measure the impact on the difference made on the kids and their families in the form of dropout rates, GPA, attendance rate, and job retention.

Build Skills and Performance in the Housing and Community Development Field

NeighborWorks® Center for Homeownership Education and Counseling

NeighborWorks® is the Nation's largest certifier of high-quality homeownership educators and counselors, working to empower consumers to make the biggest investment of their lives a successful one. Although the value of homeownership education and counseling to homebuyers is supported by research and is increasingly recognized as a powerful tool to promote neighborhood revitalization, the quality is uneven and the coverage insufficient. There are few national certification standards, limited continuing-education requirements for trainers and counselors, gaps in coverage across the Nation, and a lack of quality control for homeownership education and counseling—ranging from intensive, multi-day curriculum and standards to "sham" counseling programs that lure potential buyers into predatory loan deals. There is also a dearth of well-trained educators and counselors to meet the growing national need.

To address these concerns, NeighborWorks® America, through the nationally recognized NeighborWorks® Training Institute, has launched the NeighborWorks® Center for Homeownership Education and Counseling (NCHEC) to create a national force of high-quality homeownership and financial education counselors. To date these counselors have helped more than 500,000 Americans gain critical financial literacy skills and make the most of homeownership.

NCHEC aims to increase the number of homeownership educators and counselors trained and certified through the NeighborWorks® Training Institute from 700 to more than 2,000 per year—indirectly ensuring the education and counseling of several million individuals and families by 2007. The total number of counselors and educators provided both certification training and continuing education will increase to more than 3,000 per year.

In the fall of 2004, the Department of Housing and Urban Development awarded NeighborWorks® America $7.75 million over 2 years to train and certify HUD-approved housing counselors around the country through NCHEC. In addition to expanded homeownership and community-lending training offered at the NeighborWorks® Training Institutes, NCHEC will partner with other intermediaries, statewide counseling collaboratives, and NeighborWorks® organizations to offer trainings in local settings around the country.

NeighborWorks® Training Institutes

For more than 15 years, NeighborWorks® America has been providing outstanding community development training in the country through its NeighborWorks® Training Institutes, which are held four to five times a year in different cities throughout the United States. In recent years, NeighborWorks® America has begun taking its NeighborWorks® Training Institute courses to local markets in the form of "place-based trainings" conducted in collaboration with local and regional partners.

CONCLUSION

Let me close by thanking the subcommittee for the opportunity to brief you on our work, and the results generated by NeighborWorks® America's congressional appropriation. The NeighborWorks® System and NeighborWorks® America's congressional appropriation represents a precious asset for 235 community development organizations and more than 2,700 communities across America. With our leveraging of dollars, NeighborWorks® has been efficient and effective in ensuring the maximum impact of our Federal appropriation. Congress has allowed NeighborWorks® America to be flexible and responsive to local needs; as a result, families and communities are stronger and more self-reliant.

The need for NeighborWorks® has never been greater. Federal and State policies are aggressively promoting home ownership. Mortgages are becoming increasingly complex and risky. Personal debt is rising. And, stubborn homeownership and wealth gaps persist despite economic improvements and recent increases in minority homeownership.

NeighborWorks® America is committed to continuing to build healthy, strong and safe communities all across America. Your continued support is vital to us in accomplishing this goal.

U.S. CONSUMER PRODUCT SAFETY COMMISSION

PREPARED STATEMENT OF THOMAS H. MOORE, COMMISSIONER

Mr. Chairman, Ranking Member, and members of the subcommittee, thank you for providing me with this opportunity to submit testimony on the U.S. Consumer Product Safety Commission's (CPSC) fiscal year 2006 appropriations request. The full details of our fiscal year 2006 appropriations request are set out in our budget document submitted earlier this year to the subcommittee. These details reflect the agency's initial efforts to outline possible impacts of the administration's broad efforts to reduce non-security Federal spending. We anticipate that we will be able to provide more specificity after we perform a more careful and systematic review of our costs and our safety programs later this summer.

In summary, for fiscal year 2006, the President's request for our agency is for $62,499,000 which is an increase of $350,000 above our fiscal year 2005 appropriation and will support the agency at approximately 446 FTEs. If measured from our fiscal year 2005 funded FTE level, the request for fiscal year 2006 represents a FTE reduction of 25 FTEs. However, the average FTE level for fiscal year 2004 was 461 FTEs and because we now have no intention of staffing up to our planned 2005 level, actual reductions will be around 15 FTEs. We estimate that we will be able to achieve these reductions through attrition and we are very hopeful that with a careful review of our costs and our safety programs we will be able to achieve these reductions with our safety programs largely intact and with minimal disruption to our agency operations.

IMPACT OF BUDGET REQUEST

CPSC is a staff intensive organization with about 90 percent of its funding allocated to staff salaries and office rent. At the heart of CPSC's operation is its staff, without question, our greatest and most important asset. In order to keep our staff intact and sustain our safety programs at our fiscal year 2005 authorized level we would need additional funding of $2.4 million above our fiscal year 2005 level. This $2.4 million increase would simply fund salary and rent increases in support of 471 FTEs. Any funding level which does not contemplate an increase or contemplates an increase less than $2.4 million will require some staff adjustments. The requested increase of $350,000, instead of the needed $2.4 million, will certainly mean a reduction in our FTEs but we are confident that we can manage this reduction without forced layoffs.

In presenting our budget request to the subcommittee today we are mindful of our Nation's present state of affairs. Considering our Nation's prevailing budget priorities there are certainly some positive implications in the President's recommendation for CPSC. Our product safety work and safety guidance provide a sustained, uniform measure of protection for our Nation's families, and also provide businesses a national, level playing field for both domestic and imported consumer products. Taking into account that the administration proposes to cut the Nation's non-security discretionary accounts by nearly 1 percent in its fiscal year 2006 budget, the President's budget request of a $350,000 increase shows some confidence in CPSC and its programs and we at the Commission are dedicated to continue earning that confidence.

However, we must put the consequences of our increase in the proper perspective. Since 1994, CPSC has been forced to reduce its funded FTE level by 14 percent from 518 to the fiscal year 2006 proposed level of 446. This erosion of our most valuable asset comes despite the fact that we still have over 15,000 types of consumer products under our jurisdiction; creative new technologies constantly introduce potentially new product hazard issues; new consumer uses for products originally created for commercial use are being introduced; imports are increasing, many from countries that may not have similar consumer product safety standards; and despite the fact that we still face over 25,100 deaths and over 33.3 million injuries each year associated with consumer products under CPSC's jurisdiction.

CPSC'S IMPORTANT SAFETY WORK MUST CONTINUE

By all current measures, CPSC provides both tremendous service and tremendous value to the American people. Each year through reductions in deaths, injuries, and other costs associated with unsafe products, such as health care costs and property damage, CPSC saves the Nation many times the agency's annual budget. Our agency is the major factor in the overall 30 percent decline in the rate of deaths and injuries related to consumer products since 1974. During that time, through our standards work, compliance efforts, industry partnerships, and consumer information, there has been a 42 percent reduction in residential fire deaths, a 72 percent reduction in consumer product-related electrocutions, a 36 percent reduction in consumer product-related carbon monoxide deaths, an 86 percent reduction in poisoning deaths of children younger than 5 years of age, an 88 percent reduction in baby walker injuries and a 92 percent reduction in crib-related deaths. We expect the annual number of deaths and injuries prevented by just these examples to reduce societal costs by almost $16 billion. These savings by themselves are over 250 times CPSC's proposed fiscal year 2006 funding request.

To further illustrate how successful CPSC's staff is in protecting American consumers by addressing the unreasonable risk of harm posed by many, many consumer products we can look at some fiscal year 2004 numbers. For example, CPSC completed 356 cooperative recalls involving over 216 million product units. The Commission staff also obtained many other corrective actions that did not involve a consumer level recall. We completed 10 civil penalty cases that resulted in almost $4.2 million in fines for failure to report hazardous defects and other violations associated with our various statutes and regulations. We assisted in securing 2 criminal convictions for violations of the Federal Hazardous Substances Act. In addition, CPSC staff, working with the U.S. Customs, conducted 278 seizures and detained over 6.7 million units of imported products that were in violation of U.S. safety standards.

Moreover, we informed the public of hazardous products through 312 press releases, 13 video news releases, 2 million distributed publications, specific consumer product safety discussion appearances on network TV shows, and through CPSC's consumer hotline, web site, and National Injury Information Clearinghouse. We had 11.9 million visitors to our Web site, 159,200 readers of our Consumer Product Safety Review, and 140,000 callers to our consumer hotline.

I would like to note that thus far, for fiscal year 2005, in our enforcement area, the Commission is on a record pace for assessing civil penalties against companies who fail to report product hazards to the Commission as required by our statutes. We have completed five civil penalty cases that have resulted in $8.5 million in fines including our largest assessing ever issued of $4 million.

These numbers by themselves demonstrate the indisputable consumer product safety role that the Commission has performed for the American consumer over the years. We at the Commission also strongly feel that many, many more deaths and injuries have been prevented as a result of the heightened attention given to safety issues by manufacturers and consumers due to CPSC's leadership. These results clearly illustrate the benefits of CPSC's Federal presence in today's consumer product marketplace and therefore provide substantial justification for present and future consideration for keeping our safety programs intact.

FUTURE CONSIDERATIONS

Given future funding considerations, there is one particular funding area that I have mentioned in previous budget submissions and I still strongly feel that we can provide better service to the American public if this area is funded in the future. It is crucial to our mission and continued success that we are able to upgrade and establish a modernization cycle for our information technology (IT) infrastructure and databases. As a data-driven agency, we are dependent on information technology and therefore must continually invest in the tools we use to identify and analyze hazards.

For fiscal year 2005, because a Commissioner's office remained vacant for 7 months and, because we are taking steps now to reach the anticipated fiscal year 2006 FTE level, we estimate that we will have some financial flexibility to reallocate funds from salary savings to address some of our IT needs. However, with the anticipated reductions in our FTE funding, we certainly will no longer have that sort of financial flexibility to reallocate funds from salary savings in the future. Depending on temporary salary savings is no way to fund IT needs. The lack of a permanent capability to maintain and enhance our systems will jeopardize our future work. The long-term benefit to our work of a strong, proactive IT program can not be overstated.

CONCLUSION

Our small agency has found that cooperative partnerships, innovative initiatives, and open, voluntary participation of the interested community contribute to a successful, cost-effective and least burdensome regulatory scheme appreciated by both those whom we serve as well as those whom we regulate. For example, www.Recalls.gov results from a CPSC partnership with five other Federal agencies and features a website which provides a one-stop shop for all government-regulated product recall information. This information is helpful to both consumers and businesses. In 2004, over 900,000 visitors logged on to this site.

Additionally, we continued other cooperative initiatives the "Fast Track Product Recall Program" and the annual "Recall Roundup Program." Both of these initiatives are designed to remove unsafe consumer products from the marketplace and the homes of consumers. For example, nearly 950 firms have participated in our "Fast Track Product Recall Program" resulting in over 1,679 recalls involving over 190 million consumer product units.

In conclusion, Mr. Chairman, we all recognize that the Nation is again facing very difficult decisions regarding its allocation of resources. The President, Congress, and the American public have all shown confidence in CPSC and its consumer product safety programs. However, despite all the progress the Commission has made, and is currently making, in reducing deaths and injuries related to consumer products, the marketing of unsafe consumer products remains a major national problem. We still have a long way to go to prevent hazardous consumer products from killing and injuring people. The continued support of this subcommittee is essential to a successful fulfillment of our mission.

I strongly urge the subcommittee to fully support our activities by providing the $62.5 million requested.

PREPARED STATEMENT OF HONORABLE HAL STRATTON, CHAIRMAN

I am pleased to have the opportunity to present the appropriation request for the U.S. Consumer Product Safety Commission (CPSC) for fiscal year 2006. Most Senators are generally familiar with the mission of the CPSC, but because we are new to your subcommittee, I would like to give you an overview of our agency and the work that we do to reduce product hazards and to increase product safety for Americans young and old.

The Consumer Product Safety Commission is a bipartisan, independent agency charged with protecting the public from unreasonable risks of serious injury or death from more than 15,000 types of consumer products under the agency's jurisdiction. Deaths, injuries and property damage from consumer product incidents cost the Nation more than $700 billion annually. Since its inception, the CPSC has delivered critical safety benefits to America's families and has made a significant contribution to the 30 percent decline in the rate of deaths and injuries related to hazardous consumer products. We are proud of our mission and our achievements, and we appreciate the support that Congress has extended to the Commission and to its goals over the years.

The CPSC performance budget request for fiscal year 2006 is $62,499,000. Compared to some of the other agencies under your subcommittee's jurisdiction, this is not a relatively large amount, but I can assure you that we respect the fact that these dollars come from hard-working American taxpayers, and we will spend these dollars efficiently and effectively in assuring consumers that the products they are bringing into their homes, and into other aspects of their lives, are as safe as possible.

This year's requested level of funding is an increase of $350,000 over our fiscal year 2005 budget. This is a smaller increase than we have requested in the past; however, I am confident that with strong leadership and good management, we will not only continue to maintain our basic safety mission but also continue to make progress on the priorities that we have established for the upcoming year.

We are a small agency with a big mission. We currently have approximately 460 FTE staff who work in our headquarters and our laboratory site in suburban Maryland, and at our field locations across the country. CPSC is a staff intensive organization with about 90 percent of its funding going to staff salaries and office rent. To accommodate expected staff salary and office rent increases in 2006, we are planning to reduce our staffing numbers during the year through attrition with a goal of 446 FTE staff by the start of 2006. The final FTE staffing figure may end up higher than that since we are seeking to identify other efficiencies throughout the agency. For example CPSC is in full compliance with the Telework Act, and this has led to rent savings at our field locations.

As I noted earlier, I would like to take this opportunity to give a brief overview of the agency for the Senators who did not serve on our previous appropriations subcommittee. The CPSC has three core functions: hazard identification and reduction, compliance activities, and consumer information.

The CPSC's Office of Hazard Identification and Reduction (HIR) collects information needed to assess product hazards and develop injury reduction strategies. The staff collects data on consumer related injuries and deaths, as well as hazard exposure information, for those products under our jurisdiction. The basis of our injury information is our National Electronic Injury Surveillance System (NEISS) which provides national estimates for injuries related to consumer products. Along with CPSC's field staff, HIR also investigates specific injury cases to gain additional knowledge and data about injuries or hazards and how the reported product was involved.

Because quality data is central to the execution of CPSC's mission, we are continuing to strengthen our data collection and analysis process. Recent improvements include the development of new statistical systems for fire deaths and injuries and the implementation of our National Burn Center Reporting System which focuses on children's clothing. Staff also conducts several types of studies each year, including special investigations and emerging hazard evaluations. Taken together, these activities lay the groundwork for our standard setting and other hazard reduction activities.

I should mention at this point that the Commission is currently working on two new flammability standards that if promulgated would be the most significant safety regulations that the CPSC has ever issued. Mattresses and bedding materials continue to be one of the main contributors to residential fire deaths. The Commission recently issued a proposed standard addressing open flame mattress flammability and an Advance Notice of Proposed Rulemaking on bedclothes.

Residential fires involving upholstered furniture are another leading cause of fire deaths and injuries. CPSC staff is developing a revised draft flammability standard containing performance requirements to address both cigarette and open flame ignition of upholstered furniture and is preparing a package of regulatory options for the Commission's consideration.

When a safety standard or ban is established, it is CPSC's Office of Compliance, working closely with the agency's field staff, that enforces the law. The Compliance office also conducts investigations of product hazards to determine whether corrective action (recall) is necessary. CPSC may initiate an investigation based on information we have received from outside sources such as letters and calls from consumers, newspaper reports, trade complaints, and inquiries from State and local governments. Alternatively, CPSC staff may start an investigation based on statutorily required product hazard reports from manufacturers and retailers. The Office of Compliance has recently announced a new model for reporting by retailers; it has already resulted in many more reports.

CPSC staff conducts programs to monitor compliance with safety standards by conducting field inspections of manufacturing facilities and distribution centers and making purchases at retail establishments or via catalogs or the internet. Additionally, staff conducts surveillance and sampling of imported products at ports of entry. In 2004, CPSC staff conducted 278 seizures and detained over 6.7 million units of imported products for possible safety hazards.

Our governing statutes permit the Commission to assess civil penalties and to seek public notice and corrective action for defective products that create a substantial risk of injury to consumers. Recently, we announced the largest civil penalty ever issued by the CPSC, $4 million, against a company that failed to report to the agency some 12 million products that posed a danger to young children. Due to aggressive enforcement of our safety laws, 2005 is likely to be the highest penalty year in the history of the Commission. I should note that all of these amounts are returned to the U.S. Treasury and none are retained by the CPSC.

Also in 2004, the CPSC announced 356 recalls that involved a record 218 million product units. The largest of these recalls involved toy jewelry that contained accessible lead, a serious health threat to children. Other recalls involved a range of products including bunk beds that posed a strangulation hazard, floor fans that posed a fire hazard, and strollers that posed a head injury hazard.

One key element of any recall is targeted public notices to inform owners of a recalled product of the hazard and the remedies available. That effort is led by our Office of Information and Public Affairs using a wide range of resources to publicize the recall.

CPSC continues to be pro-active in improving recall effectiveness. Last year, we launched the Neighborhood Safety Network (NSN), a grassroots effort to communicate important safety messages to vulnerable and hard-to-reach populations. In partnership with other government agencies and private sector organizations, NSN is reaching populations categorized by age, region, culture or economic status. The goal of NSN is to get safety information to larger audiences quickly and efficiently. I am especially proud that CPSC has been very successful in improving outreach to the Nation's Hispanic community. In the last 2 years, visits to the CPSC website's Spanish home page have jumped 155 percent. Phone calls from Spanish-speaking consumers to CPSC's Hotline tripled in fiscal year 2004 from the previous year.

Another initiative that I am proud of is Recalls.gov. Over 1 million visitors have logged on to Recalls.gov, which provides consumers with one single source to get information on all the recalls conducted by the Federal Government. The site also allows consumers to report a problem with a consumer product, motor vehicle, food or environmental product.

CPSC led the way in bringing together the EPA, FDA, NHTSA, the Coast Guard and Department of Agriculture to create Recalls.gov in the Fall of 2003. In November 2004, we added a new "Recent Recalls" feature, which provides your constituents and consumer reporters with a link to breaking news about product recalls. To build on the success of Recalls.gov and further expand the reach of the Web site, CPSC is creating a feature that allows parents and consumers to sign-up for e-mail notifications when recalls occur of products about which they are concerned.

Another important outreach effort is our annual Recall Roundup Campaign which focused last year on resale outlets such as thrift stores. CPSC joined forces with the National Association of Resale and Thrift Shops, the National Safe Kids Campaign, and the Danny Foundation to stop resale, consignment and thrift shop stores from selling previously recalled or banned products. Additionally, safety seminars were conducted across the country to educate store employees about how to check their stores for hazardous products. The CPSC also continues to work with companies like eBay to ensure that dangerous products are not sold on public auction websites.

On another front, recognizing that the market is global and that the vast number of our consumer products are imported from overseas, I established a new office, the Office of International Programs and Intergovernmental Affairs, to focus on these challenges. Through this initiative, CPSC has established working relationships with our counterparts in other countries through the execution of formal memoranda of understanding, or MOUs, with China, the European Commission, Costa Rica and Taiwan. The agency expects to formalize MOUs with other countries including India, Canada, Mexico, Peru and Chile in the near future.

As the first CPSC Chairman to visit China, my goal is to get beyond the American ports of entry and get to the actual sites around the world where these products are produced and make certain that our safety message and safety standards are understood and respected globally. For example, last June I had the opportunity to return to China to address the International Organization for Standardization on toy safety. China is now the No. 1 toy producing country in the world, and the United States is the No. 1 toy consuming country in the world. It is critical that we work to make certain that these products are safe for American families before they are ever put on a ship bound for an American port.

As Chairman of the CPSC, I am committed to openness and transparency in government. Prior to my tenure, it was not the practice to have oral testimony by citizens or stakeholders at most agency regulation briefings. We changed that policy because I believe it is critical that we hear from the families and the businesses that are impacted by our decisions.

Further, last October, we launched two pilot programs to invite public comments on product safety voluntary standards positions and research reports. At present, CPSC staff is involved in the development of over 60 consumer product voluntary standards. This pilot program is inviting public comment on a number of staff's voluntary standards activities including those on smoke alarms, pool safety, portable generators, bunk beds and child resistant gasoline containers.

Before closing, I would like to update the committee on the status of CPSC's laboratory modernization. No funds for this project are requested in this year's budget request; however, a feasibility study has just been received that includes a final design that CPSC staff, the General Services Administration (GSA) and the design contractor agree would meet the agency's needs. The projected cost of this proposal is approximately $23 million dollars which would be divided equally between the GSA building fund and the CPSC providing specific laboratory build-outs. Construction could begin as early as 2009. CPSC staff will keep the committee advised during the year on the status of this proposal as additional information becomes available.

I appreciate the committee's support of our work, and I want to again assure the Senators that we at the CPSC are committed to our mission to reduce product hazards and to assure the safety of consumer products in American homes.

U.S. OFFICE OF GOVERNMENT ETHICS

PREPARED STATEMENT OF MARILYN L. GLYNN, ACTING DIRECTOR

Thank you for the opportunity to present this statement in support of the request of the U.S. Office of Government Ethics (OGE) for fiscal year 2006 resources of $11,148,000 and 80 FTEs. This request is the same as OGE's fiscal year 2005 appropriated amount.

The Office of Government Ethics is responsible for overseeing the ethics program of the executive branch, a program designed to help prevent conflicts of interest and promote integrity in government. OGE sets the requirements of the program, develops executive branch-wide policies, serves as a resource/consultant to agency ethics officials and monitors agency programs to help ensure that the agencies are carrying out their responsibilities effectively. While each executive branch agency is responsible for carrying out many of the day-to-day functions of the program, OGE's specific role includes: reviewing and certifying the financial disclosure forms filed by Presidential nominees requiring Senate confirmation; reviewing and certifying annual financial disclosure reports filed by senior executive branch employees; serving as the primary authority on executive branch conduct and financial disclosure issues; conducting evaluations of agency ethics programs; training agency ethics officials and developing employee training materials used by agencies in their ethics training; offering direct support to agencies through a desk officer program, under which OGE staff serve as ethics liaison to executive branch departments and agencies; and providing interpretative guidance of the criminal conflict of interest laws.

