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Opportunities to Control Costs and Improve the Effectiveness of Department of Transportation Programs

Statement of

The Honorable Kenneth M. Mead

Inspector General

U.S. Department of Transportation

Chairman Nussle, Ranking Member Spratt, and other members of the Committee,

We appreciate this opportunity to testify today about opportunities to control costs and improve the effectiveness of Department of Transportation (DOT) programs. At this Committee's direction, the Concurrent Resolution on the Budget for Fiscal Year (FY) 2004 requires House and Senate authorizing Committees to identify opportunities to eliminate waste, fraud, and abuse in programs under their jurisdiction. Efforts to combat waste, fraud, and abuse take on even more importance today, when we face significant financial challenges. The Congressional Budget Office recently updated its estimate of the FY 2003 deficit to $400 billion, or close to 4 percent of gross domestic product.

This Committee and the Senate Budget Committee also identified savings targets expected from each authorizing Committee. The target for budget authority that was provided to the House Transportation and Infrastructure Committee totaled $491 million, a little less than 1 percent of DOT's FY 2004 budget request.

This approach calls for the Committees with expertise about specific programs to target waste, fraud, and abuse associated with those programs. DOT, for example, administers several important transportation programs that contribute to meeting national economic, safety, and mobility goals. Overall, DOT's FY 2004 budget request is $54.3 billion, of which $46.2 billion (85 percent) is from DOT trust funds and $8.1 billion (15 percent) is from the General Fund.

We believe the Committee's target of identifying about $500 million in waste, fraud, and abuse in DOT programs is reasonable and can be achieved by implementing administrative and legislative opportunities to (1) improve the efficiency and effectiveness of DOT programs, (2) avoid unnecessary program cost increases, and (3) cut costs and reduce losses to fraud and abuse.

We in the DOT Office of the Inspector General have attempted to do our part to identify program improvements, cost avoidance opportunities, and direct cost savings to reduce program cost growth and ensure that we get the most from our transportation investments. From FY 1997 through the first half of FY 2003, we made over $6 billion in recommendations to put funds to better use, and we have questioned more than $475 million in costs. Our investigators also completed 1,486 convictions and obtained over $260 million in fines, restitutions, and civil judgments—bringing funds back to the U.S. Treasury or to affected programs.

I want to use our time today to focus on opportunities we have identified to use funds more efficiently and effectively, avoid unnecessary cost increases, and reduce costs in (1) Federal Highway Administration (FHWA) and Federal Transit Administration (FTA) grants to States and localities; (2) Federal Aviation

Administration (FAA) operation, maintenance, and acquisition programs; and (3) Maritime Administration's (MARAD) Title XI Loan Guarantee Program. Finally, I will conclude my remarks with a few observations about Amtrak, which presents a different type of challenge because its program structure is fundamentally broken and needs to be rethought.

