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Withdrawal/Redaction Sheet (George Bush Library)

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01. List	Re: Privatization Council: Vice President Meeting List; birthdates and Social Security numbers redacted. (3 pp.)	n.d.	(b)(6)	

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Collection:

Record Group: Quayle Vice Presidential Records
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APRIL 16, 1990

Forbes

Faces Behind the Figures

Paul Fetters



Consultant John Stainback

Public projects, private financing.

Private party

How will the U.S. find the money to fix its aging roads and bridges and water lines? John Stainback, 41, thinks he has an answer, and it shows in the name of his Washington, D.C.-based consulting firm, Privatization International.

Stainback explains: "I come in, identify a municipality's assets and teach them how to leverage the hell out of 'em."

In the past two years, Stainback has advised on the financing and construction of some \$2 billion of municipal projects. Examples: the new \$125 million U.S. Judiciary Office Building in Washington, a \$30 million library in San Antonio and the \$51 million expansion of West Point's Hotel Thayer.

Say a city wants to build a new police station on municipal property. Stainback arranges for the city to enter a joint development agreement with a private real estate firm and commit to a long-term lease on the proposed structure. This reduces the developer's risk and helps him get financing at a good rate. Thus, the city can be saved a possibly painful trip to the bond market.

Of course, taxpayers must foot the rental bills, but the bills are stretched over a long period of time and scarcely noticeable.—Gretchen Morgenson

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CRAIN'S NEW YORK BUSINESS

AUGUST 26, 1991

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Privatization now a cottage industry

But is there money to be made?

BY MARCIA PARKER

CRAIN'S NEW YORK BUSINESS

Embarking on a \$1 billion rebuilding program it knows it can't finance, the U.S. Military Academy at West Point is considering privatizing as many of its operations as it can to save money.

West Point is working from a list of 113 possibilities—including its hotel, athletic facilities and parcels of real estate—that were identified by Privatization International Inc., a Manhattan consulting firm.

"We think privatization makes sense," says Lt. Col. Richard Ashley, the academy's project coordinator and long-range planning chief.

So does Privatization International, only one of scores of companies creating a cottage industry in Manhattan and elsewhere to serve a growing number of public- and private-sector converts.

Financially squeezed state and local governments around the nation, and even in New York, are debating whether turning over public facilities, infrastructure and services to private corporations can stretch hard-pressed budgets. In response dozens of consultants, law firms, accounting firms, investment banks, foundations and think tanks are cashing in on the privatization drive.

"A lot of people have jumped on the bandwagon," says John Stainback, president of Privatization International.

But as is the case with Western companies flocking to Eastern Europe, success is far from assured. One problem is how governments will pay for advisers.

"It's hard for many governments to justify the money they spend to hire a privatization adviser when they are laying off people," says Mr. Stainback.

Nevertheless, consultants abound like Kenneth Gibson, Newark's former mayor. "With the economy in recession, many businesses that would not normally chase public-sector work do now," Mr. Gibson

(Continued on Page 38)

John Stainback, president and chief executive of Privatization International Inc.



SHERIE NICKOL

Many companies see a future in privatization

adds. He recently was hired by his first public-sector client, the Irvington, N.J., Board of Education, which is studying privatization plans to build and maintain schools. Hill International Inc., a Willingboro, N.J.-based construction consultant, is selling a privatization computer model to municipalities including New York.

The Big Six accounting firms, including Ernst & Young and Price Waterhouse, also have thriving privatization practices. At Ernst & Young the focus is on environmental applications such as private companies running waste water treatment facilities. Price Waterhouse is concentrating on privatization opportunities in the transportation field.

Law firms like Skadden Arps Slate Meagher & Flom also claim their expertise is in great demand as complex contracts are drawn up to govern the ventures. Skadden has 15 to 20 lawyers who specialize in corporate, real estate, public finance, and tax issues focused on privatization, says Karen Hedlund, a partner who heads up the group and Skadden's public finance group.

Some of the most ambitious efforts are at investment banks, including Morgan Stanley & Co., Goldman, Sachs & Co., and Smith Barney, Harris Upham & Co.

Goldman Sachs set up a privatization group last winter and

business has been picking up steadily. Smith Barney just hired Michael Basham, former deputy assistant secretary for federal finance at the U.S. Treasury Department, for its operation.

Earlier this year, Smith Barney executives met with dozens of state and local government officials throughout the country. "That led us to believe there's a business to be built," says Frank Zarb, Smith Barney's chairman. "I'll let you know in a year if it's profitable."