The ethics program that OGE directs is part of the basic infrastructure that supports good governance within the executive branch of the Federal Government. The resources expended by OGE to help promote integrity and prevent conflicts of interest are small compared to the resources expended by investigators and prosecutors who enforce ethics and conflict of interest rules and laws. Moreover, our preventive efforts help guard against the loss of government resources through inadvertent or deliberate misuse. We believe the resources we have requested are those necessary to support a strong ethics program.

FISCAL YEAR 2006

We would like to highlight some of the major programs we anticipate for fiscal year 2006.

Although the influx may not be as great as that anticipated for the current fiscal year, OGE expects that there will continue to be a significant number of Presidential nominees to positions requiring Senate confirmation during the second year of the current administration. OGE performs a key role in clearing these nominees, a process which is designed to help them understand the application of the conflict of interest requirements to their government service and to secure their agreement to take the necessary steps to resolve potential conflicts of interest. Our goal is to review nominee financial disclosure statements in a timely manner to avoid any unnecessary delay in the nomination/confirmation process. Once an individual is appointed, OGE follows through to see that any agreements made by an appointee to address potential conflicts of interest are carried out. In addition, over this period, OGE will continue to conduct a second level review of over 1,000 annual and termination financial disclosure statements filed by Presidential appointees each year.

The Intelligence Reform and Terrorism Prevention Act of 2004 (Public Law 108–458) directed OGE to prepare and submit two reports to Congress in fiscal years 2005 and 2006. The first report, which was delivered in March 2005, evaluated the executive branch financial disclosure requirements. The second, which OGE will compile in consultation with the Department of Justice, is due in fiscal year 2006 and will examine the criminal conflict of interest laws as they pertain to the executive branch. OGE will work with the Office of Management and Budget and the Congress on any Congressional efforts to consider and implement any needed changes identified by these two reports, including possible hearings and legislation. In addition, OGE will take the necessary steps to revise its financial disclosure forms and regulations to implement any changes in existing law.

OGE expects to purchase some new hardware and software, including security software to protect our network and keep it 100 percent FISMA compliant, software necessary to keep our network up to date, and hardware to replace computers that fail. We will also obtain contract support as necessary for making OGE documents accessible in compliance with Section 508 of the Rehabilitation Act, particularly if major publications require revision following any changes in executive branch financial disclosure requirements. OGE takes its responsibilities under the Rehabilitation Act seriously and makes every effort to ensure that its web site is fully compliant with section 508 accessibility requirements.

As part of its ongoing education and training efforts, OGE will prepare and conduct ethics training for agency ethics officials. To reach ethics officials outside the Washington area, OGE plans to offer three regional symposia. In addition, OGE will plan the 16th National Government Ethics Conference for approximately 700 ethics practitioners. These events provide an introduction to the ethics rules and laws for new agency officials and advanced updates and refresher sessions for those who are more experienced. Attendees will include ethics practitioners, trainers, counselors, financial disclosure reviewers, and enforcement officials.

OGE will continue to provide international technical assistance at the request of the Departments of State and Justice. The United States is being evaluated under two separate international anti-corruption instruments. One of these, the Council of Europe's Group of States Against Corruption (GRECO), will conduct its on-site review of the United States in fiscal year 2006. The Office of Government Ethics has been a lead agency with the Department of Justice in responding to the questionnaire associated with this evaluation; in fiscal year 2006, we will be heavily involved in reviewing the draft report, and will be a member of the U.S. delegation in the GRECO evaluation when the report reaches the plenary stage for this process. OGE will also be a key participant in the meetings with the GRECO on-site review teams, and will help coordinate the necessary meetings in Washington and at the State and local level during the review.

OGE desk officers will maintain their day-to-day communications with agencies assigned to them. This continuing liaison between OGE and agency ethics staffs enables OGE to respond to the needs of the agencies in a timely and accurate manner. In addition, this interaction provides OGE with an early warning that an agency ethics program is deficient or has problems that require specialized attention. We also plan to conduct on-site ethics program evaluations in 35 Federal agencies, regional offices and military commands.

As we noted earlier, OGE's request for fiscal year 2006 is at the same level as the fiscal year 2005 appropriated amount. In fiscal year 2004, resources freed up by vacant positions and other savings allowed OGE to conduct employee surveys regarding individual agency ethics programs. The information gathered through these surveys provided OGE with a better basis on which to judge the effectiveness of the individual agency programs under review and of the overall ethics program. We hope to be able to conduct additional employee surveys in fiscal year 2005 and fiscal year 2006.

The programs and activities we have described are just some of those envisioned for fiscal year 2006. We are pleased with the past success of the executive branch ethics program and look forward to the challenge of maintaining and enhancing the quality of the program.

FEDERAL MARITIME COMMISSION

PREPARED STATEMENT OF HONORABLE STEVEN R. BLUST, CHAIRMAN

Mr. Chairman and members of the subcommittee, thank you for this opportunity to present the President's fiscal year 2006 budget for the Federal Maritime Commission.

The President's budget for the Commission provides for $20,499,000 for fiscal year 2006. This represents an increase of 6 percent, or $1,158,968, over our fiscal year 2005 appropriation. This budget provides for 133 workyears of employment, a straight-line of the 2005 level.

Our fiscal year 2006 budget request contains $15,218,000 for salaries and benefits to support the Commission's programs. This is an increase of $874,968 over our fiscal year 2005 appropriation, i.e., approximately 76 percent of the total increase. This includes all salaries, including those for employees hired in fiscal year 2005, and 2006 promotions, within-grade increases, and an anticipated 2.4 percent cost of living adjustment. The funding also includes annualization of the fiscal year 2005 increases. As mentioned earlier, our fiscal year 2006 budget does not contain funding for any additional positions; it only will fund the number of positions anticipated to be on board at the beginning of the fiscal year. We believe the agency can provide the same high quality of service to its stakeholders during an era of increasing outreach and compliance activity without increasing its staff; we are doing this by refocusing staff efforts as the result of our recent agency realignment, and by a staff commitment to exploring means of working "faster, better, cheaper."

Official travel has been straight-lined at $180,000, our fiscal year 2005 level. Travel remains an essential aspect of our effort to provide better service to the ocean transportation industry and to accomplish our oversight duties more effectively. We are committed to working within our straight-lined travel funding to ensure that our expanded outreach and compliance programs are fully supported, in addition to providing appropriate travel funds to support all other program efforts.

Lastly, administrative expenses have increased $284,000 over fiscal year 2005, to $5,101,000. The Commission is planning for an increase of $160,000 to accommodate GSA rental rate increases, as well as an increase of $55,000 for maintaining government and commercial contracts, primarily to fund Homeland Security charges. Other administrative expense increases of $99,000 will be incurred in fiscal year 2006 to support increases in our customary business expenses, such as telephones, postage, and supplies, as well as to pay for the lease-to-own of agency computers. These increases are partially offset by a reduction of $30,000 for furniture and equipment.

As we have noted in prior years, the Commission's budget contains primarily nondiscretionary spending. It is composed of mandatory or essential expenses such as salaries and benefits, rent and guard services, health services, accounting services, telephone and other communication costs, supplies, mandatory training, and printing and copying costs. These items represent the basic expenses any organization faces in order to conduct its day-to-day operations, and are crucial to allow us to meet the responsibilities Congress has entrusted to the agency. This budget request therefore represents a modest increase over the current year appropriation, primarily to address anticipated cost increases over current year expenses.

As you know Mr. Chairman, the Commission is responsible for the regulation of oceanborne transportation in the foreign commerce of the United States. Since 1916, the Commission and its predecessor agencies have effectively administered Congress' directives for the ocean transportation industry, and its long-standing expertise and experience have been recognized by Congress, as well as by the industry the Commission oversees, courts, and other Nations. Working with the industry, we have developed a regulatory system that allows for necessary oversight with minimal disruption to the efficient flow of U.S. imports and exports. I would like to highlight for you some of the significant activities in which the Commission is involved.

I am pleased to advise you that as of January 19 of this year, non-vessel-operating common carriers ("NVOCCs") are now permitted to enter into confidential arrangements with their shipper customers detailing the terms and conditions of their international ocean transportation. As you know, the Shipping Act permits ocean common carriers, or vessel-operating common carriers ("VOCCs"), to enter into service contracts with one or more of their shipper customers, and the Ocean Shipping Reform Act ("OSRA") provides that these contracts be filed confidentially with the Commission. While NVOCCs may enter into service contracts as shippers with ocean carriers, the Act does not grant NVOCCs the right to offer service contracts in their capacity as carriers to their shipper customers.

As you might recall, the Commission had received eight petitions, seven from individual NVOCCs and one from the National Customs Brokers and Forwarders Association of America, a national trade association representing NVOCCs, seeking various types of relief from this disparate treatment. These petitions generated hundreds of comments from the industry as well as Members of Congress. Subsequently, several of the petitioners, along with the Transportation Intermediaries Association and the National Industrial Transportation League, filed a joint proposal with the Commission suggesting a unified approach to this issue. After assessing that proposal, the Commission issued a proposed rule to grant the relief the industry was seeking within the parameters of the Shipping Act.

In order to grant an exemption from the requirements of the Shipping Act, the Commission must find that it will not result in a substantial reduction in competition or be detrimental to commerce. Based on these criteria, the proposed rule set forth a conditional exemption from the tariff publication requirements of sections 8 and 10 of the Shipping Act. The Commission made minor modifications to its proposal based on comments received from the industry, and I am pleased to report that a final rule is now in effect. NVOCCs otherwise in compliance with the licensing, financial responsibility, and tariff publication requirements of the Shipping Act may now enter into confidential NVOCC Service Arrangements ("NSAs") with their shipper customers in lieu of publishing those rates in a publicly-available tariff, provided that the NSA is filed confidentially with the Commission and the essential terms are published in the NVOCC's tariff. This new regulatory scheme is consistent with the regulations governing service contracts between ocean common carriers and their shipper customers, and we anticipate that it will result in greater competition in the shipping industry.

To ensure that NSAs are consistent with the statutory scheme established by Congress in the Shipping Act, the regulations proscribe certain types of discriminatory conduct similar to the prohibitions applicable to service contracts in section 10 of the Shipping Act. In addition, the rule does not permit unrelated NVOCCs jointly to offer NSAs, nor does it allow NVOCCs or shippers associations with NVOCC members to participate in NSAs as shippers. We are certainly mindful of industry concerns over these limitations. However, we believe they are necessary as a result of recent judicial interpretations which construe the antitrust provisions of the Shipping Act in a manner we believe to be much broader than what was envisioned by Congress, this Commission, and indeed even the industry. As we indicated when we issued the final rule, we will monitor the judicial developments and continue to work with the industry to address this issue as circumstances warrant.

Also in January, the Commission implemented new regulations governing agreements among ocean common carriers and marine terminal operators. The new rules reduce the burden and cost of complying with the agreement filing requirements of the Shipping Act while ensuring that the Commission receives the information necessary for effective oversight. The rules provide the shipping industry with enhanced certainty as to FMC requirements, continued flexibility in commercial relationships, and sufficient confidentiality for sensitive commercial information. The provisions governing modifications and exemptions have been clarified, and include a new exemption for low market share agreements among ocean common carriers that do not contain pricing or capacity rationalization authority. Further, the information, monitoring report and minutes reporting requirements have been reformulated, reducing the overall burden of complying with the Commission's rules. We continue our vigilant review of carriers' utilization of their antitrust immunity to ensure that their collective activities do not result in market-distorting practices, and the new regulations will further our efforts in this area, while permitting agreement parties the flexibility they need for successful commercial relationships.

The Commission continues to address restrictive or unfair foreign shipping practices under section 19 of the Merchant Marine Act, 1920 ("Section 19"); the Foreign Shipping Practices Act of 1988 ("FSPA"); and the Controlled Carrier Act of 1978. Section 19 empowers the Commission to make rules and regulations to address conditions unfavorable to shipping in our foreign trades; FSPA allows the Commission to address adverse conditions affecting U.S. carriers in our foreign trades that do not exist for foreign carriers in the United States. Under the Controlled Carrier Act, the Commission can review the rates and rules of government-controlled carriers to ensure that they are not unjust or unreasonable.

With respect to the People's Republic of China, recently there have been several pending proceedings related to shipping conditions in China. In particular, the Commission was investigating whether Chinese laws and regulations might discriminate against and disadvantage U.S. vessel operators and NVOCCs with regard to a variety of maritime-related services. In December of 2003, the United States, through the Secretary of Transportation, and his Chinese counterpart, the Minister of Communications, signed a bilateral maritime agreement which appeared to address many of the concerns raised by the Commission, including issues affecting vessel operators, NVOCCs, and other industry interests. That agreement became effective with the exchange of diplomatic notes in April of 2004.

Subsequently, the Commission requested comment from the industry on whether the commitments made in the bilateral agreement, which would have relieved the impediments to U.S. companies identified by the FMC, were being honored. We received positive feedback from the U.S. industry in this regard. I am pleased to report to you that many of the issues we raised have been adequately addressed. In particular, 29 U.S. NVOCCs have availed themselves of the opportunity provided for in the Commission's rules to file proof of additional financial responsibility with the Commission as an alternative to meeting China's requirements for the deposit of at least $96,000 in a Chinese bank.

As a result of diplomatic efforts which positively addressed numerous matters of concern, the Commission recently terminated its proceeding which investigated shipping restrictions, requirements and practices of the People's Republic of China. I am encouraged that the Commission's traditional practice of allowing for a diplomatic resolution to the issues we have raised in the foreign trades has again been fruitful. Although the Commission is optimistic that recent developments will yield positive effects for vessel operators, intermediaries and the U.S. shipping public, we will take seriously our statutory duty to respond to any future allegations of unreasonably restrictive practices with respect to this, or any other, U.S.-foreign trade.

The Commission continues to promote its public outreach initiative involving a series of informational seminars hosted by the Commission's Area Representatives and other Commission personnel at various locations around the country. These seminars have been successful in creating a forum for continued and enhanced dialogue between the industry and the Commission. I am pleased to report that we have started a new program where we have invited representatives from various segments of the industry to brief our staff on current issues and concerns affecting U.S. international liner shipping. Thus far, we have met with representatives from the ocean transportation intermediary, vessel operator, port authority, and shipper communities, and we are planning additional briefings later in the year with marine terminal operators, passenger vessel operators, and other segments of the maritime industry. I am confident that these briefings will provide the Commission and its staff with a greater awareness and understanding of the most current issues facing the maritime community.

Likewise, the agency's new organizational structure has proven beneficial. As I reported to you last August, the Commission refined the agency's organizational structure to reallocate existing resources to maximize the effectiveness of the staff and facilitate agency efforts to better serve the ocean transportation industry. This was the result of a several-month effort to review the Commission's work processes and practices in light of changes in the industry. To better carry out the Commission's compliance and outreach initiatives, our Area Representatives, previously assigned to the Bureau of Enforcement, now report to the Director of Operations. In addition, to more effectively address the rapid growth of the Commission's consumer complaints program, that program and the alternative dispute resolution function were combined into a new Office of Consumer Affairs and Dispute Resolution Services. Through this office, we are able to provide a mechanism for parties involved in ocean transportation to settle their disputes without the need for costly and time-consuming litigation. The Commission's consumer affairs staff is able to assist in the resolution of informal disputes and formal proceedings involving cruises and the shipment of cargo. Additionally, the Office of Administration now has oversight over the four administrative offices: the Office of Budget and Financial Management; the Office of Human Resources; the Office of Information Technology; and the Office of Management Services. I am pleased to report that these modifications have resulted in greater communication and effectiveness between the Commission and the shipping public. Our new structure not only provides an effective regulatory structure suitable for today's shipping industry, it also allows us the flexibility necessary to grow and change as the industry continues to evolve.

Lastly, the Commission recognizes that its oversight of ocean common carriers, ocean transportation intermediaries, including ocean freight forwarders and non-vessel-operating common carriers, and marine terminal operators, is an important element in the effort to protect our Nation's seaports. We are continuing our efforts to combat unlawful participation in the U.S. ocean transportation system by ensuring that all entities engaged in the U.S. foreign commerce are in compliance with the requirements of the Shipping Act. In addition, we submitted a report to Congress in November of 2004 detailing our cooperation with other agencies involved in maritime transportation, including the Department of Homeland Security, Department of Transportation and intelligence agencies, regarding information-sharing and other possible FMC contributions to the efforts to ensure a safe and efficient maritime transportation system.

Mr. Chairman, I hope that my comments have served to give you a clear indication of the important work to be accomplished by the Federal Maritime Commission. I respectfully request favorable consideration of the President's budget for the Commission so that we may continue to perform our vital statutory functions in fiscal year 2006.

NONDEPARTMENTAL WITNESSES

[CLERK'S NOTE.—The following testimonies were received by the Subcommittee on Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies for inclusion in the record. The submitted materials relate to the fiscal year 2006 budget request.

The subcommittee requested that public witnesses provide written testimony because, given the Senate schedule and the number of subcommittee hearings with Department witnesses, there was not enough time to schedule hearings for nondepartmental witnesses.]

PREPARED STATEMENT OF THE UNIVERSITY OF OKLAHOMA

LOCAL AREA AUGMENTATION SYSTEM (LAAS)

Thank you for the opportunity to submit this testimony for The University of Oklahoma (OU) Navigation Solutions Institute (NSI), in support of the appropriations request for the Local Area Augmentation System (LAAS). This testimony will identify the motivating national interest and describe the NSI approach to serve those needs. We respectfully request $2.5 million in the pending fiscal year 2006 appropriations legislation for NSI to provide the engineering and technical expertise required to advance the certification effort of the LAAS, including anti-jamming mitigation. The proposed work will be performed by OU-Norman NSI, in collaboration with the OU-Tulsa electro-magnetic compatibility (EMC) facility and OU-Norman Department of Aviation flight operations.

STATEMENT OF NATIONAL INTEREST

Travelers are opting to fly rather than drive once again and National Air Space (NAS) capacity issues are imminent. The growth of air traffic has returned to pre-9/11 levels and the competition among airlines for limited network capacity, at a time of rapidly rising fuel prices, potentially jeopardizes the quality, safety, security, industry economic health, and international competitiveness of U.S. commercial and general aviation service. Coordination of local flight (take-off and landing) operations with ground (taxi and terminal) operations is a critical constraint on local area terminal capacity. The existing Instrument Landing System (ILS) is not capable of dealing with these capacity issues. Solutions cannot wait decades into the future, but are needed immediately; and Local Area Augmentation System (LAAS) technology can become available in the near term with the requested appropriation to perform the rigorous certification required by FAA standards. Issues to be addressed include hardware reliability and fault tolerance, software traceability, anti-spoof mitigation, and position solution integrity. This critical navigational aid is highly sought after by commercial and general aviation.

According to an Airports International Council report in 2000, the United States has over 5,300 airports open to public use. There are 1,364 Instrument Landing Systems (ILS) in place. The report also cites the expected increases in commercial and general aviation traffic, which will have a positive economic impact in the United States. The Joint Planning and Development Office (JPDO) forecasts three-fold increases in passenger and freight traffic by 2025 as a reference point for planning of the Next Generation Air Transportation System (NGATS). Concomitant with this growth, maintenance, modernization, and air traffic congestion are becoming issues of national priority to ensure safe, efficient, and effective air travel. A significant maintenance and modernization cost is related to precision landing systems for airports. Furthermore, accurately guided approaches and departures allow for a more efficient use of crowded airspace. GPS-based navigation systems in non-critical areas have proven to be cost-effective. However, augmentation systems are needed in order to ensure the quality of service (in terms of accuracy, continuity, and integrity) required by the aviation community. LAAS has the potential to provide a paradigm shift in air traffic management in the United States. Furthermore, there is significant interest in the international community where cost-effective solutions are of paramount importance. Finally, LAAS is capable of being deployed on a portable basis without significant infrastructure requirements, thus providing precision landing services in disaster recovery efforts or military theaters of operations, in a timely manner.

The Wide Area Augmentation System (WAAS), is not able to provide the continuity and integrity needed for CAT I precision landing services at increasingly heavy traffic levels. LAAS has been shown to provide the accuracy needed for precision CAT I, II, and III landings, but needs additional development to achieve the required continuity and integrity. The LAAS system will provide the needed international connectivity between our applications and growing international needs, which the airline community wants to provide to strengthen their operations status. The certification phase will require the requested funds and continued close association among the OU-Norman Navigation Solutions Institute, OU-Tulsa EMC Facility, OU-Norman School of Aviation, the FAA, and partner air carriers.

NSI MISSION AND APPROACH

The OU Navigation Solutions Institute has already developed a LAAS prototype. LAAS is a ground-based augmentation system for GPS and provides mitigation for both precision landing and airspace use. The cost of implementing a LAAS system is expected to be similar to the cost of implementing an ILS. LAAS provides a precision landing capability to large and small airports. For example, the deployment of a LAAS system at Chicago O'Hare airport would alleviate many weather traffic delays in the NAS. An ILS is only capable of providing a precision approach for one runway end, while a single LAAS installation can provide precision approaches for any runway end in the service area. Furthermore, NSI has shown that LAAS can provide guided, curved departures, guided missed approaches, and curved-path approaches for any runway end in the service area. On-going work at NSI has focused on hardware redundancy, reliability, and integrity flight testing. The requested funds will be used to move the current LAAS design through certification by the FAA. This requires hardware re-design of the system to meet fault-tolerance objectives; updated software development to meet DO–178B requirements for reliability and traceability; the design of far-field monitor stations to provide anti-spoofing capabilities and to monitor the integrity of the LAAS position solution; and assessment of the robustness of wireless communication between the LAAS station elements as a means of minimizing the impact on airport infrastructure.