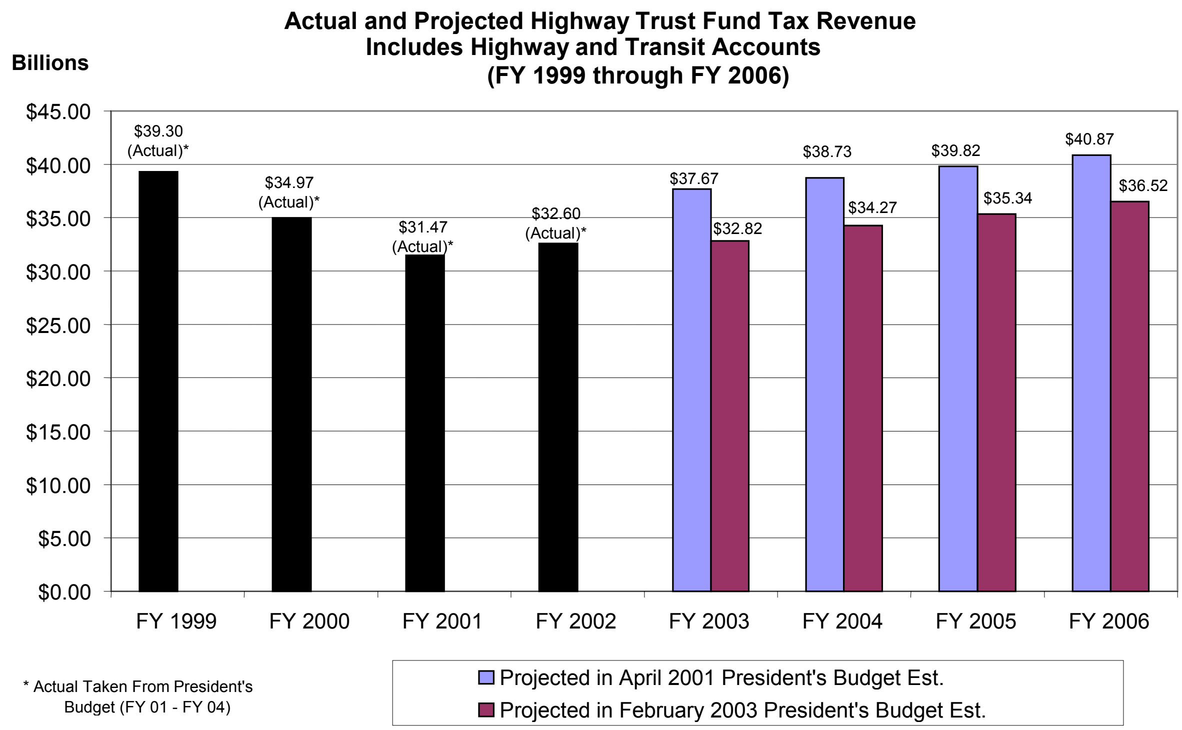
DOT management has been responsive to our recommendations to correct the deficiencies in most of these areas. In particular, Secretary Mineta, Deputy Secretary Jackson, and the Administrators have emphasized the need to improve oversight to get more value from the Federal investment. This has included making tough calls in project funding decisions and proposing significant legislative changes to strengthen stewardship, oversight, and fraud detection and prevention provisions related to highway and transit investments.

FEDERAL HIGHWAY ADMINISTRATION AND FEDERAL TRANSIT ADMINISTRATION

FHWA has requested $30.2 billion (all from the Highway Trust Fund) for grants to states and local governments to build and repair highways and to reduce highway injuries and fatalities. FTA requested $7.2 billion ($5.9 billion from the Highway Trust Fund and $1.3 billion from the General Fund) for grants to transit operators, and to state and local governments for the construction of transit facilities and purchase of transit equipment.

However, Highway Trust Fund tax receipts have fallen from $39.3 billion in FY 1999 to $31.5 billion in FY 2001, a 20 percent decline. Current estimates show that between FY 2003 and FY 2006, Highway Trust Fund tax revenues will be about $18 billion less than projections made in April 2001, and are not expected to return to the FY 1999 level until FY 2008.

Figure 1



Whether funds are lost to cost overruns, schedule delays, or fraud, the result is the same—fewer resources are available for important transportation projects. To illustrate, if the efficiency with which the $500 billion invested by the Federal Government and the states over the last 6 years on highway projects had been improved by only 1 percent, an additional $5 billion would be made available—enough to fund 4 of the 15 active major highway projects.

Although proposals have been made to increase funding for Federal-aid Highways, and these proposals may have merit, we believe considerably more can and should be done to stretch Federal dollars by ensuring that funds are spent cost-effectively. We have identified a number of ways, based on our audits and investigations, that FHWA and FTA could do a better job. These are:

Making Better Use of Available Funds

FHWA must be more vigilant in identifying funds that are no longer needed by states. These funds, sitting idle on inactive projects can be redeployed to fund active projects. We found $238 million in funds that states no longer needed on projects that should have been redirected to other projects. Of this amount, $54 million had been idle for 16 years on a freeway project in Connecticut that had never been started.