Privatization no cure-all

He also says advisers have to be careful not to offer up privatization as a cure-all for budgetary problems. "There are only some cases where public-sector assets will perform better outside of government than inside. These assignments are fraught with economic, political and labor implications," Mr. Zarb adds.

But special groups are not the only approach. Morgan Stanley opted against setting up a separate privatization group, instead drawing on the expertise of the whole firm to work on privatization projects. "We don't want to separate the skills our bankers use in the private and public sector," says Managing Director Elaine La Roche.

Morgan Stanley and Privatization International recently arranged a joint venture to acquire

public-sector sports and entertainment complexes around the country.

Even non-profit groups like the Empire Foundation for Policy Research and the Rockefeller Foundation are studying what role they can play in the privatization drive. The Empire Foundation is preparing a study on privatization opportunities in New York state, where privatization is off to a slow start.

"There are substantial privatization opportunities in New York. The economics are clear. What we have lacked is a certain amount of political will," says Thomas Rhodes, a Goldman, Sachs & Co. partner who is chairman of the Empire Foundation, a two-month-old Albany think tank.

Some players that might not be expected to join the privatization crusade are also getting involved. R. Theodore Ammon, a partner with Kohlberg Kravis Roberts & Co., the highly regarded Manhattan buyout firm, is pondering ways to adapt corporate restructuring skills for the privatization programs being hailed as a way to revive the hobbled public sector.

Mr. Stainback says he's working with a Fortune 500 company he can't identify that has decided to be among the first to commit seed money to public-sector privatization projects.

Like all new ventures, this one might not prove lucrative.

Governments leery

Many municipalities are wary of privatization as a panacea for their financial troubles and so they are moving slowly to do more than study the options.

Governments also fear running afoul of unions and other groups who oppose privatization and believe the private sector won't do any better than the public sector has.

"For some people privatization still conjures up the government selling the Grand Canyon," says Jenny Hefferon, executive director of the Privatization Council in Washington, which promotes public-private partnerships.

And while more than 100 people in New York now call themselves privatization experts, the more cautious admit it's hard to drum up interest.

"Interest is growing, but it's not an influx," says George Raftelis, director of Ernst & Young's national environmental consulting practice.

Finally, whether there is big money to be made is unclear. Privatization International is considering splitting its operation into two. One part would advise clients for relatively modest fees while the other would actually manage privatization projects for larger fees.

"Privatization wasn't a household word five years ago, but it is today," says Mr. Stainback. ■

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PRINCETON, NEW JERSEY

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ENTERPRISE

Privatization Lets Small Firms Manage Everything From Libraries to Golf Courses

By EUGENE CARLSON

Staff Reporter of THE WALL STREET JOURNAL

To sports fans, the U.S. Military Academy's Michie Stadium at West Point, N.Y., is hallowed ground, encrusted with the deeds of football legends Glenn Davis, Doc Blanchard, Col. Red Blaik and generations of Army teams.

But to consultant John Stainback, the stadium is an opportunity for the Army and small businesses such as his to profit from a wave of the times: privatizing government operations. "It's a great stadium operating at half-speed," Mr. Stainback says. "The concessions and parking are inadequate. There are no luxury seats." His four-person company, Privatization International in New York, has a contract to advise the military academy on how to make or save money on a variety of West Point facilities. His basic strategy: Let private entrepreneurs run the show.

Privatization — turning functions or property in the government's domain over to private management or ownership—is in transition. The once-radical idea that private business can manage prisons and pick up garbage is now commonplace, with both large and small companies as major players. But privatization is moving into whole new areas, from managing libraries, municipal golf courses and military airfields to helping bring free enterprise to government operations in Eastern Europe.

Small companies get a big slice of these operations, such as service jobs that federal agencies contract out to private businesses. "It's very much an entrepreneurial market," says Ronald Utt, a vice president of the U.S. Chamber of Commerce and a former associate director for privatization in the Reagan administration.

President Reagan was a big fan of privatization. He even talked about turning

U.S. Privatization Projects

Some recent government service contracts won by private firms

- Seattle solid-waste recycling (Recycle America Inc., Seattle, and Recycle Seattle Inc., Seattle.)
- Starr County, Texas, jail (Pricor Inc., Murfreesboro, Tenn.)
- 21% of Denver transit system (Mayflower Contract Services Inc., Overland Park, Kan.; Laidlaw Transit Inc., Toronto; and ATC Management Corp., St. Louis.)
- Veterans Administration mail services (DDD Co., Landover, Md.)