NSI also has developed a long-term relationship with FAA AFS–440 and has conducted several studies related to air traffic management and navigation. The following projects illustrate the engineering expertise that NSI provides:

Collision Risk Model.—NSI has developed a stereoscopic optical tracking system for the passive detection of the position of an airplane during the final approach segment (FAS) of an ILS landing procedure in IFR conditions. This system was developed in support of the initiative to extend the Airport Operations Area Collision Risk Model (CRM) beyond the decision height (DH). Currently, no flight track data exists to support the CRM from DH to touchdown. A low-cost, efficient system was developed quickly for deployment to eight major high-traffic ILS approaches around the country. The system has been deployed at Will Rogers World Airport in Oklahoma City as a test bed site and the first active CRM visual tracking system has been deployed at Atlanta Hartsfield International Airport.

RNAV Performance Data for DME-DME and C129 GPS.—The FAA has contracted NSI to develop a test methodology and test set to evaluate the performance of DME-DME navigation which relies on older technology, ground-based navigational aids. NSI has developed a DME test set capable of monitoring a DME-DME position solution, while also monitoring a GPS-truth position solution. GPS truth is accomplished by differential GPS from a known geodetic location. This study will ultimately deliver statistical analyses providing information needed by the FAA for developing area boundaries for DME-based navigation.

TERPS Standards Testing.—NSI worked under the direction of the FAA's Procedures and Flight Standards group to analyze the performance capabilities of LAAS related to Terminal Area operations. During this study, NSI developed its prototype LAAS installation and demonstrated the ability to provide highly accurate, complex approaches and departures that exceed the performance metric specified for ILS approaches.

LAAS Certifiable System Development.—The current appropriations request would provide NSI with the means to develop the prototype LAAS system to the rigorous certification level required by today's FAA standards. Issues to be addressed include hardware reliability and fault tolerance, software traceability, anti-spoof mitigation, and position solution integrity. This critical navigational aid is highly sought by both commercial and general aviation.

NSI has a close working relationship with FAA branches from the Mike Monroney Aeronautics Center to provide unique aviation-oriented engineering design and analysis services. NSI attracts high-quality graduate students who are identified as undergraduates and actively recruited into the program. Particular emphasis is given to students who have an aviation background and are able to gain a broader understanding of the implications of design decisions.

PREPARED STATEMENT OF THE NATIONAL TREASURY EMPLOYEES UNION

NTEU represents 150,000 Federal employees in 30 Federal agencies and departments, including the men and women who work at the Internal Revenue Service. I appreciate the opportunity to provide the subcommittee with comments on the IRS budget for fiscal year 2006.

There are several items in the administration's IRS budget that NTEU believes would be detrimental to the IRS's mission. The two most egregious items include the administration's plans to contract out tax collection to private collection agencies starting this summer, and an inadequate budget request that will prevent the IRS from continuing to improve its customer service record while bolstering enforcement efforts.

BUDGET

The President's fiscal year 2006 IRS budget proposal is woefully inadequate to provide the resources necessary to meet its enforcement goals to reduce the outstanding U.S. tax gap. I commend the administration for acknowledging in its Budget in Brief that the "IRS yields more than four dollars in direct revenue from its enforcement efforts for every dollar invested in its total budget." But I must criticize the administration for failing to request a budget that would enable the IRS to meet the enforcement challenges it faces with its $350 billion annual tax gap.

The IRS brought in $5.5 billion more in fiscal year 2004 than it did in fiscal year 2003 through enforcement efforts. This represents a 15 percent increase. It makes good business sense to fund the Agency at an amount where it can continue to see a similar return on investment. Unfortunately, the President's budget does not make good business sense.

The IRS needs a budget that anticipates required expenses such as congressionally imposed pay raises and rent increases. Part of the President's IRS budget request for enforcement will be used to cover inflationary costs. Of the $446 million proposed for new enforcement investments, $182 million will be needed just to keep enforcement at its current levels.

Furthermore, the way in which the administration proposes to enhance the enforcement budget will mean cuts to other parts of the IRS budget—such as taxpayer assistance. The President's budget calls for a cut of 1,385 service personnel—87 percent of whom directly assist taxpayers and tax professionals. The IRS has taken great strides to improve taxpayer service over the past few years and has been quite successful in making significant progress. The Service must not let the pendulum swing in the other direction and neglect service so that it can focus on enforcement. Service and enforcement must go hand in hand toward increasing taxpayer compliance and shrinking the tax gap.

NTEU strongly supports the IRS Oversight Board's proposed budget recommendation of $11.6 billion for fiscal year 2006—a 9 percent increase over the President's budget recommendation and a 13 percent increase over the fiscal year 2005 appropriation. I urge the subcommittee to also support the Board's recommendation.

PRIVATE TAX COLLECTION

NTEU strongly opposes the administration's plan to privatize IRS debt collection, as authorized by Congress last year in H.R. 4520, American Jobs Creation Act of 2004. Under the statute, the IRS would be permitted to hire private sector debt collectors and pay them a bounty of up to 25 percent of the money they collect. Let me be clear: NTEU opposes this short-sighted proposal, anticipates its complete failure as witnessed in a similar 1996 pilot program and will work towards its repeal.

This proposal would risk the loss of confidentiality of millions of taxpayers' private information, would subject taxpayers to the abusive tactics of private debt collectors, and would cost U.S. citizens much more money than if IRS employees did the job.

One of the most often heard arguments in favor of the use of private collection agencies is that if they are paid out of the proceeds of what they collect, it increases the IRS's enforcement capabilities without having to increase appropriations. Numerous congressional supporters said they would prefer to have tax collection done by Federal employees, but would go along with the use of private collection agencies solely because it avoids the difficult issue of getting Congress to approve additional appropriations for the IRS.

The statute that gives the IRS the authority to use private collection agencies (PCAs) allows 25 percent of collected revenue to be returned to the collection companies as payment and 25 percent to be retained by the IRS for enforcement efforts, thereby circumventing the appropriations process altogether.

There is nothing magical about revenues collected by private collection companies. If those revenues could be dedicated directly to contract payments and IRS enforcement efforts, there is no reason some small portion of other revenues collected couldn't be dedicated to IRS enforcement efforts. This would allow for increased enforcement by IRS employees, which most people indicate is the preferable route and eliminate large payments (up to 25 percent of collections) to private collection companies, significantly increasing net revenue to the General Treasury. While legislation would be required to allow for this kind of dedication of revenue, I believe the precedent has now been set with the private collection agency funding provisions. Congress should consider supporting this approach as a common sense way to make real progress in closing the tax gap, lowering our deficits and making more funding available for our Nation's critical needs.

According to GAO's May 2003 testimony before the House Treasury Appropriations Subcommittee (GAO–03–732T), one major concern the IRS must address prior to implementing tax collection outsourcing is the ability to identify "delinquent debts with the highest probability of resolution through PCA contacts. Earlier pilot efforts to study the use of PCAs in 1996 and 1997 were hindered, in part, because the IRS was unable to do this . . . While IRS proposes using the 'case selection analytics' to identify appropriate cases, the analytical model has not been developed."

It appears as though the IRS has not yet addressed case selection. According to the IRS's February 15, 2005 "Filing and Payment Compliance Modernization Briefing: The Use of Private Collection Agencies," there are five major issue areas that still need to be addressed before handing work over to the PCAs. One of the issue areas is selecting the workload for PCAs (called Filing and Payment Compliance), which will be part of the Business Systems Modernization Program. Since case selection was a major obstacle for the IRS in its 1996 pilot program, the IRS should ensure that the technology is in place prior to handing over any work to the PCAs.

Furthermore, the IRS does not have the technology in place to ensure that taxpayer information is kept secure and confidential when it is handed over to the PCAs. The IRS expects to hand over taxpayer information, including Social Security number, to the private collection companies.

Recent security breaches at three data brokerage firms here in the United States should alarm every member of Congress and put into question the IRS's plans for moving forward with this privatization plan. ChoicePoint compromised the personal information of 145,000 Americans. At LexisNexis, thieves were able to access 32,000 records including Social Security numbers and driver's licenses. And Bank of America recently reported it has lost personal data—including Social Security numbers and account information—on 1.2 million Federal employees, including some members of the Senate. These are companies that are in the business of trading—and securing—personal information. If they aren't able to secure confidential consumer information, I have little faith that a private debt collection company will be able to guarantee U.S. taxpayers that their information will remain secure.

I would urge the subcommittee to work with your colleagues to repeal this ill-fated proposal. Additionally, I would urge the subcommittee to require the IRS to perform cost comparisons and closely track the contractors' costs. This is the only way that taxpayers can be certain their tax dollars are being spent wisely.

CUSTOMER SERVICE CUTS

The President's budget proposes to cut $134,103,000 and 1,205 positions from customer service, with Taxpayer Assistance Centers (TACs) targeted for drastic reductions. IRS Taxpayer Assistance Centers are taxpayers' source for personal, face-to-face tax help. Taxpayers who have complex issues, need to resolve a tax problem, or are more comfortable talking with someone in person can visit a local Taxpayer Assistance Center. IRS representatives in these offices can help with inquiries or adjustments to tax accounts, payment plans for those who owe tax and cannot pay the full amount, questions about IRS letters and notices, and levies on wages or bank accounts.

These cuts will mean that minorities and low-income taxpayers, who rely on the Centers to help with language barriers, the earned-income tax credit and general tax preparation, will see the tax services they rely on cut. As Janet Spragens, law professor and director of American University College of Law's Federal Tax Clinic, notes in her testimony before the IRS Oversight Board (February 1, 2005):

" . . . these taxpayers, many of whom have limited or no proficiency in English, are generally not part of the information age. They are not Internet connected . . . They tend to be helped better through local walk-in offices and opportunities for face-to-face meetings than with an organizational structure based on specialization of function, remote offices, mailed documents, telephone trees with automated selections and electronic transfers."

Even the IRS Oversight Board raises concerns of the IRS's plan to eliminate additional customer service personnel. In its fiscal year 2006 IRS Budget Special Report (March 2005), the Board states its concerns:

"Increasing enforcement resources at the expense of service resources is a trend that can lead to a system that fails to meet the needs of all honest taxpayers."

The IRS claims that taxpayers will continue to have access to tax forms and information through on-line access, telephone assistance and volunteer tax preparation. Unfortunately, many taxpayers who use the walk-in centers have little or no proficiency in English and are not part of the electronic information age. Tax forms on the Internet and phone trees do them little to no good. They rely on face-to-face contact with their local Taxpayer Assistance Centers to help them comply with various complexities of the tax code.

While the agency has not yet provided specific information either to NTEU or to affected employees, it is my understanding that the agency is reviewing options that include closing either 105 TACs, affecting 528 employees, or 67 TACs, affecting 516 employees. Either way, the plan is a significant step backward in the ability of the IRS to do its job effectively.

The IRS has suggested that private tax assistance programs using volunteers can fill the void that will be created by the cutbacks. While volunteer taxpayer assistance organizations play an extremely helpful role in assisting taxpayers to meet their tax obligations, it is foolhardy for the agency to rely on volunteers to do work that should be performed by trained and accountable Federal employees. Volunteers claim there's already a shortage of computers and other resources to help every taxpayer who seeks assistance, and that situation will only worsen if the IRS follows through with its proposed cuts to customer service.

Furthermore, as the IRS is cutting back walk-in customer service operations, it is also planning to close six of its call sites in Boston, Houston, Chicago Des Moines, Wichita, and Omaha. Especially hard hit will be the Boston, Houston and Chicago facilities where nearly 200 employees could be affected. These are facilities where the employees receive taxpayers' inquiries and respond to their tax questions.

Congress must commit to funding the IRS at adequate levels so the IRS is not made to choose between bolstering enforcement and providing the superior service our taxpayers expect and deserve.

PAY PARITY

While the President proposed a 3.1 percent pay raise for members of the uniformed military in 2006, he has only recommended a 2.3 percent pay raise for the Federal workforce. NTEU supports the higher pay raise for all Federal employees. This budget fails to recognize the important role Federal workers play in protecting our homeland and providing services to America. In recognition of the fact that these two groups of public employees more often than not work side by side in support of our country, Congress has approved equal pay adjustments for military and civilian employees in 17 of the last 19 years. NTEU urges Congress to approve equal pay adjustments again for 2006.

Pay parity has broad bipartisan support in the House and Senate and Senator Susan Collins (R-ME) and Representative Tom Davis (R-VA), the Chairmen of the Senate Homeland Security and Governmental Affairs and House Government Reform Committees, respectively, strongly support continuing pay parity in 2006. Last year the House voted in favor of pay parity by a 299–126 vote. In addition, both Senate Chairman Collins and House Chairman Davis have added their names as cosponsors of resolutions supporting pay parity. I commend those members of Congress who voted for the pay parity resolution and urge the appropriators to fund civilian pay on par with military pay at a 3.1 percent increase for fiscal year 2006.

CONTRACTING OUT

Despite provisions in last year's House and Senate fiscal year 2005 Treasury-Transportation Appropriations bills that would have prohibited OMB from using its revised May 29, 2003 A–76 Circular as the guideline for competitive sourcing, the administration insisted that this provision be stripped from the final bill. The administration is more determined than ever to proceed with public-private competitions using the revised OMB Circular which gives a clear advantage to the private sector.

Before contracting out any more government work to the private sector, the playing field for public-private competitions must be leveled. There are several areas where Congress should require OMB to make changes to the A–76 Circular in order to establish a fair outsourcing process.

First, the A–76 Circular must allow Federal employees to offer their best bid with a most efficient organization (MEO). Under the revised A–76 process, a "streamlined" competition allows the agency to avoid organizing an MEO and just take a "snapshot" of the current work being performed and the costs associated with it.

Second, a minimum cost savings of 10 percent or $10 million must be required of the contractor in order for the work to be contracted out. There is no requirement under current statute or under the revised A–76 Circular which requires the contractor to provide a savings at least equal to the amount it costs to run a competition. Congress ought to require the contractor to save the agency at least enough so that the competition is paid for and taxpayers aren't cheated.

Third, the process should prohibit the contractor from receiving a cost advantage in the competition by offering an inferior employer-sponsored health benefit than the Federal employees receive. Contractors have an incentive to cut benefits to their workers in order to reduce labor costs when offering their best bid. However, contracting out should not be a race to the bottom. If contractors want to offer inferior benefits to their workers, they should not be rewarded for this by being given an advantage in the competition for the work.

Fourth, Congress must also make sure that Federal employees are treated fairly throughout the competition process by sharing the same legal standing before GAO for appeals purposes as has long been enjoyed by contractors.

This list is by no means exhaustive but it's a good starting point. If the administration is going to insist on using its flawed revised A–76 Circular, then Congress must insist on correcting those flaws in the competitive sourcing rules.

CONCLUSION

On behalf of the dedicated Federal employees NTEU represents, I am proud to submit these views for the hearing record. I encourage the committee to make a strong investment in the Federal workforce by appropriating the 9 percent increase as requested by the IRS Oversight Board; repealing the IRS's authority to privatize tax collection; prohibiting the IRS from closing up to one-quarter of its Taxpayer Assistance Centers; providing pay parity for Federal workers; and giving the Federal workers a level playing field when competing for their jobs with private contractors.

Without a doubt, the frontline employees are committed to working with management and Congress to increase efficiency and customer satisfaction. NTEU is committed to striking a balance between taxpayer satisfaction, business results and employee satisfaction. I encourage Congress to join us in this commitment.

PREPARED STATEMENT OF THE CAPITAL METROPOLITAN TRANSPORTATION AUTHORITY

Mr. Chairman and members of the subcommittee, on behalf of the Capital Metropolitan Transportation Authority in Austin, Texas, I am pleased to submit this statement for the record in support of our fiscal year 2006 funding requests from the Federal Transit Authority for Capital Metro—the transportation provider for Central Texas. I hope you will agree that the appropriation of funds for these Central Texas projects warrants serious consideration as Austin and the surrounding Texas communities plan for our region's growing transportation needs.

Capital Metro requests funding for four critical projects that we hope the subcommittee will include in its fiscal year 2006 appropriation bill: (1) $15 million for an Urban Commuter Rail Line; (2) $4.5 million for a Rapid Bus Project; (3) $1.5 million for a North Operating Facility; and (4) $4.2 million for improvements in and expansions of our bus service and facilities.

Before describing each project in some detail, let me first thank you for your past financial support for transportation projects in Central Texas. Your support has proven valuable to Capital Metro and to our Central Texas community as we face new challenges.

As you know, Interstate 35 runs from Canada to Mexico, and along the way it also runs through the City of Austin and Capital Metro's 600-square-mile service area. While traffic in this important corridor has always been a challenge, the North American Free Trade Agreement has resulted in increased traffic and congestion for our region. In fact, a 2002 study by the Texas Transportation Institute determined Austin, Texas to be the 16th most-congested city nationwide.

Also, Central Texas' air quality has reached near non-attainment levels. Together, our community has developed a Clean AirForce, of which Capital Metro is a partner, to implement cooperative strategies and programs for improving our air quality. Capital Metro has also unilaterally implemented several initiatives such as offering free rides on ozone action days for the last 13 years, converting its fleet to clean-burning Ultra Low Sulfur Diesel (ULSD), becoming the first transportation authority in Texas to introduce environmentally-friendly hybrid-electric buses, and creating a GREENRide program to carpool Central Texas workers in low emission hybrid gas/electric automobiles.

To address these transportation and air quality challenges as well as our region's growing population, in 2004 Capital Metro conducted an extensive community outreach program to develop the All Systems Go Long-Range Transit Plan. This 25-year transportation plan for Central Texas was created by Capital Metro, transportation planners, and local citizens. More than 8,000 citizens participated in the design of the program that will bring commuter rail and rapid bus technologies to Central Texas. The plan will also double Capital Metro's bus services over the next 25 years.

By a vote of over 62 percent, this long-range transportation plan was adopted by the Central Texas community in a public referendum on November 2, 2004. The plan received bipartisan support, along with endorsements from the business community, environmental organizations, neighborhood associations, and our community leaders.

An important component of the All Systems Go Long Range Transit Plan is the creation of an urban commuter rail line along a 32-mile-long freight rail line currently owned and operated by Capital Metro. The proposed starter route would provide urban commuter rail service extending from downtown Austin (near the Convention Center) through East and Northwest Austin and on to Leander. Capital Metro is seeking $15 million for this project.

The All Systems Go Long-Range Transit Plan also relies heavily on new rapid bus technologies. The plan creates several new rapid bus routes throughout the Central Texas region. The Rapid Bus Project is designed to provide faster, frequent and dependable service in main bus corridors with high ridership while avoiding large fixed costs and long lead times. Capital Metro is seeking $4.5 million for the Rapid Bus Project.

Additionally, Capital Metro will complete work this year on the North Operating Facility. This facility will serve as a maintenance and housing facility for the vehicles serving Capital Metro's many Northern routes and the University of Texas shuttle services. Capital Metro's Special Transit Services operations will also be located at this facility. Work began in Spring 2004 on the North Operating Facility. This project is in the final stages of construction and will be complete in Fall 2005. Capital Metro is seeking $1.5 million for this project.

Capital Metro has embarked on a long term plan to improve and expand bus service. In addition to improving bus routes, the agency is investing in critical park and ride facilities, transit centers and enhanced bus stop locations and amenities. New planned facilities include the North IH–35 Park and Ride, the South Central Transit Center, the Leander Park and Ride, and a new administrative facility in East Austin. Also, in response to increasing air quality concerns, Capital Metro will be engine-retrofitting its fleet to help improve air quality in Central Texas (a grant from the Texas Emission Reduction Plan will provide 20 percent of the local funds for this project). Capital Metro seeks $4.2 million for these improvements and expansions of our bus service and facilities.

On behalf of Capital Metro, I am grateful for your consideration of our requests for funding in the fiscal year 2006 cycle. I look forward to working with each of you in order to demonstrate the necessity of these projects.

Prepared Statement of the City of San Marcos, Texas

AIRPORT IMPROVEMENTS REQUEST—SAN MARCOS MUNICIPAL AIRPORT, SAN MARCOS, TEXAS

Mr. Chairman and members of the subcommittee, on behalf of the City of San Marcos, Texas, I am pleased to submit this statement in support of our requests for project funding for fiscal year 2006.

The City of San Marcos requests Federal funding for the San Marcos Municipal Airport to accomplish improvements that are in the public interest. The improvements are described in the three specific projects listed below:

Northside T-Hangar Construction	$3,500,000
New Terminal Building	4,500,000
Fixed Base Operator (FBO) Facility	1,500,000
Total Request	9,500,000

The San Marcos Municipal Airport is a public general aviation airport owned and operated by the City of San Marcos, Texas. It is located just east of Interstate Highway 35 on Texas Highway 21 approximately 30 miles south of Austin and 45 miles north of San Antonio in one the fastest growing corridors in Texas.

The airport is part of a closed military base; the remainder of the former Air Force Base is occupied by the United States Department of Labor's Gary Job Corps Center. When the base was closed and divided in 1966, the Job Corps retained the portion of the property with the buildings and other amenities while the City of San Marcos was given the aeronautical facilities consisting of runways, taxiways, and the parking apron.

This arrangement has resulted in a "bare bones" airfield that lacks the support structure to sustain an economically viable modern airport. We have adequate aeronautical facilities and real estate but little other facilities. In addition, current legislation provides for airport capital improvement funding assistance through the Federal Aviation Administration for aviation infrastructure, but not for the type of improvements that this airport needs.

The City of San Marcos requests help to transform the airport into a modern, self-sustaining enterprise. After analysis and master planning, we have determined that the three projects herein described will get us the "biggest bang for the buck." These projects will meet our highest priorities and most immediate needs, and they will be a highly visible indicator that the San Marcos Municipal Airport is on the move. We are firmly convinced that these improvements will kick-start further development and attract private investment that will far surpass the amount that we are seeking in Federal support.

The following program descriptions outline our three requests:

Northside T-Hangar Construction—$3,500,000

The layout of the former Gary Air Force Base is such that all the buildings and developed area of the base were to the south of the airfield. When the base was divided between the Gary Job Corps Center and the San Marcos Municipal Airport, the airport was given only a thin sliver of land on the south side to provide access and support the airfield. There is not enough room for all the support facilities such as hangars, maintenance shops, and terminal buildings that an active airport requires.