Strengthening Project Management

We have reviewed projects in which management and oversight were ineffective, leading to significant cost increases, financing problems, schedule delays, or technical or construction difficulties. These projects include the Central Artery, the Woodrow Wilson Bridge, the Springfield Interchange in Virginia, Puerto Rico's Tren Urbano, the Los Angeles Metro Red Line, and the San Francisco Bay Area Rapid Transit (BART) Airport Extension.

One problem we have repeatedly seen is that cost estimates on major highway and transit projects have been unreliable and have led to substantial cost increases in the long run. For example, we found the Virginia Department of Transportation understated project cost estimates by $236.5 million, or 35 percent, on the Springfield Interchange Project by not including estimates for some known and planned costs. Significant cost estimating problems also occurred on the BART Airport Extension. Our April 2000 report noted that the project's costs had increased by $316 million over the initial cost estimate.

Another problem is that finance plans are not usually required for highway projects under $1 billion, although such projects can also burden a state's management resources. A finance plan is a management tool that is vital in providing project managers and the public with information on how much a project is expected to cost, when it will be completed, whether adequate funding is committed to the project, and whether there are risks to completing the project on time and within budget.

In our opinion, finance plans should be prepared for projects costing $100 million or more, and responsibility for approving those plans should be delegated to the states, with the Secretary reserving the right to review any plan. If the states are going to spend $100 million of taxpayer money, it is reasonable to require them to develop an approved finance plan that identifies project costs, milestones, and funding sources. The Department has incorporated this new requirement in its reauthorization proposal.

Our work has identified two reasons for ineffective oversight of Federal-aid highway projects. First, until recently, FHWA managers rarely focused on program and major project management and financial oversight. FHWA took a partnership approach in exercising its oversight role of Federal-aid Highway projects, with FHWA channeling money for highways to the states and working with state highway personnel to administer highway contracts. This partnership is important, but it is equally important that FHWA be willing to step back and make the hard calls when necessary.

Second, today's highway projects require professional competencies in emerging technologies, financing, cost-estimating, program analysis, environmental processes, and schedule management. Yet, FHWA's expertise in these areas is severely limited because its workforce is structured almost exclusively around engineering skills that were in greater demand during construction of the interstate system. FHWA should restructure its staffing mix to bring the right set of skills to bear on oversight activities.

Detecting and Preventing Fraud

During the last 4½ years highway and transit-related fraud indictments have tripled, convictions have doubled, and monetary recoveries totaled more than $80 million. We currently have over 100 ongoing investigations of infrastructure projects or contracts. Fraud schemes that we are commonly seeing today include bid-rigging and collusion among contractors; false claims for work or materials not provided on the project; product substitution by contractors or vendors who provide substandard or inferior materials; bribery of inspectors to look the other way on their duty to ensure quality of work or materials; failure by contractors to pay workers required prevailing wages; and fraud against the Disadvantaged Business Enterprise (DBE) Program for minority and women contractors who are used as "false front" companies.

DBE fraud is an area with serious enforcement and compliance problems that requires more attention and appears to be nationwide in scope. In an effort to protect the Government's interest against fraud on transportation projects we recommended the Department adopt language in its highway reauthorization proposal to make debarment mandatory and final when a contractor is convicted of a fraud. In addition, since state programs are the ones damaged by fraud, allowing states to share in any recoveries would help them restore their programs and provide support for further fraud deterrence and detection efforts.

Increasing Revenue Collections

Fuel tax fraud drains the Highway Trust Fund of an estimated $1 billon annually, which can be mitigated with strengthened enforcement and investigative efforts to increase tax collections. Cross-border bootlegging of fuel and diversion of aviation "jet" fuel are two areas needing further attention. Federal and state legislative changes could facilitate more effective tax collections and investigations.