Some privately owned infrastructure projects finished or under way

- Dulles International Airport toll road (Toll Road Corp. of Virginia, Leesburg, Va.)
- U.S. Supreme Court office building, Washington, D.C. (Boston Properties Inc., Boston)
- Sludge composting plant, Springfield, Mass. (Resource Control Inc., Barre, Mass.)
- Solid waste to energy plant, Dakota County, Minn. (ABB Resource Recovery Systems, Windsor, Conn.)

over the Postal Service and some air-traffic control centers to private operators. But Congress didn't agree, and the Bush administration hasn't pushed the issue.

Nevertheless, the concept is flowering among U.S. entrepreneurs, even without active White House support.

—American Golf Corp., Santa Monica, Calif., operates about 80 public golf courses in 20 states. The company, which also manages private courses, just signed up four municipal courses in Detroit. "It's difficult for governments to run golf courses profitably," says Ron Johnson, American Golf's president.

—Aspen Systems Inc., Rockville, Md., manages libraries at the U.S. Department of Housing and Urban Development, the Labor Department, the Interior Department and the National Oceanic and Atmospheric Administration. The company also runs clearinghouses for outsiders who need

information from the agencies.

—With privatization in full swing in Eastern Europe, Michael Sumichrast, an economist in Washington, D.C., has cornered a handful of consulting contracts for projects in his native Czechoslovakia, including the privatization of state-owned automobile and munitions factories. "The opportunities are absolutely staggering, if you know what you're doing and if you're serious about staying there for the long haul," says Mr. Sumichrast.

—Centre Management in Landover, Md., has taken over management of civic arenas in Baltimore and Springfield, Mass. In two years under private management, Baltimore's city arena swung from a \$1.2 million operating deficit to a modest profit, the company says.

—Dynamic Science Inc., based in Phoenix, Ariz., has weapons-testing contracts
Please Turn to Page B2, Column 3

ENTERPRISE

Privatization Lets Firms Manage Range of Facilities

Continued From Page B1

for the Defense Department and runs a small Army airfield in Aberdeen, Md. Its employees there staff the control tower and service airplanes and helicopters, among other tasks.

—DDD Co., Landover, Md., has grown from start-up to a \$10 million company in nine years with a series of low-tech government contracts under a federal program designed to encourage privatization. DDD staffs mail rooms for the State Department, the Justice Department and the Transportation Department. It also fills orders from aviators and sailors for government aeronautical and nautical charts.

"Privatization has created intense competition, and you have to bid very lean to win these contracts," says John Mattingly, DDD's chief financial officer.

Unions argue that much of the cost benefits stem from replacing government employees. Ralph Rockow, president of Dynamic Science, concedes that the savings business brings to labor-intensive government operations stem largely from lower employee overhead. Private workers tend to get less in costly benefits than government workers, and "you can hire and fire without going through a lot of bureaucratic problems," he says. "It's a positive for the taxpayer, but a negative for the government employees you're displacing."

Mr. Utt, the former Reagan administration official, says much of the resistance to privatization stems from an "elitist attitude" that governs the idea of turning over government jobs to private business. "If something is done by poorly educated people, nobody seems to mind if it's contracted out" to business, he says. "But once you get into white-collar jobs, they become inherently governmental."

Nevertheless, increasing interest

prompted Mr. Stainback in the past year to create his company, which advises governments on how to privatize. At West Point, Privatization International is receiving \$160,000 to suggest innovative ways to use the academy's assets, says Lt. Col. Richard Ashley, the academy's chief of long-range planning. The company could also earn management fees worth roughly 3% of the cost of any new projects. "We gave him a laundry list of all the assets that might have some value," Col. Ashley says. "It's kind of open-ended."

The 42-year-old Mr. Stainback, who started his career as an architect and urban planner in Philadelphia, says he might turn to an arena-management company to increase revenue at Michie Stadium. "Running a sports facility requires a certain entrepreneurial flair," he says. "If a stadium is running at 60% of capacity, a good marketer can fill it up."

Privatizing Michie Stadium alone could bring the military academy an extra \$1.5 million to \$2 million a year, he says, from increased attendance, a busier schedule, and higher charges for everything from parking to popcorn. Mr. Stainback also has his eye on Eisenhower Hall, a performing arts center, and 640 acres of Army-owned land off the academy grounds. A needed new science classroom building could be financed with savings and new revenues from privatization projects, he suggests. Mr. Stainback says the design, finance and construction portions of these projects could well be handled by small firms.

As a potential model for some of the West Point projects, Mr. Stainback points to a \$127 million office building now under construction on Capitol Hill for the U.S. Supreme Court. Rather than following its customary practice of renting space in privately owned buildings, the federal govern-

ment leased a parcel of its own land to a private developer, **Boston Properties Inc.** of Boston.