However, on the north side of the airfield is real estate that has never been developed. One prime piece of the northside area consists of approximately 40 acres of very desirable airport land that fronts on Texas Highway 21 and borders a newly refurbished main airport taxiway. Except for the absence of infrastructure, it is the "McDonald's" location on the airport. The area requires an access road, drainage improvements, pavements, and utilities. It also needs a seed project to stimulate private investors to move into the area.

Our plan proposes to construct the infrastructure and to then build approximately 50 nested T-hangars in two or three city-owned buildings. Our planning estimate for the cost to implement this project is $3,500,000. We are also convinced that once this northside development ball starts to roll, the future of the new San Marcos Municipal Airport will shift from the limited and constrained south side to the several hundred acres of undeveloped land available on the north side.

New Terminal Building—$4,500,000

The commercial, economic, and public service hub of a modern airport is the public terminal building. The terminal building provides public amenities such as a waiting room or lounge, airport administration offices and public meeting rooms, restrooms, flight planning facilities and communications links to obtain flight planning information, commercial lease space for such businesses as an airport restaurant, airport shops, and other aviation-related commercial activities.

These facilities are sorely lacking in our present airport configuration. It is opportune that the Federal Aviation Administration is programming a new air traffic control tower for our airport in fiscal year 2006. A new terminal building located adjacent to the control tower could be architecturally coordinated with the control tower for aesthetic advantage. The two facilities could achieve a significant efficiency in the coordinated construction of road access, utility services, parking facilities, drainage improvements, and landscaping. This same concept is being touted at several other airports similar to ours. (Dallas Executive Airport is a prime example.) The planned terminal building planning concept is for a building of approximately 10,000 square feet first floor and total cost estimated at $4,500,000.

Fixed Base Operator (FBO) Facility—$1,500,000

For general aviation operations, airport activity centers on the FBO. This is where the transient and based pilots and aircraft operators go to buy fuel and obtain direct support for their flights. It is also a place where transient and based pilots can arrange to have their aircraft serviced, repaired, and hangared overnight or longer when required.

It is again opportune that the San Marcos Municipal Airport has an established FBO that is capable of accomplishing these vital services if a facility were available for them to lease. We propose that a modern, state-of-the-art FBO be constructed to meet the airport's present and future commercial requirements. The approximately 30,000 square foot structure would be mainly hangar space with an attached business, shop, and office area. Cost is estimated at $1,500,000. Lease payments and other airport fees would offset this investment; and the investment is calculated to be a profitable enterprise for the airport in the long term.

The 1,356 acre San Marcos Municipal Airport is a potential economic dynamo for this region of Central Texas. The three airport improvement projects that we are proposing will result in an increase in activity and private investment. This is a good investment of public revenue that will result in more high-paying aviation jobs, an increased tax base, and more direct revenues in the form of airport fees and rents. Our airport will also better serve the aviation needs of the region and spur further growth, development, and prosperity for our citizens. These projects are grounded in sound public policy principles. They will result in excellent value for the American taxpayer and for the traveling public that will utilize the facilities.

The City of San Marcos sincerely appreciates your consideration of these requests for funding in the fiscal year 2006 cycle, and respectfully requests your support.

PREPARED STATEMENT OF THE COALITION OF NORTHEASTERN GOVERNORS

As the subcommittee begins the fiscal year 2006 transportation appropriations process, the Coalition of Northeastern Governors (CONEG) is pleased to share with the subcommittee testimony on the fiscal year 2006 Transportation, Treasury, the Judiciary, and Housing and Urban Development Appropriations bill. The CONEG Governors commend the subcommittee for its past support of funding for the Nation's highway, transit, and rail systems. Although we recognize the extensive demands being made upon Federal resources in the coming year, we urge the subcommittee to continue the important Federal partnership role that is vital to strengthening the Nation's multi-modal transportation system. This system is a critical underpinning to the productivity of the Nation's economy and the security and well-being of its communities.

The Governors urge the subcommittee to fund the combined highway, public transit and safety programs at levels that will continue the progress in recent years to improve the condition and safety of the Nation's highways, bridges and transit systems. Continued and substantial investment in these infrastructure improvements—in both urban and rural areas—is necessary if the Nation's surface transportation system is to safely and efficiently move people and the substantial growth in freight movement that is projected in the coming decade. Providing robust funding of the Nation's transportation programs will allow States to continue investment that will improve the conditions and performance of the Nation's highways, bridges and public transit systems.

Within the public transit program, the Governors strongly urge the subcommittee to provide funding levels that at least maintain the basic program structure and address the solvency of the mass transit account. Further, the Governors urge the subcommittee to maintain the authorized 80/20 Federal-State match for the New Start Program. Transit programs like New Starts and the Bus and Bus Facilities Discretionary Grant Program have been instrumental in ensuring that needed funds are invested to improve and extend vital services in both our urban and rural communities.

The CONEG Governors request that the fiscal year 2006 Appropriations allow for at least $1.8 billion in funding for intercity passenger rail to ensure stability of the current system as critical decisions are made in the coming months on the future of the intercity passenger rail system and service. We understand that Amtrak has implemented management reforms, modified service, reduced personnel, and sought to increase non-Federal revenues. A capital investment program to bring essential infrastructure closer to a state of good repair will essentially exhaust the cash reserves that made it possible for Amtrak to continue operations the last few years. Yet bringing about necessary system reforms will require time for an orderly transition that does not jeopardize service and safety. As discussions on appropriate reforms in the Nation's intercity passenger rail system intensify, an appropriation of $1.8 billion for Amtrak, plus additional resources for a State-controlled corridor development, will enable continued operation and basic maintenance of a national system, and phased investment in infrastructure critical to safe and efficient operations.

The safety and security of the Nation's highways, transit and rail systems remains a priority of the Governors. The safety and security of the aging rail tunnels along the Northeast Corridor is a particular concern, and we urge the subcommittee to fund life safety improvements for the Amtrak-owned Baltimore and New York tunnels. The Governors also support maximum funding for the Section 130 Highway-Rail Crossing Program. As part of the Federal-State partnership to correct hazardous conditions on the Nation's highways, investments in highway-rail crossings can reduce injuries and death from accidents even as they allow higher train speeds and increased reliability.

The Governors urge the subcommittee to provide sufficient funding for border crossing and gateway infrastructure programs. A strong program—one that invests in transportation projects addressing both security and transportation needs—can contribute to safer, more efficient and secure flows of people and goods across international borders and through gateways.

The Governors support continued Federal investment in transportation research and development programs, particularly the Federal Railroad Administration's Next Generation High Speed Rail program. This program enhances safety and helps stimulate the development of new technologies which will benefit improved intercity rail service across the Nation. The President's fiscal year 2006 budget would zero out the Next Generation High Speed Rail Program that has funded a range of rail improvement programs such as train control systems, non-electric locomotives, grade crossings, track and structure improvements, corridor planning and maglev.

The Governors urge the subcommittee to continue funding for investments in Intelligent Transportation Systems (ITS) that can maintain and enhance the capabilities and security of the Nation's transportation system. ITS helps States and communities along the densely populated Atlantic Coast region improve the safe and reliable operations of highway and transit systems on a daily basis. The Northeast's rural areas and communities also benefit significantly from ITS investments. The region's ITS systems, including those provided by TRANSCOM and the I–95 Corridor Coalition, have demonstrated their critical role, both in the emergency management and recovery phases, when security demands put added pressure on the region's transportation networks.

The Governors also support the President's funding request of $23 million for the Surface Transportation Board. The Board is essential for oversight and effective implementation of decisions in the ongoing process of railroad consolidations and restructuring that affect local and regional economies across the Nation.

The CONEG Governors thank the entire subcommittee for the opportunity to share these priorities and appreciate your consideration of these requests.

Prepared Statement of the California Industry and Government Central California Ozone Study (CCOS) Coalition

Mr. Chairman and members of the subcommittee, on behalf of the California Industry and Government Central California Ozone Study (CCOS) Coalition, we are pleased to submit this statement for the record in support of our fiscal year 2006 funding request of $600,000 from the Department of Transportation for CCOS. These funds are necessary for the State of California to address the very significant challenges it faces to comply with new national ambient air quality standards for ozone and fine particulate matter. The study design incorporates recent technical recommendations from the National Academy of Sciences (NAS) on how to most effectively comply with Federal Clean Air Act requirements.

First, we want to thank you for your past financial support of the Central California Ozone Study (CCOS) and California Regional $PM_{10}/PM_{2.5}$ Air Quality Study (CRPAQS). Your support of these studies has been instrumental in improving the scientific understanding of the nature and cause of ozone and particulate matter air pollution in Central California and the Nation. Information gained from these two studies is forming the basis for the 8-hour ozone, $PM_{2.5}$, and regional haze State Implementation Plans (SIPs) that are due in 2007 (ozone) and 2008 (particulate matter/haze). As with California's previous SIPs, the 2007–2008 SIPs will need to be updated and refined due to the scientific complexity of our air pollution problem. This request would fund the extension of CCOS to address important questions that won't be answered with results from previously funded research projects.

To date, our understanding of air pollution and the technical basis for SIPs has largely been founded on pollutant-specific studies, like CCOS. These studies are conducted over a single season or single year and have relied on modeling and analysis of selected days with high concentrations. Future SIPs will be more complex than was anticipated when CCOS was originally designed and involve new technical challenges. The National Academy of Sciences (NAS) is now recommending a weight-of-evidence approach that will involve utilizing more broad-based, integrated methods, such as data analysis in combination with seasonal and annual photochemical modeling, to assess compliance with Federal Clean Air Act requirements. This will involve the analysis of a larger number of days and possibly an entire season. In addition, because ozone and particulate matter are formed from some of the same emissions precursors, there is a need to address both pollutants in combination, which CCOS will do.

Consistent with the new NAS recommendations, the extended CCOS study will involve the conduct of corroborative analyses with the extensive data provided by past studies, advance the state-of-science in air quality modeling, and improve our understanding of multi-pollutant, multi-year air pollution. In addition, it will facilitate continuous data collection, using an expanded monitoring network, over a 3-year period. Access to data over a multi-year timeframe will enable us to perform seasonal and annual modeling of all pollutants. It will also allow us to consider year-to-year variations in air quality. The study will incorporate further refinements to emission inventories, develop observation-based analyses with sound theoretical bases, and include the following five general components:

—Conducting weight-of-evidence data analyses, 2006–2008;
—Developing an enhanced monitoring network, 2006–2007;
—Making emission inventory improvements, 2006–2010;
—Collecting enhanced monitoring data, 2007–2009;
—Performing seasonal and annual modeling, 2008–2011.

As with CCOS and CRPAQS, Policy and Technical Committees consisting of representatives from Federal, State and local governments, as well as private industry, would direct the new study elements. Under CCOS and CRPAQS, these committees set landmark examples of collaborative environmental management. The proven methods and established teamwork provide a solid foundation for this study.

For fiscal year 2006, our Coalition is seeking funding of $600,000 from DOT through highway research funds. DOT is a key stakeholder in air quality issues because Federal law requires that transportation plans be in conformity with SIPs. Billions of dollars in Federal transportation funds are at risk if conformity is not demonstrated for new transportation plans. As a result, transportation and air agencies must be collaborative partners on SIPs and transportation plans, which are linked because motor vehicle emissions are a dominant element of SIPs in California and nationwide. Determining the emission and air quality impacts of motor vehicles is a major part of the CCOS effort. To support the region's new SIPs and to address the new NAS recommendations, a heavy-duty truck model is needed. The continued growth of heavy-duty truck travel, including increases in interstate and international goods movement, makes this element of the SIP transportation emission estimate critical. We propose funding of this activity at a level of $600,000 for 3 years.

The funding for this year's request will go into the first phase of the heavy-duty travel activity data collection. The goal will be to collect data that can be used to more accurately characterize heavy-duty truck emissions, including those resulting from NAFTA. A heavy-duty truck model is needed because on-road emissions for air quality modeling purposes are currently based on the available light-duty vehicle activity data collected by local transportation agencies. This is due to the lack of data specific to heavy-duty vehicles. This is a problem because heavy-duty trucks are known to have very different driving patterns than light duty cars and, despite smaller numbers, are responsible for a disproportionate amount of emissions (e.g. approximately 50 percent of NO_X emissions).

Thank you very much for your consideration of our request.

PREPARED STATEMENT OF THE INTERNATIONAL LORAN ASSOCIATION

FEDERAL AVIATION ADMINISTRATION

On behalf of the International Loran Association (ILA), I am submitting this outside witness testimony and respectfully request that it be added to the subcommittee hearing record in conjunction with subcommittee work on the fiscal year 2006 appropriations bill.

Specifically, the ILA is asking for your support for $25 million in funding from the Federal Aviation Administration (FAA) Facilities and Equipment (F&E) budget—the same level as we requested last year—to continue modernization of the Loran-C system. Because Loran is the only multimodal system we have that can support the global positioning satellite (GPS) system in all modes of transportation as well as timing applications affecting the majority of our population, we believe completing Loran modernization has critical national importance.

Last year, the Appropriations Committee provided $22.5 million for this recapitalization initiative and since 1997, Congress has provided approximately $140 million to modernize the Loran infrastructure in order to provide a reliable, multimodal backup to the GPS in numerous transportation applications and to help ensure the safety and security of our critical national infrastructure. This modernization has proceeded under an interagency memorandum of agreement (MOA) between the Federal Aviation Administration (FAA) and the U.S. Coast Guard (USCG), with recapitalization resources provided through the FAA budget and the $27 million annual operations and maintenance (O&M) costs funded through the USCG budget.

In recent years, we have gained greater recognition about GPS vulnerabilities that could affect the safety of tens of millions of Americans and the security of our critical national infrastructure. In combination with a modernized Loran system, GPS and Loran can together form the basis of a national infrastructure that is extremely robust and secure, now and well into our future.

Immediately before September 11, 2001, DOT's Volpe Center released a widely read and accepted report entitled "Vulnerability Assessment of the Transportation Infrastructure Relying on the Global Positioning System." That study clarified the dependence of our critical infrastructure on GPS and the national vulnerabilities associated with that dependence.

The Volpe report was followed by a July 2002 FAA report that identified Loran as the best "theoretical" backup to GPS, because Loran-C:

—"provides an independent source of navigation with the potential to meet required navigation performance (RNP) 0.3 area navigation (RNAV) requirements;
—"is not subject to the vulnerabilities of GPS;
—"provides redundant and in some cases primary capability as a source for precise timing; and
—"can provide a backup and potentially redundant ground based communication channel for the WAAS broadcast."

As a consequence of these events and our new awareness, Loran became the subject of intense scrutiny. A highly regarded team of experts conducted the most extensive technical evaluation of Loran ever performed, and "Loran's Capability to Mitigate the Impact of a GPS Outage on GPS Position, Navigation, and Time Applications" was released in December 2004. This study unequivocally demonstrated that Loran could serve to backup GPS and protect our national infrastructure in numerous critical applications, and a Loran benefit/cost study performed at the same time also contained favorable findings. In fact, Secretary Mineta confirmed the positive results of both the Loran technical evaluation and the accompanying cost-benefit analysis in letters to various members of Congress in August 2004.

Significantly, the President just authorized a new GPS policy in December 2004, and it specifically calls for the improvement and maintenance of GPS backups, and as indicated above, Loran is the only system available to support GPS in multiple critical infrastructure applications. The new "U.S. Space-Based Positioning, Navigation, and Timing Policy" affirms that GPS "is a key component of multiple sectors of U.S. critical infrastructure." Furthermore, the policy goes on to state: "The continuing growth of services based on the Global Positioning System presents opportunities, risks, and threats to U.S. national, homeland, and economic security . . . The United States must continue to improve and maintain the Global Positioning System, augmentations, and backup capabilities to meet growing national, homeland, and economic security requirements."

GPS AND LORAN

GPS and Loran are radionavigation systems that operate in virtually identical ways but have extremely different properties—properties that make them uniquely synergistic systems. GPS is a satellite-based, high frequency, and very low signal level system, while Loran is a ground-based, low frequency, and a very high signal level system. Given their distinctly different properties, GPS and Loran do not share vulnerabilities, e.g. interference that may affect one system will not affect the other. Both GPS and Loran are multimodal (i.e. they can be used for aviation, marine, terrestrial and timing applications), and they are the only multimodal systems we have. Given its multimodal and performance capabilities, Loran is the second most widely used navigation and timing system in the world. Additionally, both GPS and Loran are RNAV systems, which would make future air navigation and landing procedures consistent between GPS and Loran. This is a key capability in the aviation community's gradual transition from the current, highly structured air traffic control system to the future "Free Flight" system envisioned by the FAA.

It costs about $27 million annually to operate and maintain the entire nationwide Loran infrastructure, making Loran the least expensive navigation system available to operate and serve multiple transportation user requirements; it is also important to note that when the modernization program is complete, Loran's annual operation and maintenance expenses are projected to be less than $15 million.

NATIONAL TRANSPORTATION SAFETY AND CRITICAL INFRASTRUCTURE SECURITY

Congress and the Nation have become extremely focused on protecting the national infrastructure and safety of life, and on seeking practical, cost effective solutions to very real concerns. Through a full range of studies and reports, including those cited in this submission and several others, overwhelming evidence has accumulated about the need for systems that complement and backup GPS, and Loran is the best system for that role.

Since virtually every aspect of our national infrastructure (e.g. transportation, telecommunications, and power) relies on GPS, and because GPS is an inherently fragile system, GPS dependence is a core national vulnerability. Basically, GPS is vulnerable to intentional and unintentional interference, and neither can be completely controlled today or in the future, regardless of system augmentations/modifications or resources expended on those efforts. For example, intentional jamming was used in Iraq, as reported by The Washington Post, Reuters, and other news sources, and while such acts are recognized tactics in modern war situations, recent history tells us that such tactics could be applied in the United States.

There have also been numerous examples of unintentional jamming and interference, and these incidents exemplify how easily GPS reception can be disrupted. Our personal experiences with cell phones, AM/FM radios, wireless networks, TV reception etc. illustrate that wireless communications are not perfect, and will not become so in our lifetime. We believe it is also reasonable to assume, particularly given the huge popular migration to wireless communication technologies, that the wireless spectrum will only become even more congested in the future.

The reality is that our national transportation and related infrastructures are increasingly reliant on GPS and our infrastructure is vulnerable. The reality is also that GPS can never be made to be invulnerable, and we cannot completely control our radio frequency environment today or in the future. Loran is a very inexpensive, yet extremely capable system that can mitigate this vulnerability and provide the Nation with an infinite backup to GPS.

ECONOMIC ISSUES

It is clear that the Nation's transportation infrastructure is increasingly reliant on GPS and that satellite technology is vulnerable. It is also clear that the Nation must seek cost-effective means to protect our national transportation and other infrastructure. In this regard, Congress has shown exceptional leadership, supporting numerous steps to take advantage of Loran's utility as a national asset that can complement GPS in a multimodal and cost-efficient manner.

With regard to Loran's ability to complement GPS in aviation, it is important to note that the current VOR/DME system costs approximately three times more than Loran to operate annually. In contrast, Loran can not only provide navigation benefits to aviation today and in the future, but its multimodal capabilities mean those benefits can also be provided to millions of other Americans. Furthermore, Loran's costs will drop substantially after the modernization is completed.

To address another important economic issue, it should be noted as in previous years, that two U.S. firms, Rockwell Collins and FreeFlight Systems, are currently developing combined GPS/Loran systems for aviation and terrestrial users. These ongoing programs not only represent increasing commercial interest in such systems, but also promise lower consumer costs, new jobs and related economic benefits.

In addition to these direct benefits to aviation and terrestrial applications, other major transportation user groups wish to enjoy these same benefits, and they have solidly endorsed the Loran modernization program. In the marine community for example, the National Boating Federation (NBF) and United States Power Squadrons (USPS) represent millions of recreational boaters, and these organizations have strongly supported Loran modernization for years.

It should also be noted that the telecommunications and timing community also has an intense interest in the Loran modernization program, and their applications affect the majority of American citizens. For example, the T1X1 standards committee of the Alliance for Telecommunication Industry Solutions (ATIS) has endorsed the Loran modernization program in a letter to the National Institute of Standards and Technology (NIST).

LORAN MODERNIZATION

As indicated above, the Loran recapitalization effort has already yielded cost-savings and national infrastructure enhancements at sites in 17 States (AK, CA, FL, IN, LA, ME, MA, MN, NV, MT, NM, NY, NC, OK, TX, WA, WY) across the country with the potential to benefit various transportation modalities. For example, major progress has been made in replacing old tube transmitters with modern, high efficiency solid-state technology and associated electronic systems. This modernization program has already enabled personnel reductions, increased reliability, and enhanced performance.

As noted previously, these improvements will ultimately reduce Loran's annual O&M costs from $27 million to under $15 million, and do so while improving Loran's ability to complement GPS. Once the recapitalization effort is completed, Loran can act as a multimodal backup for satellite technology, greatly benefiting our national transportation infrastructure for a minimal annual investment.

CONCLUSION

It is a certainty that modern Loran can help protect our critical infrastructure and assist in meeting our national transportation safety and security objectives. The Loran modernization program is indeed a prudent and necessary investment in America's future.

The committee should continue its support for Loran modernization, and we respectfully ask that no less than $25 million in fiscal year 2006 resources from the FAA Facilities and Equipment (F&E) budget be provided for undertaking additional modernization projects through the collaborative efforts of the FAA and the Coast Guard.

Prepared Statement of Easter Seals

EASTER SEALS PROJECT ACTION (ACCESSIBLE COMMUNITY TRANSPORTATION IN OUR NATION)

Chairman Bond, Ranking Member Murray and members of the subcommittee, Easter Seals appreciates this opportunity to share the successes and needs of Easter Seals Project ACTION.

PROJECT ACTION OVERVIEW

The Transportation appropriations process initiated Project ACTION in 1988 by providing funding to the Federal Transit Administration to undertake this effort with Easter Seals. We are indeed grateful for that initiative and the ongoing strong support of this subcommittee in subsequent years.

Following its initial round of appropriations, Congress authorized assistance to Project ACTION in 1990 with the passage of ISTEA and reauthorized the project in 1997 as part of TEA21. The strong interest and support of all members of Congress has been greatly appreciated by Easter Seals as it has pursued project ACTION's goals and objectives.