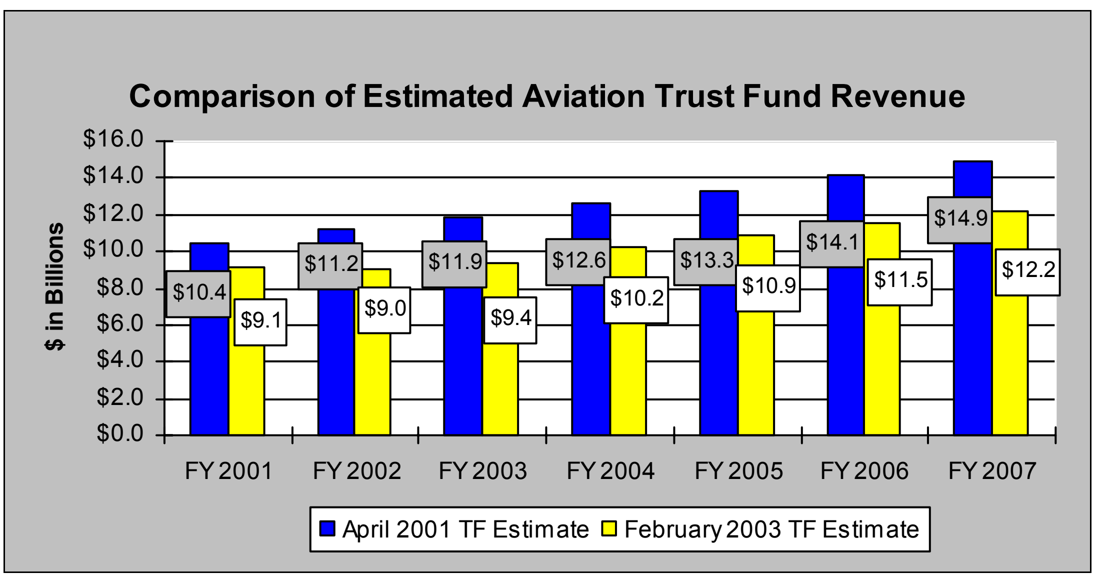
FEDERAL AVIATION ADMINISTRATION

In 1996, Congress acted to make FAA a performance-based organization by giving the Agency two powerful tools–personnel reform and acquisition reform.

The expectation was that, by being relieved of Government personnel and procurement rules, FAA would operate more like a business—that is, services would be provided to users cost effectively and air traffic control modernization programs would be delivered approximately on time and within budget.

Seven years later, FAA's budget has grown from $8.2 billion in FY 1996 to $14 billion in FY 2004–an increase of $5.8 billion, or over 70 percent. About half of that increase was attributable to FAA's operating budget. During this period, we have also seen large cost overruns and schedule slips in FAA's major acquisitions. Continued growth of that magnitude is unsustainable, given the multibillion-dollar declines in projected Aviation Trust Fund receipts and greater dependence of FAA on the General Fund. In fact, projected tax receipts to the Aviation Trust Fund for FY 2004 have dropped from approximately $12.6 billion estimated in April 2001 to about $10.2 billion estimated in February 2003. Over the next 4 years (FY 2004 through FY 2007), Aviation Trust Fund tax revenues are expected to be about $10 billion less than projections made in April 2001.

Figure 2



We see three areas based on our audits and criminal investigations that need to be addressed to ensure that Federal funds are spent cost-effectively.

FAA's Spiraling Operating Costs Are Unsustainable and Need to Be Brought Under Control

To date, the most visible results of personnel reform are increased workforce costs. While there has been improved labor/management relations with controllers (FAA's largest workforce), FAA's operating costs, which are primarily payroll, have increased by $3 billion, going from $4.6 billion in FY 1996 to $7.6 billion in FY 2004—an increase of over 65 percent.