Boston Properties obtained private financing, coordinated design and construction and will lease the building's 650,000 square feet back to the government for 30 years at a fixed annual rent. At that point, the government will own the building. In the meantime, the landlord has a dependable tenant, and the government doesn't have to pay a big chunk of money up front or act as property manager.

Mr. Stainback is focusing his privatization guns on property development. "The U.S. government owns \$1.4 trillion of real estate, and in my opinion, most of it is tremendously underutilized," he says. Cities are another target. They own buildings and vacant lots, he says, "and half the time they don't even have an inventory."

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NO MORE NICE GUISE

Monday: Clouds increase; 60s
Tuesday: Could rain; around 60
High tide: 12 a.m., 12:33 p.m.
Full report: Page 34

MONDAY, APRIL 29, 1991

'Privatization' would be far-reaching

Weld plan for companies to take over programs could reshape government

By Scot Lehigh
GLOBE STAFF

If Gov. Weld pursues "privatization" plans currently under consideration within the administration, Massachusetts state government would undergo a radical transformation, with private companies taking over dozens of functions now performed by traditional governmental bureaucracies.

State parks would be privately managed, state prisons privately run, the state's roads privately maintained and plowed, and court fees would be privately collected. It is possible that the Massachusetts Bay Transportation Authority and Logan Airport could be run by private firms.

Those and other privatization possibilities are contained in an internal planning document obtained by the Globe last week.

Asked about the document last week, Mark Robinson, Weld's chief of staff, called it "a first step toward what Gov. Weld meant by smaller government doing fewer things better," but said more extensive study will have to be done before any final decisions are made about which functions to try to privatize.

Still, Robinson said he thinks the administration will end up pushing many of the proposals, most of which would require enabling legislation.

"I think you will see a number of these ideas become reality," he said. "The governor and lieutenant governor want to change the face of state government and not just to downsize but also to make it better and more efficient."

Chief Secretary John Moffitt, the point man on the privatization project, said Weld would be "looking at all that and more. I think there are substantial areas in government that could be privatized to the benefit of

the taxpayer."

The idea behind privatization is that the private sector can more efficiently provide many services now performed by the state. In a time of strapped revenues, privatization holds the prospect of saving tax dollars or providing more services for the same amount of money.

A survey done by Mercer Group, an Atlanta-based management consulting firm, shows that other areas have been pleased with their experiments with privatization. That survey found that 97 percent of the cities and 99 percent of counties that had tried privatization liked the results. All the government entities surveyed reported savings, while 45 percent thought the quality of the work was significantly improved.

If Weld decides to privatize some state functions, he can count on opposition from public employee unions, based on other states' experiences. He may also face opposition from a Legislature reluctant to give up control.

But if he succeeds, he will preside over a dramatically altered government.

Some of the biggest changes would take place in the Department of Correction, where the state would seek private companies to run "prison operations and maintenance" and provide inmate health care. Private operators would also be sought for the corrections boot camp Weld has talked about establishing for some juvenile offenders. The juvenile detention centers currently operated by the Department of Health and Human Services would also be privatized, as would the management of state hospital inventory.

The Department of Labor's employment and training functions would be privatized, and the Industrial Accidents Board, which reviews

worker compensation claims, would have its arbitration functions and penalty collections contracted out. In the area of the environment, private companies would take over management of state parks and recreation facilities, fine and fee collections, and some training functions.

Court fees would be privately collected, while private firms, rather than the Board of Bar Overseers, would be responsible for administering the bar exam. The Massachusetts Health and Educational Facilities Authority be authorized to float bonds for scholarship funds.

Gathering momentum

Under a category of "additional privatization possibilities," the document lists general possibilities for privatization that would mean even larger changes. That list includes "airports, rail lines, convention centers, recreation facilities, seaports, waste disposal plants, and incinerators."

Specific facilities are not singled out in the document, but Robinson acknowledged the administration will explore privatizing the MBTA and commuter rail systems, as well as the Massachusetts Port Authority.

The administration's list touches on an especially wide array of government functions, but the direction is one any number of state and local governments are pursuing.

"We are definitely seeing a trend toward privatization in a major way," said Jack Nicholson, special industry consultant for Arthur D. Little Inc., the Cambridge-based consulting firm. "It is driven by the need for more efficient use of the money and increased specialization in the industries affected."

Based on a preliminary study

done by Arthur D. Little, Nicholson said he expects the number of privatized functions will triple by the end of the decade.

Nicholson, whose recommendations 15 years ago resulted in Louisiana turning the Superdome over to private management, said that usual targets for privatization are "things that generate revenue easily: sports arenas, space centers, golf courses."

Tougher tasks

But other efforts have gone further. According to a 1991 report on privatization by Reason Foundation of Santa Monica, Calif., states have turned over prisons, roads, and social service programs to private companies to run.