Since the project's inception, Easter Seals has administered the project through a cooperative agreement with the Federal Transit Administration. Through steadfast appropriations support, Easter Seals Project ACTION has become the Nation's leading resource on accessible public transportation for people with disabilities. The current project authorization level is $3 million, and Easter Seals is pleased to request the appropriation of that sum for fiscal 2006.

The strength of Easter Seals Project ACTION is its continued effectiveness in meeting the congressional mandate to work with both the transit and disability communities to create solutions that improve access to transportation for people with disabilities of all ages and to assist transit providers in complying with transportation provisions in the Americans with Disabilities Act (ADA).

The activities of the project are guided by input from a national steering committee that includes representatives from transportation and disability organizations. Easter Seals Project ACTION has worked effectively with the Department of Transportation under four Presidents, and numerous Department of Transportation (DOT) Secretaries and Federal Transit Administration (FTA) Administrators. Today, Project ACTION is working closely with Secretary Mineta and FTA Administrator Dorn and their teams. Secretary Mineta, who worked on the original authorization of Project ACTION, has worked closely with us since taking over DOT.

Easter Seals Project ACTION was also heavily featured in the President's New Freedom Initiative Progress Report released in 2004. This demonstrates how closely the administration is working with Project ACTION to reach our shared goal of a safe, accessible, reliable, efficient and affordable transportation for and by citizens with disabilities at the local, State, regional and national levels throughout the United States.

SUPPORT FOR EASTER SEALS PROJECT ACTION

Easter Seals Project ACTION's successes are diverse and the value of the Project to both the transit and disability communities can be well documented. For instance, Barry Barker, Executive Director of the Transit Authority of River City (Louisville, KY) states that, "Easter Seals Project ACTION's support has enhanced our ability to maximize the quality of service we provide to all of our customers. The project helps us provide our customers with the mobility necessary to fully participate in the community."

Maureen McCloskey, National Advocacy Director of the Paralyzed Veterans of America states that, "The forum that Easter Seals Project ACTION has provided has created a dynamic dialogue between the disability and transit communities that has resulted in increased access to transportation for people with disabilities."

EASTER SEALS PROJECT ACTION WORKING AT THE COMMUNITY LEVEL

Among the programs pursued by the project in the recent period have been efforts aimed at increasing community capacity to meet the transportation needs of people with disabilities. For instance, in 2001, Easter Seals Project ACTION initiated the first Mobility Planning Services (MPS) Institute. The latest Institute took place in March of this year and approximately 25 communities took part in the 2-day event. This was the third group of communities to go through the MPS training. The first two groups of communities remain active and working with Project ACTION to continue their work at the community level. To participate in the Institute, each community had to identify a leadership team to attend the training. The leadership team had to consist of representatives from transit providers, disability service providers and disability advocacy organizations. This team approach will assure that all stakeholders are involved in implementing MPS. The greatest success so far of the MPS concept has been that it provides the disability community and the transportation industry an opportunity to develop tools for working together where in the past there had often been a lack of communication and in some cases even animosity. By implementing MPS, communities do a better job of meeting the transportation needs of people with disabilities and therefore better meet the transportation needs of all residents. Communities that participate in MPS receive ongoing in-depth technical assistance from Project ACTION staff ranging from access to Project ACTION materials to on-site training and facilitation by Project ACTION staff.

EASTER SEALS PROJECT ACTION WORKING AT THE STATE LEVEL

Project ACTION is has partnered with the FTA on several initiatives designed to increase the capacity of States to support accessible transportation for people with disabilities.

A good example of this collaboration is the work that Project ACTION is doing with the FTA to support the success of the multi-Federal Department "United We

Ride" initiative. Project ACTION helped facilitate a national meeting in March of 2003 of Governor-appointed representatives from State Departments of Labor, Transportation, Education and Health and Human Services. Forty-six States and territories participated in this forum that was one of five elements of an FTA effort to bring together Federal and State agencies to help identify, plan and alleviate barriers to human service transportation coordination. Project ACTION is assisting in the dissemination of the FTA developed Framework for Action planning process guide to help States and communities build and operate coordinated transportation systems and is providing technical assistance on its use throughout the country.

EASTER SEALS PROJECT ACTION WORKING AT THE NATIONAL LEVEL

Some of the materials that Easter Seals Project ACTION has developed over the years include:

—Pocket guides for Taxi drivers and transit operators to help them better serve customers with disabilities;
—A collection of "success stories" that share, in the own words of people with disabilities, stories about their successful use of transportation and the positive difference it made in their lives;
—New resources and guidance on good practices for conducting physical functional assessments for determining paratransit eligibility;
—A collection of innovative practices in operating paratransit;
—A redesigned resource called "You Can Ride," a reference guide on how to use public transportation for people who can't read; and,
—A model for solving rural transportation issues.

All resource materials available from Easter Seals Project ACTION activities are available free of charge through the Project ACTION clearinghouse on the Project ACTION website www.projectaction.org.

As mentioned, Project ACTION staff also are involved in continuously providing technical assistance to transit providers, nonprofit human service organizations, people with disabilities, and the general public. The forms of technical assistance provided are provided based on the determination of what would be the most helpful in the situation being addressed. Assistance from Project ACTION ranges from the delivery of basic information in the form of brochures from our national clearinghouse to telephone, e-mail, participation in the training program and on single or ongoing on-site work.

CONTINUING NEED FOR EASTER SEALS PROJECT ACTION

Access to transportation is a vital issue for people with disabilities. For many people with disabilities, a lack of accessible, affordable pubic transportation is the primary barrier to employment, education and participation in community life. In his New Freedom Initiative, President Bush recognized the importance of accessible transportation for people with disabilities, and has proposed an increase in Federal support for promoting innovative and alternative transportation solutions for people with disabilities. As these proposals are implemented, it will become increasingly important that the resources and skills, relationships and knowledge that Easter Seals Project ACTION has fostered remain strong. Should the appropriations process support this New Freedom Initiative, Project ACTION is committed to working with DOT on implementation.

There is a growing need for outreach by Project ACTION to specific populations. While Project ACTION has historically worked with rural communities to help address their transportation issues, the lack of access for rural residents with disabilities is still unacceptable. Easter Seals national headquarters and Project ACTION are working together to coordinate efforts to better serve rural residents with disabilities in a variety of service areas including transportation. Further, as the population ages, there is also a need to provide additional specific resources and assistance to transit providers and older passengers. Since most people will experience some level of disability as they age and require accessible transportation, Project ACTION's resources will again be invaluable as transit providers struggle to meet the needs of this new wave of riders.

FISCAL 2006 REQUEST

In order to continue the outstanding work of Easter Seals Project ACTION, Easter Seals national headquarters respectfully requests that $3 million be allocated in fiscal 2006 to the Department of Transportation for project activities.

Mr. Chairman, thank you for the opportunity to present this testimony to the subcommittee. Your efforts have improved the accessibility of transportation for persons with disabilities and the ability of the transportation community to provide good service to all Americans. Easter Seals Project ACTION looks forward to continuing to work with you toward the pursuit of these objectives.

PREPARED STATEMENT OF THE UNIVERSITY CORPORATION FOR ATMOSPHERIC RESEARCH (UCAR)

On behalf of the University Corporation for Atmospheric Research (UCAR) and the university community involved in weather and climate research and related education, training and support activities, I submit this written testimony for the record of the Senate Committee on Appropriations, Subcommittee on Transportation, Treasury, the Judiciary, and Housing and Urban Development.

UCAR is a consortium of 68 universities that manages and operates the National Center for Atmospheric Research (NCAR) and additional research, education, training, and research applications programs in the atmospheric and related sciences. The UCAR mission is to support, enhance, and extend the research and education capabilities of the university community, nationally and internationally; to understand the behavior of the atmosphere and related systems and the global environment; and to foster the transfer of knowledge and technology for the betterment of life on earth. In addition to its member universities, UCAR has formal relationships with approximately 100 additional undergraduate and graduate schools including several historically black and minority-serving institutions, and 40 international universities and laboratories. UCAR is supported by the National Science Foundation (NSF) and other Federal agencies including the Federal Highway Administration (FHWA), the Federal Railroad Administration (FRA), and the Federal Aviation Administration. I would like to comment on the fiscal year 2006 budgets for the FHWA and the FAA.

THE FEDERAL HIGHWAY ADMINISTRATION

The fiscal year 2006 budget request for the FHWA should support the administration's and the country's commitment to a safe, efficient, and modern surface transportation system. Weather research and intelligent transportation system (ITS) technology significantly contributes to this commitment. According to the National Academy of Sciences, weather reduces roadway safety, capacity and efficiency and is often the catalyst for triggering congestion. In the United States each year, approximately 7,000 highway deaths and 450,000 injuries are associated with poor weather-related driving conditions. The economic toll of these deaths and injuries is estimated at $42 billion per year. Weather plays a role in about 28 percent of the total crashes and 19 percent of the total fatalities. The societal and economic impacts of adverse weather on the highway system are enormous.

Road Weather Research Program

To mitigate the effects of weather, the FHWA's Road Weather Management Program conducts applied research in partnership with a broad spectrum of the weather research and transportation stakeholders with a goal of transitioning advanced weather detection and forecasting technologies into operational use to support traffic, incident, and emergency management, maintenance operations, and traveler information systems. Leveraging the work of the research community, the FHWA has made tremendous strides in just a few years in understanding and developing decision support systems to address the impact of poor weather on the surface transportation system. Enhanced research on pavement condition prediction, snow and ice control, fog, road friction, flooding, thunderstorm forecasting, icing, sensor development, and other areas will result in even more savings, in lives and dollars. Advanced surface transportation weather technologies are critical components of ITS solutions.

Regarding the fiscal year 2006 request for the FHWA, I would like to comment on accounts related to surface transportation weather research that fund the collaborative work of surface transportation weather researchers and stakeholders. These accounts are relatively small in dollar amounts, but the work is potentially life saving for the users of the national surface transportation system. It should be noted that according to the 2004 National Research Council's report titled Where the Weather Meets the Road: A Research Agenda for Improving Road Weather Services, the investment required to satisfy the unmet needs for road weather information is $25 million per year for 15 years. An investment at this level would be focused on developing decision support systems for traveler information systems, winter road maintenance, traffic, incident and emergency management, in-vehicle information systems, and ITS.

Only recently has the FHWA begun investing in road weather research and this investment level has been very low (~$2 million to $4 million per year) considering its impact on the transportation system. The funding has come partly from ITS Research and Development and from FHWA Operations. An investment at a much higher level is required.

An adequately funded road weather research program will improve the safety, capacity, efficiency and mobility (reduce congestion), of the national roadway system. It will benefit the general public, commercial trucking industry, State DOT traffic, incident and emergency managers, operators and maintenance personnel. The road weather program will focus on the development of decision support systems for winter maintenance to improve snow and ice control operations by reducing staff costs and optimizing chemical use, which will result in environmental benefits. It will also focus on detecting, predicting, and communicating road weather hazards such as black ice, fog, hail, flooding, strong winds, and snow. Decision support systems for traffic, incident, and emergency management will also be developed and implemented taking advantage of new and emerging ITS technologies, such as vehicle infrastructure integration, and road weather information sensor systems. In-vehicle information systems capable of alerting drivers to dangerous weather and road conditions will also be developed as part of this research program.

The Transportation Reauthorization Bill, H.R. 3 (TEA–LU), Section 5607 contains language that establishes a merit based Road Weather Research and Development Program within the FHWA ITS Research and Development Program with annual funding at $4 million (significantly less than the NRC recommendation of $25 million). The establishment of a Road Weather Program is well supported by numerous organizations including the American Association of State Highway and Transportation Officials (AASHTO), the International Transportation Safety Association (ITSA), the Transportation Research Board (TRB), the National Research Council (NRC), and State Departments of Transportation (DOTs). Please support this important roadway safety and efficiency improvement program; I urge the committee to fund a Road Weather Research and Development Program of, at a minimum, $4 million in fiscal year 2006.

FEDERAL AVIATION ADMINISTRATION (FAA)

"Hazardous weather is a leading cause of aviation accidents—with more than 100 general aviation fatalities per year due to weather—and providing weather information directly to the cockpit is seen as a key factor in helping reduce weather-related accidents."—FAA's ARA News Bulletin.

Safety is of paramount importance to the flying public; weather is a primary factor in more than 40 percent of commercial aviation fatal accidents. A goal of the FAA is to reduce weather-related fatal accidents for commercial and general aviation by 80 percent by 2006. While substantial progress has been made through the FAA's Aviation Weather Research Program (AWRP), continuation of ongoing efforts is essential to reach its goal.

To mitigate the effects of weather, the FAA's AWRP conducts applied research in partnership with a broad spectrum of the weather research and user communities with a goal of transitioning advanced weather detection and forecasting technologies into operational use. Leveraging the work of the research community, the FAA has made tremendous strides in understanding and mitigating severe weather on aviation. Enhanced research on turbulence, thunderstorm forecasting, oceanic weather, icing, and other areas will result in even more savings, in lives and dollars. I ask you to support the fiscal year 2006 request of $20.6 million for the Aviation Weather Research Program, which is within the FAA's Research, Engineering and Development (RE&D) appropriations.

I also ask you to support the request for the following accounts that fund the collaborative work of researchers in universities and Federal laboratories. These accounts are relatively small in dollar amounts, but the work is potentially life saving for our Nation's pilots and passengers.

Joint Planning and Development Office (JPDO)

The President has requested $18.1 million in its RE&D appropriation for the JPDO in fiscal year 2006 to support planning and development for the Next Generation Air Transportation System (NGATS). Working in close collaboration with the Departments of Commerce, Defense, and Homeland Security, the FAA, NASA, the White House Office of Science and Technology Policy, and other experts from the public and private sectors, the JPDO is developing a business plan for the aviation system of the future. Its goals and objectives focus on eight specific areas, one of which is aviation weather forecasting. The research community has years of expertise and knowledge to contribute to this area. The request of $18.1 million is a significant increase from the fiscal year 2005 level of $5 million, and is supported by the Secretaries of Transportation, Commerce and the Air Force, and the NASA administrator. I urge you to support the requested amount of $18.1 million for the Joint Planning and Development Office.

Wind Profiling and Weather Research—Juneau

Turbulence costs U.S. airlines an estimated $100 million each year in injuries and operational disruptions such as delays and rerouting. High wind information can help airlines adjust their routes and schedules to optimize usage of the airport. Within the FAA's Facilities and Equipment is the program, Wind Profiling and Weather Research-Juneau, which supports the Juneau Airport Wind System (JAWS), an operational system in development, designed to detect and warn of wind hazards. For fiscal year 2006, the FAA is requesting $3.16 million to continue this work; while it is less than last year's level approved by Congress, I am pleased that this is the first year the FAA has requested funds for this effort. I ask that you support the administration's request of $3.16 million for Wind Profiling and Weather Research-Juneau.

Wake Turbulence

Improving the detection and forecasting of wake turbulence is a key element to the FAA's goal of tripling air travel capacity by the year 2025. The Joint Planning and Development Office Integrated Product Team is committed to better understanding wake vortex behavior, and improved forecasting of this invisible threat. Within the FAA's F&E account, $2 million is requested for wake turbulence research. Another $2.3 million is requested in its RE&D account. Given the importance of this relatively small research program to the FAA's capacity goal, I urge you to support these requests for wake vortex capacity enhancement.

On behalf of UCAR, as well as all U.S. citizens who use the surface and air transportation systems, I want to thank the committee for the important work you do that supports the country's scientific research, training, and technology transfer. We understand and appreciate that the Nation is undergoing significant budget pressures at this time, but a strong nation in the future depends on the investments we make in research and development today. We appreciate your attention to the recommendations of our community concerning the fiscal year 2006 FHWA and FAA budgets and we appreciate your concern for safety within the Nation's transportation systems.

PREPARED STATEMENT OF THE FOND DU LAC BAND OF LAKE SUPERIOR CHIPPEWA

Mr. Chairman, members of the committee, I am Peter J. Defoe, Chairman of the Fond du Lac Band of Lake Superior Chippewa. On behalf of the Band, we would like to thank you for this opportunity to submit testimony on fiscal year 2006 appropriations relating to the Department of Housing and Urban Development. We submit this testimony to urge Congress to increase the Federal funding levels for Indian housing programs that are provided through the Department of Housing and Urban Development.

Specifically, we ask that Congress increase, or at least restore to fiscal year 2005 levels, funds for the Native American Housing Block Grant Program (NAHASDA), and to increase all other HUD programs serving Native Americans. Although the NAHASDA program is the principal source of Federal financial assistance for housing on Indian Reservations, the President's proposed fiscal year 2006 budget would cut that program by 7 percent from fiscal year 2005 levels. Because of the severe and persistent deficiencies in housing in Indian country, such cuts should not be made. Congress should increase, in light of inflation, the funding for these vitally important programs.

Native Americans suffer the most substandard housing—at a rate of six times that of the population at large. The Fond du Lac Band, like tribes nationwide, has longstanding and severe housing needs. Our Reservation, located in northeastern Minnesota, is part of our aboriginal territory. The Reservation was established for us by Treaty with the United States on September 30, 1854 as our permanent home. We have 3,900 enrolled tribal members, and provide a wide range of services not only to our members, but also to approximately 6,500 Indian people who live and work on and near our Reservation.

The Fond du Lac Reservation did not receive public housing until 1965, 30 years after public housing was established for all other Americans. The implementation of the housing program for Fond du Lac followed many years of failed Federal policy, which served to break up families by placing children in boarding schools and foster homes, and which relocated many of the residents of the Fond du Lac Reservation from the Reservation to urban areas. In recent years, many Band members have come back to the Reservation in the interest of obtaining jobs that the Band can now provide as a result of the Band's recent strides in economic development.

Although our Reservation encompasses 100,000 acres of land, the Federal allotment policy, which was applied to the Fond du Lac Reservation in 1889, left us with the poorest lands; our most valuable lands went to timber companies and homesteaders. In addition, our Reservation is located in a geographical area that contains mostly marginal lands that require costly drainage projects for the land to be useable. Our lands are considered a difficult environment for affordable housing because they require high development costs associated with substandard soils and expensive sewage systems and a lack of decent infrastructure. In an effort to meet our members' housing needs, the Band has found it necessary to invest significant funds to remediate the Band's current lands, purchase other lands, and construct the infrastructure (septic systems, water and sewer lines, roads, and utility services) that is essential to serve those lands.

The Band cannot do this alone. The Band has long depended on the funds made available to Indian tribes through HUD to assist us in meeting the housing needs of our members. But the deficits in housing for Indian people are so entrenched and so severe that they will not be remedied without continued Federal financial assistance.

We currently have 146 units of homeownership housing, and 230 units of low rent housing. Of these housing units, 75 percent are over 15 years old, and as a result, are constantly in need of maintenance and repairs. Over 20 percent of these homes are in need of major renovation—which will cost between $10,000 and $20,000 per unit. Other units require routine repairs and maintenance, the average cost of which is $5,000 per year.

The Fond du Lac Housing Division currently has a waiting list of 224 applicants seeking housing. This is just the waiting list for low income housing. We have many other Tribal members who are also in need of housing, but who have moderate incomes and therefore are not even shown on our waiting list. To meet the needs of our low income members we need to build at least 200 new housing units. We also need to build new and upgrade existing septic systems to serve that housing, the cost of which is estimated to be approximately $5 million.

The disparity between housing conditions among our members and that of the general population is shown by the 2000 Census. In Minnesota, 0.5 percent of the population lives in homes lacking complete plumbing. In contrast, among Fond du Lac members that figure is 10 times higher—5.1 percent. In Minnesota, 0.48 percent of the population lives in homes that lack complete kitchens. In contrast, among Fond du Lac members, 4.2 percent live in homes without complete kitchens. In addition the poverty rate in Minnesota is 7.9 percent, while the poverty rate among Fond du Lac members is 14 percent.

Because of the severity of our housing shortage, approximately 40 percent of our people live in overcrowded homes. It is not uncommon on our Reservation and among our people to find 10 or more individuals living together in a two-bedroom home. Overcrowding, in turn, taxes the house itself. Overcrowded homes accelerate the wear and tear on those homes. For example, the Band has been required to rebuild septic systems because the existing system was not built to serve the number of individuals that were actually living in the home. Over the past 5 years, our Housing Division has spent approximately $1.2 million on septic repair and replacement and additional work still needs to be done. These costs, although necessary, restrict the resources that would otherwise be available for new construction of housing units. The needs are great but the resources keep getting smaller.

Overcrowding and dilapidated housing creates other risks. As discussed by the U.S. Commission on Civil Rights, in its report, A Quiet Crisis: Federal Funding and Unmet Needs In Indian Country, at 62–63 (July 2003), the high rate of overcrowded housing among Native Americans increases the risk of fire and accidents, and creates unsanitary conditions, with increased spreading of communicable but normally preventable illnesses. Overcrowded housing is especially harmful to children, who, as the Commission found, are likely to "suffer sleep deprivation and inability to concentrate in school." In addition, overcrowding "often results in stress, which can magnify family dysfunction and eventually lead to alcohol and child abuse." A Quiet Crisis at 63. We see these problems at Fond du Lac.

In addition to the problem of overcrowding, we are also faced with a burgeoning homeless problem that needs to be addressed immediately. In 1994, the Minnesota Housing Finance Agency reported that while the homeless rate for all Minnesota residents was 0.92 percent, the homeless rate among Fond du Lac members was 6.54 percent. Minnesota Housing Finance Agency, Comprehensive Housing Affordability Strategy 1996–2000 at 28, 43, 49 (December 29, 1995). The problem of homelessness still exists and is severe. The Band regularly receives requests from Band members who are homeless and in need of housing. The Band currently has no facilities to provide temporary shelters to house our members when emergencies arise. The Band is presently assisting 20 homeless families by providing shelter and rental assistance in several local hotels and motels—a situation that certainly does not foster a sense of belonging and ownership, not to mention the financial burden that this places on the Band's limited resources. The Band needs affordable low-income transitional housing in order to assist families in the interim that want to come home to the Reservation or who face housing emergencies.