The new pay system for controllers was a significant cost driver. Between 1998 (when the new system was implemented) and 2003, the average base pay for controllers increased from $72,000 to over $106,000—a 47 percent increase. This compares to an average salary increase for all other FAA employees during the same period of about 32 percent. Additionally, although linking pay and performance was a key tenet of personnel reform, only about 36 percent of FAA employees receive pay increases based on individual performance. The remainder of FAA employees receives largely automatic pay increases.

We also found that there are somewhere between 1,000 and 1,500 side bar agreements or Memorandums of Understanding (MOUs) that FAA managers entered into. These agreements cover a wide range of issues such as implementing new technology, changes in working conditions, and—as a result of personnel reform—compensation, bonuses, and benefits.
While many of the agreements serve legitimate purposes, we found some that had significant cost and/or operational impacts on FAA. For example, as part of a new pay system for controllers, FAA and the National Air Traffic Controllers Association (NATCA) entered into a national MOU providing controllers with an additional cost-of-living adjustment. As a result, at 111 locations, controllers receive between 1 and 10 percent in "Controller Incentive Pay," which is in addition to Government-wide locality pay. In FY 2002, the total cost for this additional pay was about $27 million.

Despite the cost implications, at the time of our review FAA management did not know the exact number or nature of these agreements, there were no established procedures for approving MOUs, and their cost impact on the budget had not been analyzed. Because of the significant control weaknesses, we briefed the FAA Administrator about our concerns in January 2003—2 months after initiating this review. FAA has moved expeditiously to address this issue, including identifying those MOUs that are problematic or costly and opening discussions with NATCA to reopen several agreements.

To effectively control costs, FAA needs accurate cost accounting and labor distribution systems. In 1996, Congress also directed FAA to have a fully functioning cost accounting system so it, as well as others, could know exactly where its costs were. Now, after nearly 7 years of development and over

$38 million, FAA still does not have an adequate cost accounting system, and it expects to spend at least another $7 million to deploy the cost accounting system throughout FAA. In our opinion, the principle reason that FAA does not have an effective cost accounting system is because it has not experienced any consequences for not having one. FAA also has not been held accountable to operate like a business, which must be able to identify costs by specific services, activities, and locations to support management decision-making.

To have an effective cost accounting system, FAA also needs an accurate labor distribution system. Cru-X is the labor distribution system FAA chose to track hours worked by air traffic employees. As designed, Cru-X could have provided credible workforce data for addressing controller concerns about staffing shortages, related overtime expenditures, and how many controllers are needed and where. That information, in turn, is especially important, given projections of pending controller retirements. Unfortunately, Cru-X has not been implemented as it was designed.

Given the fiscal constraints facing FAA, the availability of critical, reliable, and competent data to make informed decisions about the Agency's basic day-to-day operations must be an imperative for FAA. FAA needs to redouble its efforts to have a fully functional cost accounting and labor distribution system in place and operating. We are encouraged by FAA's response to our June 3, 2003 assessment of its cost accounting system, in which the Agency agreed to have both its cost accounting and labor distribution systems in place and operating by September 30, 2004.

FAA also needs to look at existing opportunities to reduce costs. For example, we estimate FAA could realize cost savings of nearly $500 million over 7 years by reducing the number of existing automated flight service stations by over half in conjunction with deployment of new flight service software. We also identified that FAA could save over $57 million annually by expanding the contract tower program to 71 visual flight rule towers still operated by FAA. Clearly, these actions are controversial among certain groups; however, given the current fiscal issues facing FAA, the Agency needs to objectively consider these and other cost saving measures from a business perspective.

FAA's Major Acquisitions Continue to Experience Large Cost Increases, Extended Schedule Delays, and Performance Problems

In terms of acquisition reform, FAA has made progress in reducing the time it takes to award contracts, but the Agency has not held managers accountable or used the benefits of acquisition reform to control cost and schedule slips. We found that cost growth, schedule delays, and performance problems continue with

FAA's major acquisitions. Overall, the 20 projects we reviewed have experienced cost growth of about $4.3 billion (from $6.8 billion to $11.1 billion) and schedule slips of 1 to 7 years.