We also need to address the housing needs of our elderly population by providing assisted living accommodations for them if they so choose. Our elders are our teachers and mentors and we need to honor and respect them by giving them comfort and security, and allow them to live in a secure, healthy and worry-free environment.

The Band relies on its annual grant from the Department under the NAHASDA program to meet some of these housing needs. The Band has also relied on Indian Community Development Block Grants, which the Band has been able to use for infrastructure. However, the funding for these programs has not materially increased over the years. At the same time, the costs of the supplies, materials and labor necessary to remodel and modernize our aging housing stock have increased every year with inflation. Each year we are forced to do more with less. Current funding levels simply do not meet the housing needs. Further cuts in the NAHASDA program and in the other HUD programs that are intended to serve Indians will only make this housing crisis worse. The Federal Government's trust responsibility demands that this Indian housing crisis be addressed.

The inadequacy of Federal funding for Indian housing programs was documented by the U.S. Commission on Civil Rights 2 years ago. As the Commission found, and as we have seen, Federal funding for the Indian programs provided by HUD has not even kept pace with inflation. When adjusted for inflation, it is clear that HUD funding for Native American programs has actually decreased 1.3 percent from 1998 to 2004. A Quiet Crisis at 67. In contrast, during the same period, HUD's overall budget, even when adjusted for inflation, actually increased by 46.5 percent. In fiscal year 2005, the HUD budget for Native American programs was reduced from fiscal year 2004 levels. Although Congress has consistently found that housing conditions among Native Americans are far worse than housing conditions among any other group, funds have yet to be provided to effectively address those needs.

Housing represents the single largest expenditure for most Indian families. The development of housing has a major impact on the national economy and the economic growth and health of regions and communities. Housing is inextricably linked to access to jobs and healthy communities and the social behavior of the families who occupy it. The failure to achieve adequate housing leads to significant societal costs.

For most families, the investment in housing is the only tool for wealth building. On most reservations the opportunity to use equity in home building has not been available. There are recent initiatives, such as the Section 184 Housing Program, under which guaranteed loans are made available to Indian people to build or purchase housing on trust lands. Our community is on the verge of implementing that program to assist our members. However, with the proposed cuts to the Federal budget for housing programs, there will be a comparable reduction in the availability and use of these wealth-building tools.

Decent, affordable, and accessible housing fosters self-sufficiency, brings stability to families and new vitality to distressed communities, and supports overall economic growth. Very particularly, it improves life outcomes for children. In the process, it reduces a host of costly social and economic problems that place enormous strains on the education, public health, social service, law enforcement, criminal justice, and welfare systems. For these reasons the Fond du Lac Band strongly urges Congress to increase funding for our housing needs, rather than impose cuts which will adversely affect the core of our communities.

Miigwech. Thank you.

PREPARED STATEMENT OF THE SHOSHONE-BANNOCK TRIBES

On behalf of the Shoshone-Bannock Tribes of the Fort Hall Reservation, I submit this testimony on fiscal year 2006 appropriations for Native American Programs provided through the Department of Housing and Urban Development. We are Idaho's largest tribe, with a reservation population of nearly 8,000 residents, Indian and non-Indian, spread out over a 753 square mile reservation. Like many tribes, we have vast unmet needs in housing. We oppose the administration's effort to further reduce funding for Native American housing programs that are funded through the Department of Housing and Urban Development. The administration's proposed reductions to these programs impact Indian tribes more severely than other program cuts because Indian programs are already significantly under-funded.

A housing crisis exists in Indian country, and it exists on the Shoshone-Bannock Reservation. The 2000 Census shows this. In stark contrast to all other Americans, 16 percent of all Indian homes had no electricity, 21 percent had no piped water, over half had no central heating and nearly 12 percent lacked complete plumbing. In addition, Native Americans suffer from disproportionately high rates of homelessness, or live in severely overcrowded conditions. The problems in Indian housing were also documented by the U.S. Commission on Civil Rights, which in a report issued 2 years ago, found that overcrowding on Indian trust lands "is six times the national rate." U.S. Commission on Civil Rights, A Quiet Crisis: Federal Funding and Unmet Needs In Indian Country, at 62–63 (July 2003).

The Commission on Civil Rights, in its 2003 report, found that Federal funds for Indian housing programs have never kept pace with increased housing costs and tribes are in fact losing purchasing power. During the 7-year period from 1998 to 2004, while overall funding for HUD, when adjusted for inflation, increased by 46.5 percent, HUD funding for Native American programs decreased by 1.3 percent. A Quiet Crisis at 56.

The Fort Hall Reservation encompasses four Idaho counties: Bingham, Bannock, Power and Caribou and is one of the largest land based Indian tribes in Idaho. According to the 2000 U.S. Census, more than 25 percent of Native American families residing on the Reservation live at or below the poverty level. Hundreds of Indian families are kept on our Housing Authority's waiting lists for low-income and Mutual Help homes because our resources are inadequate to finance new construction or renovate existing homes. We need to build hundreds of new homes on our reservation. Statistics mask the true need for safe and affordable housing for many eligible families simply stop petitioning for housing when year after year they are told that tribes do not have the resources. Even when the Tribes' Housing Authority is able to provide a home for an eligible family, some aspect of the project is incomplete (e.g., exterior stairs) due to lack of funds, and the family is reminded that the needs of Native Americans remain a distant concern of the Federal Government.

Despite the substantial and well-documented unmet needs in Indian housing, the administration proposes deep reductions to Federal funds for Indian housing programs in fiscal year 2006. The President's proposed budget would significantly cut funding for Indian Housing Block Grants (IHBG) that are made available to Tribes under the Native American Housing Assistant and Self-Determination Act of 1996 (NAHASDA), which funds are essential for maintaining existing housing units and building new homes. The President also proposes to reduce the funding for Indian Community Development Block Grants (ICDBG), which program serves as an important resource for constructing the infrastructure necessary for Indian housing. The net effect of the cuts in these two programs would be an overall reduction of more than $107 million, a 15 percent reduction from last year's enacted levels at a time when tribal populations are increasing along with the demand for safe and affordable housing. These reductions are unwise and will further compromise Tribal efforts to provide safe and affordable housing to eligible members.

Indian country simply cannot afford such substantial reductions in housing funds. We urge Congress not to allow such cuts to be made. We ask Congress to increase HUD funding for Indian housing programs above fiscal year 2005 levels to account for increases housing costs and inflation. Congress should appropriate $700 million for the NAHASDA block grant program and maintain, as a separate program, the $68 million for the Indian Community Development Block Grant. This will afford the Shoshone-Bannock Tribes, and other Indian tribes, some of the resources we require to address chronic housing inequities and other problems relating to inadequate infrastructure which persist in Indian country.

The Tribes would also like to see Congress restore the Rural Housing and Economic Development program which the President eliminated from the fiscal year 2006 budget. This program provides capacity assistance to rural, local and State organizations and Indian tribes. Grants awarded under the RHED program finance a variety of programs like enterprise development, affordable housing construction, staff development and computer software. We urge Congress to support continued funding of the RHED program at $25 million.

When Congress passed NAHASDA, it recognized that "through treaties, statutes, and the general course of dealing with Indian tribes, [Congress] has assumed a trust responsibility for the protection of Indian tribes and for working with tribes and their members to improve their housing conditions and socioeconomic status so that they are able to take greater responsibility for their own economic condition." We ask that the United States live up to these fine words.

If the United States truly wishes to improve the housing conditions and socioeconomic status of Indian communities, it must provide sustained funding so that tribes may recruit and retain qualified staff, so that we may prioritize housing needs, and finance and complete construction of new homes, renovate existing homes, provide other forms of housing assistance, as well as provide related infrastructure—water, sewers, roads, and utilities—which our communities so desperately need. No home in America should be without safe drinking water, a working kitchen, plumbing, and heat. Yet throughout the Fort Hall Indian Reservation, too many homes do not have these "luxuries."

The administration's fiscal year 2006 budget for Indian housing programs, like its budget for other Federal programs which benefit Indian tribes, indicates a lack of appreciation for the challenges Indian communities face each day to provide basic governmental services to their members. Infrastructure in Indian country is inadequate and contributes to the difficulties Tribal governments have to improve the economic and social wellbeing of our members. Congress must restore the President's proposed cuts and increase funding to meaningful levels so that Tribal governments can make tangible progress to improve the housing conditions of our members.

Housing is basic to all people. Safe and affordable housing also promotes the family. So much good can come from providing Indian families with this essential need.

Congress and the administration must recognize that we, like other local governments, are partners with the Federal Government, in providing for the needs of our members. Indian tribes deserve their equitable share of Federal funds to build reservation infrastructure, including housing, so that over time, we may provide for all the needs of our members. Strengthening tribal governments is a good investment of taxpayer dollars. Like the Indian Self-Determination Act, NAHASDA, the ICDBG, and the RHED programs are successful programs and Congress and the administration should increase, not decrease, funding for them.

Thank you for affording the Shoshone-Bannock Tribes the opportunity to make known our comments regarding the President's budget proposal and our needs for fiscal year 2006.

Prepared Statement of Huron Potawatomi, Inc.

INTRODUCTION

The Nottawaseppi Huron Band of Potawatomi Indians appreciates the opportunity to present testimony on the President's fiscal year 2006 budget for the Department of Housing and Urban Development. The Tribe is disappointed that the administration has failed to acknowledge the chronic housing needs facing Indian tribes and has proposed harmful and dramatic cuts to tribal housing programs that Indian tribes rely upon to fund their housing operations.

In fiscal year 2005, Congress appropriated $622 million for the NAHASDA Indian Housing Block Grant (IHBG) Program and $68 million for the Indian Community Development Block Grant (ICDBG) Program. The combined total for these programs in fiscal year 2005 was $690 million. For fiscal year 2006, the President proposes to cut these two programs by $107 million and fold a reduced ICDBG program into the NAHASDA program. The fiscal year 2006 funding for these programs would total $583 million, a 15.5 percent reduction from the fiscal year 2005 enacted level. The President's budget eliminates support for the National American Indian Housing Council which assists Indian tribes with technical assistance and capacity-building. Under NAHASDA, we are limited in the amount of funds they we may use for administration and technical assistance from HUD is limited by funding and staffing constraints.

We have stated in the past that basic infrastructure—housing, law enforcement, roads, sewers, and health facilities—is required in Indian country if tribes are to attract business and provide for their members. Safe, affordable housing is a critical element to improve the quality of living for our members. It provides family stability. It promotes health. It is a basic human need. Homeownership is part of the American dream. The President's proposed cuts to Indian housing programs are ill-advised. In the long run these cuts will have a devastating impact on Indian communities. Our numbers grow. Inflation reduces what little we have. Congress must act.

We ask that Congress reverse these proposed cuts to Indian housing programs. We request that the committee restore and increase funding for NAHASDA's IHBG program to $650 million and retain separate funding for the ICDBG program at $70 million so that we may address the acute housing needs of our members.

In February, HUD's Assistant Secretary for Public and Indian Housing testified before Congress. He noted that in fiscal year 2004, Indian tribes and their housing authorities built 2,115 new housing units. Yet, despite these successes, the Assistant Secretary acknowledged that HUD expects to see overcrowding in Indian country reduced by "at least one percent in the coming year, which means that 467 additional families will be housed." At that rate, it will take 100 years to resolve overcrowding in Indian country. This Nation can do better than that. It must.

HOUSING NEEDS

Our Tribe has over 600 enrolled members, with a total of over 390 member households. Many of our members have incomes at or below the poverty level. More than half of Huron Band families live in substandard and overcrowded housing. Less than 20 percent of our members own their own home. More than 30 percent of member households receive housing assistance. Housing assistance consists of rental, utility, rehabilitation, advocacy, training and/or apprenticeship, and construction.

Our housing program offers rehabilitation assistance to repair member homes—ranging from roofing, sewer and water, plumbing, electricity, HVAC, window replacement, insulation, and lead and asbestos mitigation. In some instances, we cannot assist members in need because our policies permit assistance to members once per year and three times in a lifetime.

In many instances, "affordable" rental housing for our members means living with substandard electrical, plumbing, and heating, often in unsafe neighborhoods.

Many of our members currently living off-Reservation have expressed a desire to relocate to the Reservation if adequate housing were available to them. Despite record-low mortgage interest rates and increased activity in the real estate market, the price of available housing within the local market is generally prohibitive to lower income families. Within our service area, the current job market is centered away from the Pine Creek Reservation, toward the larger cities and surrounding areas, particularly Kalamazoo and Grand Rapids. Rental properties within the immediate vicinity (25 to 50 miles) of the reservation present a variety of issues that include affordability and safety. Structurally, many affordable units are inferior and unsafe.

Lack of Housing

As noted above, few members own their own homes. Of those families living in rental units, many pay more than 50 percent of their monthly income in rent, leaving very little money for other household expenses. In the winter months, when temperatures routinely fall below freezing, lack of money for utilities is especially dangerous. With rising heat and electricity costs, many tribal families are forced to choose between paying rent or using the rent money to keep the utilities on, eventually facing eviction for nonpayment of rent.

We are also seeing an increase in homelessness among our members, especially among families with young children. The Tribe currently does not have enough funding to provide transitional housing, so we must refer these families to shelters in larger cities. Once there, they may be turned away if the shelter is full that day. The Tribe would like to address the growing homelessness problem by finding ways to provide temporary or transitional housing on the Reservation.

Our housing goals are modest. We seek to construct seven low-income elder rental units, six low-income rental units, provide 15 eligible tribal members with financial assistance through the Down Payment Assistance Program, rehabilitate and renovate eligible homes, provide Emergency Rental/Utility Assistance and home counseling services to eligible members.

Housing Conditions

Many of our members live in substandard housing. For example, recent cases addressed by our Housing Department included an elder who lived for several years in a home with no indoor plumbing and no running water, and a family with children with no heat that placed blankets over the windows for insulation. Other homes are in such poor condition that housing inspectors order them condemned before rehabilitation can even occur. They express disbelief that people actually live in such conditions. The Department has also intervened in cases of major insect infestation, toxic mold and mildew, indoor air quality problems and lead contamination. These deplorable housing conditions can be changed, but it takes money and adequate staff to run the program, determine eligible recipients, and monitor the work performed.

HUD FUNDING AND ACTIVITIES

We have witnessed a steady decline in our IHBG funding from a high of $419,000 in fiscal year 2002 to the current funding of $273,000 in fiscal year 2005 (more than a 33 percent reduction). This year is the first year the Tribe has been awarded funding under the ICDBG and we plan to construct a community center. Roughly 40 percent of our recent housing budget went toward new construction, another 32 percent for housing services, 6 percent for rehabilitation, 2.5 percent for housing management services, and slightly less than 20 percent for planning and administration. How will we make up for the President's proposed cuts?

The Housing Department works with the Indian Health Service and South-Central Michigan Construction Code Inspection, Inc., a local non-profit municipal agency, to provide inspection code enforcement services. The Housing Department ensures that renovation and rehabilitation projects are performed pursuant to IHS, BIA and NAHASDA standards, and are examined by a qualified, contracted inspector. The Tribe has adopted the National Building and Maintenance Codes and Construction Standards which will be enforced through an association with the South Central Michigan Construction Code Inspection, Inc. How can we be viewed as a reliable partner with other local governments if we cannot assure that essential tribal programs will have the resources required to properly staff and operate them?

The Housing Department is continually working to address Tribal member's home health and safety needs. We provide members with smoke and carbon monoxide detectors, radon testing, fire extinguishers, home repair manuals, and child-proof cabinet and drawer latches.

The Tribe was only recognized in 1996, and we do not have any formula-eligible housing stock. This summer, the Tribe will begin construction of elder housing.

CONCLUSION

Through housing programs such as NAHASDA, the Indian CDBG, and the BIA's Housing Improvement (HIP) Program, Congress has entrusted Indian tribes with resources to address our member's most basic need—safe and affordable shelter. Congress must know, however, that these resources are insufficient to the task. Census statistics and reports reveal that Native Americans are three times more likely than other Americans to live in overcrowded homes, many without central heating or complete plumbing.

Congress must reverse the President's proposed budget cuts. Appropriations for Indian housing have stagnated and are at their lowest level in 5 years. Housing construction costs have risen. Budget cuts hurt our ability to tackle housing needs. As the demand for safe and affordable housing increases, our needs increase. Construction costs increase and we must still recruit and retain qualified staff. With reduced funds under NAHASDA, as proposed by the President, we are limited in our ability to remedy unsafe and unsanitary housing conditions.

When it passed NAHASDA, Congress recognized that "through treaties, statutes, and the general course of dealing with Indian tribes, [Congress] has assumed a trust responsibility for the protection of Indian tribes and for working with tribes and their members to improve their housing conditions and socioeconomic status so that they are able to take greater responsibility for their own economic condition."

If the "government-to-government" relationship is to remain meaningful, the current administration, future administrations, and the Congress must consult with Indian tribes, learn more about our needs and how best to address them, and provide tribes the flexibility we need to address a myriad of housing problems. Most importantly, the Federal Government must not undermine the successes Indian tribes have achieved to redress chronic housing problems by cutting the Federal programs we rely upon.

Native Americans have answered the call for national sacrifice in the War on Terrorism. Those brave men and women serving in the Armed Forces of the United States deserve to know that their mothers and fathers, spouses and children, and extended families are safe at home.

The Huron Band will do its part to improve the living conditions of our members. We only ask Congress to give us, and other Indian tribes, the resources necessary for the job. We long to be self-sufficient, but until that day comes, the United States must live up to its word. The President can propose cuts, but it is the Congress which appropriates the Nation's resources. Please continue to allocate them where there is documented need.

Thank you for permitting us the opportunity to submit comments on the President's fiscal year 2006 budget for the Department of Housing and Urban Development.

PREPARED STATEMENT OF THE FORT PECK ASSINIBOINE AND SIOUX TRIBES

Mr. Chairman and members of the committee, I am Ray K. Eder, Chairman of the Assiniboine and Sioux Tribes of the Fort Peck Indian Reservation, in Montana. I am pleased to present this testimony regarding the fiscal year 2006 budget for the Department of Housing and Urban Development.

Indian communities across America continue to be plagued by severe housing shortages. The tragedy of homelessness and substandard housing is only too familiar to Indian tribes within this country. A 2003 report by the U.S. Commission on Civil Rights found that approximately 90,000 Indian families were homeless or under-housed. Native Americans are three times more likely than other Americans to live in overcrowded homes; on reservations, 14.7 percent of homes are overcrowded, compared to 5.7 percent of homes elsewhere. We are also more likely to lack sewage and water systems. The last census documented that 16 percent of all Indian homes had no electricity, 21 percent had no piped water, over half had no central heating and nearly 12 percent lacked complete plumbing.

About 6,000 tribal members live on the Fort Peck Reservation. Of these, it is estimated that 271 families live in substandard housing, all of whom have incomes below 80 percent of median income. It is also estimated that there are 389 low-income families living in over-crowded conditions.

The Department of Housing and Urban Development estimates that there is a need for about 220,000 new housing units for Indian families, but that NAHASDA funding can only meet 5 percent of this need. The housing shortage will only get worse: according to a Bureau of Indian Affairs Labor Force Report, nearly 44 percent of the population living on the reservation is under the age of 18, further increasing the need for future housing development. The Federal Government's trust responsibility demands that this Indian housing crisis be addressed.

In the face of these inequities, the President proposes to further cut funding for the Native American Housing Block Grant (NAHBG) program from $622 million to $583 million and to cut funding for the Indian Community Development Block Grant (ICDBG) program from $68 million to $57.9 million. Furthermore, the proposed fiscal year 2006 budget for HUD would roll the ICDBG program into the NAHBG program. The result of these changes would be a 15 percent ($10 million) reduction in funding for the competitive ICDBG program and a 15.5 percent ($97 million) reduction in formula funding. This is a total proposed reduction of $107 million in funding for Indian housing.

These cuts must be restored. Furthermore, appropriations for Indian housing, which have not increased significantly since 1998 and are at the lowest level in 5 years, should be increased to a level that is responsive to tribal housing needs. We support the recommendation of the National Congress of American Indians and the National Indian Housing Council that funding for Indian housing be increased to $723 million.

The Fort Peck Housing Authority manages over 955 units through HUD Low Rent and Mutual Help housing programs. With inadequate funding levels and an allocation formula based in part on existing housing stock, most tribal housing entities struggle to maintain their existing housing, leaving no money for new housing. The Tribes' annual formula grant from the Department is $4.85 million. However, because of operation and maintenance obligations to existing housing stock, the Tribes are only able to build 20 new units every 3 years. Consequently, there is a waiting list of over 400 families.

The Tribal Housing Authority continues to find ways to maximize this admittedly insufficient funding. For example, the Tribes have received $2.1 million in ICDBG funding over the past 5 years and have used this funding as seed money, leveraging it for an additional $1.6 million to support tribal housing needs. Projects include a water supply and distribution system for the towns of Frazer and Brockton, a multipurpose building, and housing rehabilitation.

We want the subcommittee to know that our housing needs are significant and that the President's proposed funding decreases will further cripple the Tribes' efforts to provide adequate housing for our members. We urge you to restore all proposed cuts and to increase funding for Indian housing to meet these needs.

I would like to thank the subcommittee for the opportunity to present this testimony.

PREPARED STATEMENT OF THE LAC DU FLAMBEAU BAND OF LAKE SUPERIOR CHIPPEWA INDIANS

"Ahneen. Gum mah quay indiznecos. Makwa Dodame. Waswagoning in doon ja ba." What I said in my native language "Ojibwemowin" was "Hello. My name is Head Woman. I'm of the Bear Clan and I'm from Lac du Flambeau, Wisconsin."

My English name is Victoria Doud, President of the Lac du Flambeau Band of Lake Superior Chippewa Indians. The Lac du Flambeau Reservation is in the North Woods area of Wisconsin and our homeland is called Waswagoning. The Federal Government is obligated by Treaty and Executive Order to provide critically needed social, educational, health and governmental services to the Band and its members in exchange for the land, water, natural resources and peace our forefathers provided. As Congress and the President work on the fiscal year 2006 budget, the obligations and commitments to provide these services must not be forgotten and should be given the highest priority. The Band submits the following issues and concerns to the subcommittee concerning the budget for the Department of Housing and Urban Development.