Billion-dollar cost growth with acquisitions is not sustainable or affordable in light of declining Trust Fund revenues. Moreover, FAA is just starting complex, billion-dollar efforts while continuing to fund projects that have been delayed for several years. If FAA does not exercise more management control over its acquisitions, existing projects will be delayed further, and new projects may not start as planned.

FAA must take a number of steps to control costs of acquisitions and get as much as it can with each acquisition dollar. We recommended FAA update the cost, schedule, and performance baselines for many of its major acquisitions. Those baselines are misleading because they do not accurately reflect the true cost, schedule, or performance parameters of the projects. This process may require FAA to establish a new strategy that accelerates some projects and defers others.

FAA Needs to Strengthen Controls Over Programs That Have Been Susceptible to Fraud, Waste, and Abuse

Our work has also found that FAA has not followed sound business practices for administering contracts. We have consistently found a lack of basic contract administration at every stage of contract management, from contract award to contract closeout. For example, we found that Government cost estimates were prepared by FAA engineers, then ignored; prepared using unreliable resource and cost data; prepared by the contractor (a direct conflict of interest); or not prepared at all. To protect the Government's interests, FAA needs to hold managers accountable and adhere to the basic principles of contract oversight and administration.

We also found that FAA's Workers' Compensation Program continues to be subject to fraud and abuse, in terms of both stress-related claims and long-term injury claims. For example, we investigated one case of an FAA employee who received over $397,000 in workers' compensation claims over a 5-year period after allegedly falling out of a chair and injuring his back. While receiving those benefits, the individual obtained a pilot's license and was employed as a pilot at various organizations.

Workers' Compensation is also an area that could benefit from Government-wide improvements. One issue we previously identified is the number of claimants who continue to receive workers' compensation benefits long after they are eligible to receive retirement benefits. For example, in 2001 for FAA alone, there were nearly 1,500 claimants over the age of 60 who were still receiving workers' compensation benefits. In fact, there were 218 claimants still receiving workers' compensation benefits who were 80 years old or older.

Converting claimants from workers' compensation benefits to retirement benefits after they reach retirement age could result in significant savings Government-wide. However, changes of this magnitude would clearly require legislative actions.

Lastly, FAA needs to remain vigilant in its oversight of airport revenue diversions. Airports that receive Federal grants are required to put any revenue generated at the airport back into the airport operating or capital funds in order to minimize Federal assistance. Any other use of the revenue is considered a diversion. Examples of common revenue diversions include airport sponsors or local governments (1) charging the airport for property or services that were not provided, or (2) renting airport property at less than fair market value.

At a time when airports are continuing to look for new ways to fund their operations, we continue to find cases of airport revenue diversion. For example, at a sample of five airport sponsors reviewed, we found approximately $40.9 million in potential revenue diversions that were not detected by FAA's primary oversight methods. Since we completed our fieldwork, the American Institute of Certified Public Accountants and FAA have taken steps to better inform independent auditors about requirements for reviewing airport revenue use during single audits.

In our opinion, those actions should improve FAA's ability to detect and prevent airport revenue diversions. However, to ensure that revenue diversions that occurred are resolved, FAA needs to verify the status of the $40.9 million in potential revenue diversions that we identified and seek recoveries as necessary.

MARAD

In the last 5 years, MARAD's Title XI Loan Guarantee Program has experienced an increase in loan defaults and in the number of firms with loan guarantees filing for bankruptcy protection. Since 1998, nine loans have defaulted, totaling approximately $490 million, six of which have occurred since December 2001. The bankruptcy of one firm affected over one quarter ($1.3 billion out of $4.9 billion at the time of default) of the value of MARAD's Title XI loan guarantee portfolio.

MARAD needs to improve administration and oversight in all phases of the Title XI loan process. During a recent audit, we identified a number of areas where MARAD could improve its Program practices, limit the risk of default, and reduce losses to the Government. For instance, in approving applications, MARAD agreed to waivers and modifications to Program financial requirements without adequate compensating provisions to reflect the increased risk to the Government. MARAD also lacked a formal process for closely monitoring the financial condition of borrowers and did not systematically monitor the physical condition of guaranteed assets.

We also note that Public Law 108-11, *Making Emergency Wartime Supplemental Appropriations for the Fiscal Year Ending September 30, 2003,* appropriated $25 million to MARAD for new loan guarantees. Before these funds can be obligated (these funds would likely guarantee loans with a face value of about $400 million), the law mandates that MARAD implement the recommendations in our report and that we certify to the Congress that our recommendations have been met. We are working with MARAD to analyze the new processes that it has proposed putting in place, and we will audit MARAD's compliance with the new processes once they are in use.

AMTRAK

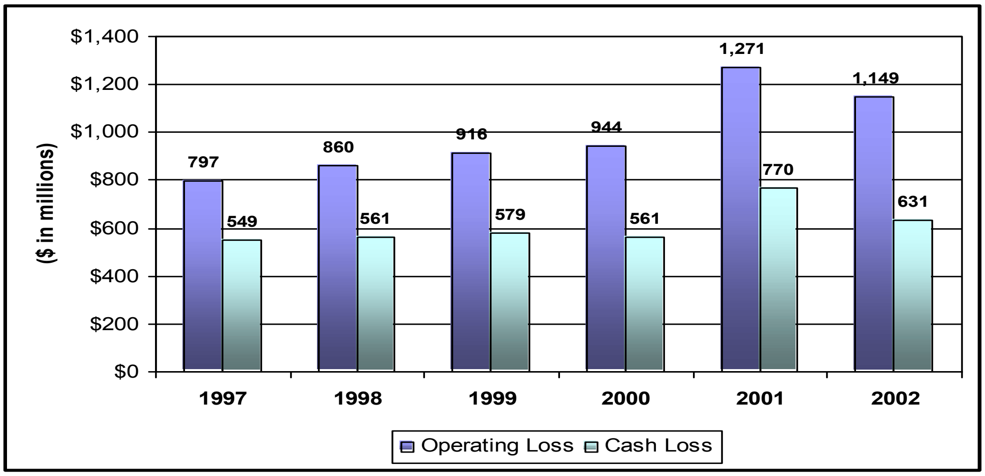
We are including a brief discussion of Amtrak because even Federal funding levels of $1 billion a year are not going to solve the fundamental problem: the current Amtrak model is broken. The problem extends beyond funding to questions of who makes the decisions about and who controls the provision of service, including commuter service. The status quo pleases no one; it will require significant increases in funding just to maintain it; and it will not meet the mobility needs of this country in the years ahead.

Although Amtrak has received about $1 billion in annual Federal assistance during the past 6 years, the general state of Amtrak's infrastructure and rolling stock continue to deteriorate. Amtrak's deferred capital investment is estimated at about $6 billion. Except for a handful of routes, the system continues to suffer operating losses on all services offered. In fact, the fully allocated losses on some trains (including depreciation and interest) can exceed $500 per passenger. For the company as a whole, annual cash operating losses have averaged $600 million for the last 6 years and are estimated to range between $700 million and $800 million over the next 5 years.

Figure 3

Growth in Amtrak's Operating and Cash Losses,

1997 Through 2002



Amtrak has requested $1.8 billion for FY 2004 in order to begin to address the capital backlog and to cover its large cash operating losses. The Administration has requested $900 million for Amtrak for FY 2004.

That concludes my statement, Mr. Chairman. I would be pleased to address any questions you or members of the Committee might have.