We request that Congress increase funding for Native American Housing programs to $723 million. Since implementation of the Native American Housing Assistance and Self-Determination Act (NAHASDA) in 1998, HUD has provided assistance to Native Americans through four programs: the Native American Housing Block Grant program (formula funds), the Indian Community Development Block Grant (competitive grants), the Section 184 Indian Housing Loan Guarantee Program and the Title VI loan guarantee program. This year, the President proposes substantial cuts to Indian housing programs. At a minimum, these cuts must be restored. Furthermore, because the budget for Indian housing programs has not increased significantly in recent years and the need continues to outstrip available funding, we join other Native American organizations in requesting that Congress increase funding for these programs.

CHIPPEWA HOUSING AUTHORITY

The Lac du Flambeau Band has approximately 3,600 enrolled members, of which 1,900 live on or near the Reservation. We provide housing for our Members through our Tribally-designated housing entity, the Chippewa Housing Authority (CHA). The mission of the CHA is to develop, operate and maintain affordable housing programs in order to provide Tribal membership with decent, safe, sanitary housing and supportive services that promote self-sufficiency and economic and community development on the Reservation. The CHA's first 20 Low Rent properties were available to the community in 1966. Today, CHA housing stock includes 196 Low Rent units, 40 Mutual Help homes, 48 Tax Credit units and 64 USDA–RDS 515 units.

Homelessness, overcrowding and sub-standard housing are serious problems in Indian Country, and Lac du Flambeau is no exception. Ninety families remain on the waiting list for CHA housing, while 135 families are in pending/review status. Furthermore, although CHA has identified 67 families as ineligible for HUD housing, we still believe that there is a housing need for those families. Because of this housing shortage, 92 of our members are homeless and many others are forced to live in overcrowded conditions. CHA has identified at least 50 overcrowded households. Housing on the Reservation, both public and private, is also in poor condition: 7 units have been identified as dilapidated, 132 units are in need of serious repairs and 175 are in need of minor to moderate repairs.

NATIVE AMERICAN HOUSING BLOCK GRANT

We ask that you increase funding for the Native American Housing Block Grant Program (NAHBG). President Bush's proposed budget for this program in fiscal year 2006 is $583 million. This amount is a $39 million decrease from fiscal year 2005 enacted levels. Moreover, because of proposed changes in the administration of the Indian Community Development Block Grant Program, NAHBG funding will suffer a de facto $97 million cut under the President's proposed budget.

According to data from the National Association of Home Builders, the median cost of a new home has more than doubled in the last 2 decades of the Twentieth Century. In order for the subcommittee to understand the funding shortfall, it is estimated that the CHA would require $2.5 million dollars per year for maintenance and rehabilitation for existing NAHASDA units, $1.2 million dollars annually for new housing development and $1.5 million for administrative costs. The Band urges Congress to increase NAHASDA appropriations to a level that is responsive to the growing housing needs on the reservation.

We also request that Congress revise the formula for allocation of funding under the NAHBG program. The CHA received approximately $1.5 million in NAHASDA Block Grant funding this year. This amount has decreased steadily in recent years, and is down from $1.6 million in fiscal year 2004. This allocation is based on an outdated funding formula that fails to address tribes' need for funds to maintain or improve existing housing and build new housing. Because of the shortfalls in funding, the CHA faces both housing shortages and inadequate funds to renovate existing units. It becomes a balancing act to determine if our limited funding should be used for housing development, rehabilitation of older units or toxic mold remediation. Currently, CHA uses NAHASDA funding for maintenance, renovation and administration, supplementing it with other small grants and rental income. Congress needs to once again revisit the formula issue, since the current formula does not take into consideration the simultaneous need for housing development, remediation, maintenance and modernization.

INDIAN COMMUNITY DEVELOPMENT BLOCK GRANTS

We request that Congress restore or increase funding for Indian Community Development Block Grants. The proposed fiscal year 2006 funding level for the ICDBG program is $57.9 million. This is nearly a 20 percent decrease from the $71.6 million requested in fiscal year 2005. Unlike NAHBGs, Indian Community Development Block grants are awarded to tribes on a competitive basis. These funds are used by tribes to improve housing stock and infrastructure, build community facilities and expand development corporations. The Lac du Flambeau Band has received approximately $500,000 in grant funding annually for community development projects. Each annual grant has been used to support a specific project, including a Planning and Information Facility, a Domestic Abuse Shelter, a Family Resource Center for alcohol, drug and mental health programs, a Wellness Center and a Business Incubator.

Finally, we ask Congress to ensure that, regardless of any administrative changes, both the NAHBG and the ICDBG programs are fully funded. The Band is concerned with the administration's proposal to move the ICDBG program, now a separately-funded competitive grant program, into the NAHBG program. Under this proposed move, $57.8 million of the budget for NAHBG would go to support ICDBG activities. This means that NAHBG formula funding will actually be reduced by $97 million. While we support the administration's effort to ensure that the program remain under the jurisdiction of the Department of Housing and Urban Development, we adamantly oppose any reduction in NAHBG funding. Tribes should not have to suffer a de facto funding cut in these already under-funded programs.

In light of the severe need for housing described above, we urge the subcommittee to increase the budget for Indian housing programs or, at minimum, to ensure that these programs to not suffer funding cuts.

Miigwetch. Thank you.

PREPARED STATEMENT OF THE AMERICAN ASSOCIATION OF SERVICE COORDINATORS

On behalf of low-income frail and vulnerable elderly, persons with disabilities, and others with special needs residing in federally assisted and public housing, the American Association of Service Coordinators (AASC) urges the committee's full support for the staffing of well-trained service coordinators during mark-up of the Transportation, Treasury, Judiciary, HUD and other agencies fiscal year 2006 appropriations bill.

AASC, a nonprofit organization based in Columbus, Ohio, represents over 1,600 service coordinators and other housing professionals nationwide who serve more than 200,000 elderly and others with special needs residing in federally assisted and public housing. AASC members are dedicated to a mission of serving low-income frail elderly, persons with disabilities and others with special needs who live in and around federally subsidized housing, including the Section 202 program and public housing.

Our members are grateful for the leadership of this committee for the establishment and funding of service coordinators. We understand that the committee faces difficult choices during this time of tight funding constraints; therefore, we urge your continued support for a sound investment in the service coordinator program.

Service coordinators are increasingly recognized nationwide as the vital "lynchpin" in linking older persons with essential community supportive services. The fragmentation, lack of awareness, and complexities of some essential services available in the community, have hindered timely access by frail elderly and others, and has contributed to many being forced to move to more costly settings. Service coordinators have helped thousands of low-income elderly and persons with disabilities with their health and supportive service needs, enabling them to age in place and avoid premature institutionalization.

In addition to individual preferences and increased quality of life issues, comparative costs of enabling frail elderly or persons with disabilities to remain longer in their home and community is clearly cost effective for limited Federal funds. The congressionally established Seniors Commission and others have documented the cost-effectiveness of service coordinators who assist frail elderly and others in postponing, if not avoid, costly nursing home placements. In addition, service coordinators allow States and local governments to respond to the administration's New Freedoms Initiative and requirements of the Supreme Court Olmstead Decision by providing options for community-based living arrangements for frail elderly and persons with disabilities.

The current policy debate over the solvency of the Social Security Fund is raising public awareness of the dramatic escalating elderly population, a demographic tsunami, that is challenging our Nation. Service coordinators can have a key role in re-positioning federally assisted senior housing as part of community-based long-term care strategies to prepare for increases in the elderly population, particularly those age 85 and older whose numbers are expected to quadruple from 3.5 million to over 14 million by 2030. While eligibility for federally assisted senior housing is age 62 and older, the average age in many senior housing facilities is well over 80 and generally need increased supportive services as they age.

HUD provides funding of service coordinators in federally assisted housing through three approaches: (1) national competition grants for eligible federally assisted senior housing (Section 202, Section 8, Section 221(d)(3) below-market interest rate, and Section 236); (2) use of the housing project's residual receipts; or (3) a budget-based rent increase or special rent adjustments to accommodate the position as part of the project's operating budget. For public housing, service coordinators have been one of the eligible uses of competitive funds through the Resident Opportunities and Self Sufficiency Program (ROSS).

Yet, despite the critical need and cost-effective role of service coordinators in assisting the elderly and others who seek to remain in their homes, funding to staff and train service coordinators in federally assisted and public housing facilities remains limited. While the administration's fiscal year 2006 budget essentially maintains the current funding levels for service coordinators in Section 202 and other federally assisted senior housing, it significantly cuts funds for coordinators assisting elderly and families residing in public housing.

AASC would urge support for the following:

—$100 million in fiscal year 2006 for service coordinators in federally assisted housing, particularly to ensure adequate funds for expiring contracts of existing service coordinators;

—full funding for Section 8, PRAC, and project operating funds to permit the staffing of a service coordinator as part of the project's routine operating budget, including an exemption, as needed, from rent caps to enable the staffing of service coordinators;

—an add-on of $75 million in Public Housing Operating Funds for service coordinators, and $75 million for Resident Opportunities for Self-Sufficient (ROSS); and

—improved collaboration between HUD and HHS with senior housing and housing for persons with disabilities, including the establishment of Interagency Council on Senior Housing and Services.

FEDERALLY ASSISTED HOUSING—$100 MILLION

The administration's fiscal year 2006 budget requests $53 million for service coordinators, a slight increase over the $50 million that has been provided over the past few years. However, this year there is a potential of losing existing service coordinator positions if the proposed $53 million is not increased. While the initial grants for service coordinators has been for 3 years, extensions of contracts is only provided for 1 year. In fiscal year 2006, there are over 1,075 existing grants for service coordinators due for renewal with an estimated funding need of $54 million to $58 million.

In addition to the jobs lost for existing service coordinators that would affect thousands of vulnerable, low-income older residents, for the first time since Congress established the program in 1990, there would be no additional funds available to staff new service coordinators. This situation is compounded by the fact that many federally assisted and public housing facilities currently do not have the resources to staff service coordinators; are ineligible for funds, such as Section 515 rural housing or Low-Income Housing Tax Credits; or due to limited funding, may need to share service coordinators between several facilities, often miles apart, thus stretching their capacity and effectiveness to assist frail elderly and others.

AASC would recommend funding the service coordinators program at $100 million in order to ensure sufficient funds for renewals of existing contracts, as well as to fund new service coordinators for the hundreds of elderly properties that currently do not have them.

PROJECT OPERATING FUNDS FOR SERVICE COORDINATORS

There is a need for a two-tier strategy for the staffing of service coordinators, to continue the funding of the Service Coordinator grant program; and at the same time to complement this program with parallel actions to permit and promote the staffing of service coordinators as a part of a federally assisted and public housing facility's routine operating budget. The Service Coordinator grant program could be developed as a transition program to initiate the staffing of service coordinators with clear instructions to HUD, accompanied with the necessary funding, to enable sponsors of federally assisted senior housing (as well as housing for persons with disabilities) to incorporate the staffing of service coordinators as part of the housing project's routine operating budget.

Many federally assisted senior housing projects do have service coordinators funded through their operating budgets, but not all housing projects are able to transition from the service coordinator grant program to the project's operating budget because of limited Section 8 or operating funds, or their inability to secure a rent increase due to regulatory impediments that cap rent increases. While there exists authority to allow HUD to take these actions, many senior housing facilities have not been able to secure the necessary rent adjustment from their local HUD office to accommodate the staffing of service coordinators. AASC would recommend that sufficient Section 8, PRACs, or other operating funds be made available, as well as to direct HUD and their field offices, to provide necessary regulatory relief to remove any barriers to enable the staffing of a service coordinator as part of the project-operating budget.

Finally, it is important that financing options continue to allow sponsors to fund service coordinators through either Service Coordinators grants or to include them within the project's operating budget, and the flexibility to phase-in or proportionally fund service coordinators through both funding sources.

PUBLIC HOUSING—$150 MILLION THROUGH ROSS AND OPERATING FUNDS

Over a third of residents in public housing are elderly who reside in age-specific senior housing, family housing, or in mixed-population housing with younger persons with physical and mental disabilities. Funding for service coordinators in public housing stems from a number of pilot programs, including the Congregate Housing Services Program (CHSP) that assist frail elderly and persons with disabilities residing in public or Section 202 housing. In the early 1990's, service coordinators were funded to assist residents living in public housing serving a mixed population, particularly frail elderly living with younger persons with mental and physical disabilities.

A number of local housing authorities have also funded service coordinators though various grant programs under the Resident Opportunity and Self-Sufficiency (ROSS) and Family Self Sufficiency (FSS) programs, including efforts to promote transition from subsidized renters to homeownership and financial independence. Of the $55 million that has been appropriated over the past few years for ROSS, only $20 million has been provided for service coordinators.

Initially part of the Community Development Block Grant (CDBG), in fiscal year 2004, the administration shifted the Elderly/Disabled Service Coordinator program (EDSC) from ROSS to the Public Housing Operating Fund. For fiscal year 2006, public housing elderly service coordinators must be included in the PHA plan; therefore, it is necessary to ensure that there are adequate funds available in the fiscal year 2006 Public Housing Operating funds to accommodate elderly service coordinators. However, HUD indicated that no new service coordinators were to be funded; and existing coordinators are subject to proportional cuts with recent year decreases in Public Housing Operating Funds. Because of limited funds, a number of public housing authorities have been forced in recent years to cut their service coordinator program.

The administration's fiscal year 2006 budget cuts in half the ROSS program from the $53 million appropriated in fiscal year 2005 to $24 million; and cuts Public Housing Operating Funds from $3.6 million to $2.6 million. Conversely, the FSS program that encourages financial independence, including homeownership opportunities, was shifted from the Public Housing Operating Funds to ROSS with an increase from $46 million in fiscal year 2005 to $55 million for fiscal year 2006 with emphasis to help low-income families in public housing transition from welfare to work and to become homeowners. AASC supports the administration's requests for the FSS program.

In addition, we support the administration's goals to make the staffing of service coordinators a part of the public housing operating expense; however, we are concerned about the smooth transition of funding service coordinators from the ROSS program to Public Housing Operating Funds. AASC would urge that a separate add-on of $75 million in the Public Housing Operating Fund be provided for the staffing of well-trained elderly service coordinators. In addition, we would urge that $75 million be provided for the ROSS program to be targeted to specific activities or to develop innovative programs to assist elderly, persons with disabilities and others with special housing needs.

COLLABORATION BETWEEN HUD, HHS AND OTHER AGENCIES

Given the strong relationship between suitable and affordable housing with timely access to a range of supportive services and health care needed by older residents and others with special needs residing in federally assisted and public housing, it is vital that there be effective collaboration between HUD, HHS, and other Federal agencies serving these vulnerable populations. Because of this critical need, AASC would urge that the committee give directives to HUD, HHS and other Federal agencies to develop means to promote collaboration with their respective programs and policies involving services to assist the elderly and persons with disabilities residing in public and federally assisted senior housing.

In addition, we urge the committee to support efforts to establish and fund a Federal Interagency Council on Senior Housing and Services to promote and facilitate collaboration between key Federal agencies to better assist frail elderly and others with special housing needs. Collaborative efforts could include: streamlined administrative systems with flexibility to accommodate effective cooperation; collaborative training of service coordinators; exchanging relevant information and data bases; development and/or identification of models that promote partnership, such as the co-location of community/senior centers with federally assisted and senior and public housing.

Thank you for your consideration of these recommendations.

PREPARED STATEMENT OF THE CONFEDERATED TRIBES OF THE SILETZ INDIANS

On behalf of the Confederated Tribes of the Siletz Indians, I would like to thank the committee for the opportunity to present testimony on the fiscal year 2006 budget for the Department of Housing and Urban Development. Our territory, while located on the beautiful Oregon Coast, is rural and isolated. The Tribes' service area spans 11 counties, serving an Indian population of 25,665. Given our large service area, our housing market encompasses metropolitan, suburban and rural areas. This presents unique challenges for the Tribes' housing program in that we have to respond to a wide variety of our tribal members' housing needs ranging from rental housing, home repair, homelessness, and home financing in these various areas and markets.

As you well know, severe housing deficiencies continue to plague Indian communities. The tragedy of homelessness and substandard housing is only too familiar to Indian tribes within this country. The last census documented that 16 percent of all Indian homes had no electricity, 21 percent had no piped water and over half had no central heating and 43 percent of Indian households were below the poverty line. The Department of Housing and Urban Development estimates that there is a need for about 220,000 new housing units for Indian families, but that NAHASDA funding can only meet 5 percent of this need. In addition, more than 20,000 homes are in need of replacement and more than 60,000 are in need of substantial rehabilitation.

At Siletz, we have 157 low income families waiting for housing assistance—we also have seven families who we classify as the working poor and while they do not meet the low income guidelines are still struggling to meet their families' needs. This translates into over 2,561 Indian families now living in substandard or overcrowded conditions. We also have handicapped members whose homes need to be rehabilitated and members, whose homes are badly in need of health and safety repairs. In addition to providing direct housing assistance, one of our housing program's key goals to is assist our tribal members in fulfilling the American dream of being home buyers and homeowners. Our program provides needed housing counseling—including instruction on how to take care of their home, paying the mortgage, and predatory lending practices. The program also provides down payment assistance for those families who can qualify for private financing to purchase homes. Thus, utilizing the limited HUD resources that the Tribes receive, we are able to meet a broad spectrum of the housing needs facing our tribal community.

Given the significant need in Indian country generally and at Siletz in particular, we were discouraged with the administration's fiscal year 2006 proposed budget for Native American housing programs. At a minimum, we urge Congress to fund for Native American Housing programs at $723 million. Furthermore, because the budget for Indian housing programs has not increased significantly in recent years and the need continues to outstrip available funding, we join other Native American organizations in requesting that Congress increase funding for these programs.

NATIVE AMERICAN HOUSING BLOCK GRANT

Specifically, we ask that you increase funding for the Native American Housing Block Grant Program (NAHBG). President Bush's proposed budget for this program in fiscal year 2006 is $583 million. This amount is a $39 million decrease from fiscal year 2005 enacted levels. If Congress restores the program to $622 million, this level of funding will only allow tribal housing programs to maintain. It will not allow these programs to address the growing backlog in housing needs.

INDIAN COMMUNITY DEVELOPMENT BLOCK GRANTS

We request that Congress restore or increase funding for Indian Community Development Block Grants. The proposed fiscal year 2006 funding level for the ICDBG program is $57.9 million. This is nearly a 20 percent decrease from the $71.6 million requested in fiscal year 2005. Unlike NAHBGs, Indian Community Development Block grants are awarded to tribes on a competitive basis. These funds are used by tribes to improve housing stock and infrastructure, build community facilities and expand development corporations.

Like tribes throughout the country, the Siletz Tribes are concerned with the administration's proposal to move the ICDBG program, now a separately-funded competitive grant program, into the Native American Housing Block Grant program. Under this proposed move, $57.8 million of the budget for direct housing funding would go to support ICDBG activities. This means that NAHBG formula funding will actually be reduced by $97 million. While we support the administration's effort to ensure that the program remain under the jurisdiction of the Department of Housing and Urban Development, we adamantly oppose any reduction in NAHBG funding. Tribes should not have to suffer a de facto funding cut in these already under-funded programs. We urge Congress to reject the administration's proposal.

Again, we thank the subcommittee for the opportunity to present this testimony.

PREPARED STATEMENT OF THE NATIONAL ASSOCIATION OF RAILROAD PASSENGERS

FISCAL 2006 AMTRAK FUNDING

The National Association of Railroad Passengers believes that the right fiscal year 2006 funding level for intercity passenger rail is $2.3 billion, consisting of:

—$1.8 billion for Amtrak. This is what the Amtrak board approved last month, and is consistent with the 5-year plan a slightly different Amtrak board—but with the same chairman—approved 1 year ago, and

—$500 million for a capital program for States investing in rail passenger development. The Federal match would be 80 percent.

WHY TRAINS ARE A GOOD INVESTMENT

Polls have consistently shown that the public wants the rail choice, and that is consistent with Amtrak's ridership statistics in recent years, including fiscal year 2004.

Ridership.—As of the end of fiscal year 2004, Amtrak had posted ridership increases in 7 of the last 8 years; the only exception was a tiny (0.04 percent) decline in fiscal year 2002 when the economy was reeling from the 9/11 tragedy. Fiscal year 2004 ridership was 28 percent above the fiscal 1996 level.

Amtrak ridership increases have come in spite of fare increases and airline fare reductions. Amtrak's yield (average fare per passenger-mile) has increased every year since at least fiscal year 1994 with the sole exception of fiscal year 2003. (A passenger-mile is one passenger traveling 1 mile.) Fiscal year 2004 yield was 62 percent above that in fiscal year 1994.

For airlines reporting financial data to the Air Transport Association (Southwest and JetBlue are among those not reporting), yields fell each year starting in calendar 2001, with the 2004 level 12 percent below the 1994 level, and 20 percent below the peak level in 2000. Even Southwest's yield fell in calendar years 2001, 2002 and 2004.

The success of State-sponsored rail passenger corridors is well known; these successes are not confined to the two coasts. Here, for example, are the changes in ridership percentage posted in fiscal year 2004 (compared with fiscal year 2003) on the corridors radiating from Chicago:

	Percent
Chicago-Grand Rapids	+19.6
Chicago-Port Huron	[1] +16.7
Chicago-Detroit-Pontiac	+12.2
Chicago-Carbondale	+10.3
Chicago-Milwaukee	+10.3
Chicago-St. Louis	[2] +8.1
Chicago-Quincy	+4.8
Chicago-Indianapolis	[3] −6.7

[1] Ridership jumped significantly when Amtrak, responding to a request from the State of Michigan, rescheduled this train on April 24, 2004. Thus, for example, the ridership growth in July, August, and September, was, respectively, 36.8 percent, 22.8 percent and 22.1 percent.
[2] After lengthy negotiations between Amtrak and the city of St. Louis, ground is expected to be broken this year for a new intermodal terminal that will serve Amtrak, Greyhound and the city's highly successful light rail line. When this terminal, originally funded in the 1991 ISTEA law, finally opens, Amtrak ridership at St. Louis should improve dramatically.
[3] The "Hoosier State" is a 4-day-a-week train (running on days when the "Cardinal" does not run) whose primary purpose usually is to ferry cars to and from Amtrak's Beech Grove shops.

However, the long-distance trains also have shown strength. In fiscal 2004, the long-distance trains carried an average 364 passengers per run, and the average number on board at any one time (passenger-miles-per-train-mile) was 171.

Other Justifications.—Items (1) through (6) are specific to long-distance trains; quotations are from Amtrak's new plan.

—(1) "Providing an important transportation link for many underserved rural communities and regions across the country;"
—(2) Providing important transportation for people who cannot fly, who prefer not to fly, or who have medical equipment and/or conditions that make flying difficult;
—(3) "Serving as a foundation of a future rail development program;"
—(4) "Forming the basis for, and connections to, emerging state-supported corridors;"
—(5) On many routes, the best way to see the Nation's natural beauty; the only practical way for those who can't take long automobile trips.
—(6) In many States, the only intercity passenger rail service. (If all long-distance trains disappeared, the surviving system would serve just 21 States, and the network would consist of four, isolated mini-networks.)
—(7) Providing needed transportation capacity with minimum impact on the environment. Except in a few key corridors already at capacity, rail can increase its capacity through-put with relative ease, by increasing train length or running more trains on existing infrastructure.
—(8) The safest mode of transportation in bad weather, and often the most reliable.
—(9) Trains enhance national security both by giving passengers another travel option—most dramatically illustrated immediately after 9/11—and by reducing the Nation's energy dependence.

Related to (3) and (4) above, development of new commuter rail or intercity corridors is more cost-effective where passenger trains already operate. Consider, for example, the creation of Virginia Railway Express, or Amtrak's extension of some Northeast Corridor trains to Richmond (and Newport News). Both efforts benefited because Amtrak's New York-Florida and New York-New Orleans services were already in place, preserving useable tracks under Capitol Hill south of Union Station, and adequate track capacity through Alexandria station.

Long-distance economics.—It is frustrating to our members to hear continual discussion that pits long-distance trains "against" short-distance trains. Both are important; they complement each other and other parts of our transportation network. Certainly, 3.9 million people—the fiscal year 2004 passenger-count on long-distance trains—is significant. Moreover, on a passenger-mile basis, corridor and long-distance trains require similar levels of operating support. (A passenger-mile is one passenger traveling 1 mile.) In fiscal 2004, the farebox recovery (passenger revenues as percent of costs) for short-distance trains outside the Northeast Corridor was 46 percent; long-distance trains were at 39 percent. The "fare box loss" per passenger-mile was almost identical for short-distance trains (22.47 cents) and for long-distance trains (21.82 cents).

DOT Inspector General Kenneth Mead has noted often that the capital needs for corridor development (especially in the Northeast) are much larger than the operating grant requirements of the long-distance trains.

It is sometimes said that "it would be cheaper to buy everyone a plane ticket than to run the long-distance trains." However, this ignores the markets long-distance trains serve which have no affordable air service or, in many cases, no airline service at all. It also ignores some of the other numbered points above.

Amtrak has made a number of route and service cuts over the past few years. Today's network is so skeletal that elimination of any additional route would remove major metropolitan areas from the system and raise the question of whether the system is truly nationwide. It is critical that Amtrak's proposed "performance improvement program" be implemented well before consideration of any route cuts, so that any weaker routes have the opportunity to get a passing grade on the "selected performance metrics" which Amtrak plans to create this year. Amtrak, for example, anticipates beginning any route termination process in fiscal 2008, and also talks of applying the metrics to "prospective new long distance routes." Past studies have indicated that a larger system would have lower unit costs and recover a higher percentage of costs from the farebox.

On-board Food Service

The suggestion has been made that Amtrak's food service costs could be reduced by $80 million–$100 million. If this is based on the assumption that dining cars could be eliminated with no impact on revenue from fares that is unrealistic. Greater efficiencies indeed may be achievable on all Amtrak food services, including dining cars, but eliminating the latter would be counterproductive.

It would be important to understand the impact of Amtrak's outsourcing a few years ago of commissaries. Did this actually improve the cost situation? Does this area show promise of further improvement?

To our observation, food service revenues could be improved if Amtrak promoted the service on board consistently. For example, on Amtrak-operated Capitol Corridor trains in California, at the initiative of local (BART) management, window decals throughout the train invite people to the food car if they are hungry, and announcements are used to do the same.

There has been some talk of simply eliminating food service on short runs under 3 hours. It is important that Amtrak first attempt promotion or other innovations (food trolley going through the train). For some people, including those with certain medical conditions, the availability of on-board food service even on short runs is vital and is a key factor in the decision to take the train.

FEDERAL-STATE PARTNERSHIP NEEDED IN ADDITION TO, NOT IN PLACE OF AMTRAK

While we agree with Secretary of Transportation Norman Y. Mineta that the "Federal-State partnership" is badly needed (second bullet at the beginning of this statement), such a partnership would be worthless absent the foundation or platform provided States by Amtrak's Federal funding and Amtrak's rights.

Secretary Mineta depicts Federal funding for Amtrak as money down a rat hole. His February 23 New York Times op-ed column said, "The federal government can do little to support [state] projects directly, because all of its money goes to Amtrak."

In reality, a lot of the money that goes to Amtrak supports and makes possible the very State projects that Mineta has praised.

—Amtrak funds overhead costs for all U.S. intercity passenger trains—including those of "State-supported" trains.

—Amtrak has provided major assistance in planning State services.

—Amtrak funds direct operating losses of several corridor services, as follows: (1) Empire Corridor (New York-Buffalo)—100 percent; (2) Chicago-Detroit-Pontiac—100 percent; (3) Chicago-St. Louis—66 percent; (4) Seattle-Portland—33 percent (50 percent if Coast Starlight is included); (5) Pacific Surfliners (southern California)—30 percent.

With regard to the Pacific Northwest, Mineta's column claimed that "Amtrak's role is reduced to running the trains under contract," clearly implying that Amtrak provides no funding. In fact, as just noted, the Federal Government through Amtrak funds direct operating losses of two of the three daily Seattle-Portland trains (three of four if counting the Seattle-Los Angeles Coast Starlight), plus overhead costs for all of the trains.

Access to Tracks, Parking Lots, Stations.—Amtrak has the right to access tracks and stations on an incremental cost and a "package deal basis," while others would have to negotiate arms' length deals (driving up the price of service). Moreover, with stations, this could involve lengthy and costly negotiations on an individual property basis. While many stations now are city owned, the private railroads generally own the platforms, and in many cases the parking lots. Even in California, there are still 13 stations owned by Union Pacific or BNSF, and several more owned by local transit authorities.

Ability to Indemnify Railroads.—The railroads accept indemnification only from Amtrak. Several States with rail passenger corridors have indicated they would not be able to offer such indemnification. If they were, it is not clear that railroads would accept it.

DOT's Plan.—Zero funding is provided for fiscal year 2006, along with ever-increasing estimates of funding that would be provided for intercity passenger rail in fiscal year 2007 and beyond contingent on "reforming" Amtrak. However, there would be no Amtrak—and no passenger rail—to reform if Federal funding ceases on September 30, 2005. OMB Director Joshua Bolten reaffirmed the administration's zero request at an April 21 Senate appropriations hearing. So it appears that the administration essentially has said to the Congress, "You figure it out and take the hit for whatever programs you cut to make room for intercity passenger rail in your fiscal year 2006 budget."

AMTRAK'S PLAN

The request for $1.8 billion from a board all of whose members are appointees of President Bush is significant. Also important is their finding—contrary to DOT's—that, due to cost and complexity, the risk of removing Amtrak as Northeast Corridor owner "simply outweighs the benefit," to quote Amtrak Chairman David Laney. An Amtrak official has noted that it would have been impossible to quickly "backfill" Acela Express schedules with Metroliners if infrastructure and carrier had been separately managed.

Obviously, we also agree with their support for a Federal-State partnership on rail corridor development, including "reliable" Federal funding with an 80 percent match.

As rail passengers, our fundamental interest is in the quality and quantity of rail passenger service. However, we are concerned about the passion which the board shows for development of competing carriers, since the freight railroads whose tracks Amtrak generally uses outside the Northeast Corridor are firmly against giving Amtrak's access rights to others. Rhetoric about addressing railroads' concerns "by making franchises exclusive over defined routes" and time-limited is not new to the railroads, and—unless Amtrak knows something we do not—the railroads are not impressed. Also, the effective capacity of today's limited fleet of rolling stock—and the ability to respond to a crisis like the Acela Express withdrawal—would be reduced if the rolling stock ownership was divided among a number of different carriers.

We agree that a more competitive supply industry would benefit the entire railroad industry, but that likely would flow from an adequately funded rail program (including Amtrak and corridor development) and does not require specific legislative changes.

It is important that progress be made on specific contract issues whose relevance to productivity is generally acknowledged, including those mentioned in the Amtrak report (pages 17, 20, 27). Such progress must not be "derailed" either by Amtrak's discussion of changes in Railroad Retirement and the Railway Labor Act, which has already produced angry releases from the unions, or by the discussion of competing carriers which both the freight railroads (as just noted) and rail labor oppose.

Thank you for considering our views.

PREPARED STATEMENT OF THE AMERICAN PUBLIC TRANSPORTATION ASSOCIATION

INTRODUCTION

Mr. Chairman and members of the subcommittee, on behalf of the American Public Transportation Association (APTA), I thank you for the opportunity to testify on the need for and benefits of investment in Federal Transit Administration (FTA) programs under the Transportation, Treasury, the Judiciary, Housing and Urban Development, and Related Agencies Appropriations bill for fiscal year 2006.

ABOUT APTA

APTA's 1,500 public and private member organizations serve the public by providing safe, efficient, and economical public transportation service, and by working to ensure that those services and products support national economic, energy conservation, environmental, and community development goals.

APTA member organizations include public transit systems and commuter railroads; design, construction and finance firms; product and service providers; academic institutions; and State associations and departments of transportation. More than 90 percent of the people who use public transportation in the United States and Canada are served by APTA member public transportation systems.

OVERVIEW

Mr. Chairman, the fiscal year 2006 Transportation appropriations bill is an opportunity to advance national goals through increased Federal investment in the Nation's surface transportation infrastructure, including public transportation. U.S. citizens support Federal policies that create good, high-paying jobs, especially jobs that cannot be exported abroad. Not only does public transportation create jobs, it also helps improve the economy by reducing congestion, promoting energy conservation, and providing transportation options to workers and others.

In 2004, public transportation ridership grew at a rate about the same as vehicle miles traveled on the Nation's roads. Ridership on light rail grew by more than 8 percent, on heavy rail by more than 3 percent, and on bus systems by more than 2 percent. Light rail's strong growth should be of no surprise, considering the establishment of new service in communities around the country including Houston, Charlotte, Little Rock and Minneapolis. As gas prices continue to climb to record highs, public transit agencies in Chicago, Columbus, Denver, Jacksonville, Miami and New York, all have reported increases in ridership.

To augment Federal investment, communities across the Nation are voting for local funding to support new and expanded transit service every year. Voters in 44 areas, including Denver, Phoenix and San Diego approved new or extended existing taxes in November 2004 to finance such new service. Demand for these options is partly a product of frustration with constantly growing congestion that negatively affects our quality of life by wasting time and money, and a desire for cleaner air. Indeed, polls show that voters support public transportation regardless of whether they live in urban, suburban, or rural communities, and that they will vote for candidates who support such investment. However, transit service is only useful if is convenient and available, and today less than 55 percent of all families have access to any public transportation, based on the 2003 American Household Survey for the United States, and an even smaller number of households have access to adequate public transportation service.

Similarly, with the population aging, many older Americans would benefit from increased investment in public transportation. As driving becomes a less viable option for many elderly citizens, they and persons with disabilities want good public transportation options so that they can continue to participate fully in society. Ridership on demand-response systems grew by more than 4 percent in 2004. Because of funding constraints at all levels of government, many older Americans and people with disabilities have limited access to public transportation services, despite the fact that good transit service can make the difference between living independently and moving into assisted living facilities.

Clearly, we need to maintain, improve, and expand the public transportation systems that have served this country so well, but the needs are great. The American Association of State Highway and Transportation Officials (AASHTO) and Cambridge Systematics, Inc. estimate that an annual capital investment of more than $44 billion is needed to adequately maintain and improve existing transit systems. The Senate took an important step towards meeting these needs when it overwhelmingly passed a Transportation Equity Act for the 21st Century (TEA21) reauthorization bill that provides nearly $295 billion in investment for Federal transportation programs, including $53.8 billion for public transportation, through fiscal year 2009.

FISCAL YEAR 2006 GOALS

APTA recognizes the need to wisely invest limited Federal resources and an investment in public transportation is a wise use of limited funds. It is important to maintain and expand the Nation's basic transportation infrastructure, including transit, to meet the public's growing demand for service. In addition to being an important part of our overall surface transportation network, transit investment produces excellent returns and serves national goals by producing jobs and providing more mobility options to all Americans. It improves the environment, reduces dependence on foreign oil, and provides a solid return on the investment by fostering economic growth. According to a Cambridge Systematics Inc. study, for every $10 spent on transit capital projects, $30 in business sales is generated. Every $10 invested in transit operations results in $32 in business sales.

APTA's funding request for FTA programs in fiscal year 2006 is based on APTA's recommendations for reauthorization of TEA21, which were developed over a 2-year period and adopted by APTA's Board of Directors in 2002. Those recommendations proposed funding transit at $10.1 billion in fiscal year 2006. We recognize the constraints that the subcommittee faces, however, and we urge that it fund the transit program at no less than $8.9 billion, which is the level included for the Federal transit program for fiscal year 2006 in the reauthorization bill which the Senate approved this week by a vote of 89–11.

PUBLIC TRANSPORTATION INVESTMENT CREATES JOBS AND KEEPS THE ECONOMY MOVING

Policy makers know that increased investment in our Nation's transportation infrastructure, and especially in public transportation, will help the economy and produce good-paying jobs. Secretary of Transportation Norman Mineta points out that for every $1 billion in Federal highway and transit spending, 47,500 jobs are created or sustained. Investment in public transportation creates jobs that are high-paying, stable, and cannot be exported. These jobs are not just those needed to operate new and expanded transit service, which are significant, but also in the private sector, which has an impact nationwide. For instance, buses are built by Chance Coach in Wichita, KS; Neoplan USA in Lamar, CO; New Flyer in St. Cloud, MN; GILLIG in Hayward, CA; North American Bus Industries in Anniston, AL; Champion Bus in Imlay City, MI; MCI in Pembina, ND; Orion Buses in Oriskany, NY; and the list goes on. Transmissions for many of those buses are built by Allison Transmission of Indianapolis, a General Motors subsidiary. Indeed, the APTA Business Member Board of Governors presented GM Chairman and CEO Rick Wagoner with its Outstanding Business Executive of the Year Award in 2004. In accepting the Award, Mr. Wagoner spoke in support of public transportation, saying, "We have supported a federal transit program because we know that personal vehicles are only part of the solution . . . that a balanced transportation system is the best approach." Engineering services may be provided by Parsons Brinkerhoff Quade and Douglas, and DMJM + Harris or a score of other private sector firms with offices around the country. Opportunities for businesses across America expand when investment in public transportation is increased.

While investment in public transportation is good for the economy, it serves another important economic purpose: alleviating highway congestion. It was reported last year that the cost of congestion exceeds $67 billion annually—including more than 3.6 billion hours of delay and 5.7 billion gallons of excess fuel consumed. The average driver loses more than a week and a half of work (62 hours) each year sitting in gridlock. The average cost of congestion per peak road traveler is $1,160 a year. All of that congestion delays more than 64 percent of the Nation's freight that moves by truck on highways, which represents annual value to the economy of more than $5 trillion. Were it not for public transportation, the Nation would have lost another 1.1 billion hours and $20 billion dollars while stuck in congestion.

Public transportation does not just improve the economy by taking cars off the road—it also provides transportation options to low-income workers who cannot afford to drive to their jobs. According to the Surface Transportation Policy Project (STPP), the proportion of household expenditures devoted to transportation has grown from 14 percent in 1960 to almost 20 percent today. As transportation costs increase, a recently published Bureau of Transportation Statistics (BTS) Issue Brief found that Americans who commute by car or truck spent about $1,280 per year in 1999, while those who were able to use public transportation to get to and from work spent just $765 per year. These costs have risen faster with the recent increase in the cost of gas. Clearly those who need to work the most to provide for their families have much to gain from the savings that public transportation can provide.

PUBLIC TRANSPORTATION IS IN DEMAND

Last November voters in cities across the country, from Phoenix, Austin, San Antonio, and Northern Virginia to Ludington and Kalamazoo, Michigan; and Bend, Oregon voted for new taxes to provide new and expanded public transportation services. These were just a few of the efforts across the country to increase funding for transportation infrastructure, which saw voters approve a strong majority of transit-related referenda. According to the Center for Transportation Excellence (CFTE), of the 28 measures on ballots that included public transportation funding in November 2004, 22 initiatives (worth an estimated total of over $40 billion) were approved.

Eighteen were approved earlier in the year for a total of 40 approved initiatives in 2004. In total, the public voted to support 80 percent of these recent ballot initiatives. This approval rate is being driven in large part by citizen demand for more transportation choices.

That these referenda have been approved by such large margins should come as no surprise. As APTA reported in testimony before this subcommittee last year, polls have consistently shown that the American public supports increased public transportation services and also supports providing the resources to pay for it. A Wirthlin Worldwide poll taken for APTA in 2004 showed that 80 percent of Americans see quality of life benefits from increased investment in public transportation, 76 percent of Americans support public funding for the expansion and improvement of public transportation, and a strong majority of Americans believe transportation investment is preferable to tax cuts to stimulate the economy. These findings hold true across all geographies—urban, suburban, small town and rural residents. Another poll from 2003 by APTA and the American Automobile Association (AAA) showed that 95 percent of Americans said traffic congestion, including commutes to and from work, has grown worse over the last 3 years, and that 92 percent said it was either very important (71 percent) or somewhat important (21 percent) for their community to have both good roads and viable alternatives to driving.

While demand for new and expanded service is increasing, the resources required to simply maintain the present level of service are immense. The Department of Transportation's own 2002 Conditions & Performance Report indicates that an investment level of $75 billion a year is needed for highway and transit capital infrastructure in order to begin to improve the condition of the Nation's highways, bridges, and transit systems.

PUBLIC TRANSPORTATION PROVIDES MOBILITY OPTIONS

Public transportation provides mobility options to persons for whom driving is not an option due either to cost, disability, or other reasons. For many in this population, public transportation may be the only option to living a fully independent and productive life. The affordability of public transportation for low-income workers has been addressed, but for some it is not a problem of affordability but rather ability to drive. For many of these people, public transportation can be the difference between staying in their own homes and moving into an assisted living community.

According to the AARP's Beyond 50.03: A Report to the Nation on Independent Living and Disability, released in August 2003, as people move from their 70's into their 80's, the percentage of licensed drivers falls to 50 percent from just over 90 percent. With the baby-boom generation approaching retirement age, this means the population of elderly Americans who do not have a driver's license will soon pose a serious challenge.

Persons with disabilities face similar mobility problems. Many cannot drive or afford vehicles that are fitted to their needs. Public transportation can provide them the options they need to stay active and independent. However, according to AARP's report, 32 percent of people with disabilities over 65 report that inadequate transportation is a problem. The report goes on to say that while public transportation is more economically efficient in areas with high population density, many older Americans with disabilities live "outside of central cities in communities where public transportation is found least often."

PRESIDENT'S BUDGET PROPOSAL

In February, the Bush Administration released its fiscal year 2006 budget proposal, which recommends a funding level of $7.781 billion for the Federal transit program. Despite proposing an overall cut in non-defense discretionary spending, the administration's public transportation funding proposal represents an increase in investment over fiscal year 2005. This increase for transit investment was accompanied by a recommendation in the budget request for a 6-year funding level for TEA21 reauthorization of $283.9 billion, an increase of $27.9 billion over the administration's proposal last year. The DOT budget release states that this "figure reflects the emerging consensus in Congress that was developed in a conference committee in 2004."

Clearly, the administration understands the value that increased investment in our surface transportation infrastructure, including public transportation, provides to the American people and the role it plays in meeting the important national goals described above. The administration's support for public transportation investment is matched by Congress. The Senate went further towards meeting our transportation needs when it approved, by an 89–11 vote, TEA21 reauthorization legislation that authorizes nearly $295 billion, $11 billion more for Federal transportation programs than the administration proposed.

NEW STARTS APPROVAL PROCESS

The FTA issued a Dear Colleague letter dated March 9, 2005, in which it invited interested parties to comment on a number of issues relating to FTA's New Starts Program by April 1, 2005, including its proposal to no longer consider projects without at least a "medium" cost-effectiveness rating. In a March 31, 2005, comment to FTA on its Dear Colleague letter, APTA opposed changing the cost-effectiveness rating level for project funding recommendations, noting that under Federal transit law and regulation project determinations are to be based on a multiple measure approach in which the merits of candidate projects are to be evaluated on a range of criteria, not just on cost effectiveness. APTA further noted that transit reauthorization legislation now pending in Congress may be enacted soon and would also require revisions to the New Starts program, and thus asked FTA not to proceed with its proposed changes at this time. Finally, APTA expressed support for five other changes proposed by the FTA, some of which the industry had proposed for many years, and looks forward to working with the FTA on their implementation. On April 29, 2005, the FTA issued a Dear Colleague letter on this matter, responding favorably to a number of industry comments but not changing its position regarding projects needing at least a "medium" cost-effectiveness rating for funding decisions.

CONCLUSION

Public transportation can play a key role in meeting the goals of the administration and Congress in providing economic development, energy independence, transportation options for Americans who cannot afford to drive or are not able to, and preserving the environment. To do so will, however, require a commitment on the part of the Federal Government in the form of increased, predictable investment in our Nation's infrastructure.

Mr. Chairman, we look forward to working with the committee as it advances the fiscal year 2006 appropriations bills that deal with national transportation infrastructure needs.

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