That report says that 11 states, led by Florida, Tennessee, and Texas, now have privately run jails or prisons. "At least three of the privately operated facilities are maximum-security institutions, debunking the perception that the private sector only takes on easy, low-risk jobs," the report says.

Dr. Keon Chi, a senior fellow at the Council for State Governments in Lexington, Ky., says the experience of turning prisons over to private management has basically been positive. "In some cases you can find some problems, but despite the rhetoric from opponents, in my opinion privatization has been used very successfully," Chi said.

More and more, privatization involves functions once thought to be part of government's core responsibilities. For example, John Stainback, president of Privatization International, a New York City firm that specializes in privatization, is

currently working on a plan under which a private firm would build a \$60 million toll road linking four Mississippi communities to the Jackson International Airport.

"Most governments really cannot afford to maintain the needed public facilities and services and infrastructure, and at the same time, they can't continue to raise taxes," Stainback said. "That can't always be the answer. So we believe that privatization is the answer."

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JACK NICHOLSON
*Special industry consultant,
Arthur D. Little Inc.*

E.S. Savas, chairman of the management department at the City University of New York, Baruch College, and an acknowledged expert on privatization, says a well-designed privatization program cuts costs by infusing former public-sector functions with private-sector incentives.

"Competition versus monopoly"

"The great advantage of privatization is that when it is done right you introduce competition, and that is the best and most proven way of improving the delivery of government services," Savas said.

Moffitt echoes those sentiments. "The issue is not public versus private," he says. "It is competition versus monopoly."

Savas says privatized government functions result in average costs savings of about 25 percent "for the same level and quality of services."

But that hardly means Weld can expect whatever proposals he makes to breeze through the Legislature without a fight. The Reason Foundation study found that public employee unions' objections are a significant barrier to taking functions private, while Chi says a governor proposing privatization programs can expect opposition from those fearing loss of jobs and loss of state control.

"The biggest opponents are public employee unions, who unnecessarily fear loss of jobs and elimination of unions," Savas said. "But that is not the case at all." In most cases he has studied, Savas says, wages were not cut and in some cases the private firm actually paid more than the public sector.

Although work forces in privatized areas were generally smaller, that diminution was usually achieved through attrition rather than large layoffs. All that leads Savas to conclude that "the concern about job loss is exaggerated."

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Privatization Is the Answer, but There Is No Free Lunch

John P. Stainback

Through privatization — the full or partial transfer of selected government responsibilities to the private sector — financing strategies can be designed to meet the public's need for services, new or renovated facilities, and infrastructure.

Governments worldwide are seeking to structure public/private finance and development plans to meet the enormous need to rehabilitate or replace public facilities and infrastructure. While privatization can carry tremendous advantages — indeed, it may be the only way many public needs can be met — the approach is frequently misunderstood, and the amount of government effort it requires is frequently underestimated.

John P. Stainback is a privatization consultant based in Washington, D.C. He is past President and CEO of Privatization Development of America, Inc., which is in Houston, and has worked on projects in conjunction with the Architect of the Capitol, the U. S. Navy, U. S. Army at West Point, the Baltimore District of the Army, and the U. S. Air Force, and with states and cities as well. Mr. Stainback has recently been appointed to the Board of Directors of The Privatization Council, a nonprofit industry organization headquartered in Washington, D. C.

A Confluence of Trends

Why is the privatization approach being used more and more in America and overseas? Over the last 10 to 15 years there has been a confluence of several "big picture" trends that have led to privatization. For example, there is an increasing need to rehabilitate, replace, or build new public facilities and infrastructure, and to build new facilities to meet the population growth. Yet, at the same time, there is a decreasing amount of government funds available to finance these facilities and infrastructure, and a decreasing tolerance among taxpayers to increase taxes. There is also an increasing realization on the part of many governments worldwide that they should not own and/or operate certain types of facilities and infrastructure.

The cost of private finance for privatization proj-

ects is decreasing, to the point where it has become competitive with the cost of public finance. Finally, the number of successful privatization projects is increasing, which raises the confidence of the public and private sectors in using the approach.

Some of these trends have been evolving over the last few decades, while others have emerged only in the last few years. Combined, they create an integral basis for government decision-making, creating a strong impetus toward privatization.

Privatization Defined

Simply stated, privatization is the full or partial transfer of selected government responsibilities to the private sector. These responsibilities include financing, design, construction, and operation of public facilities and infrastructure, as well as required public services. Today various levels of government find themselves in the role of developer and/or operator of public facilities and infrastructure. In most instances they should not be in the development or operations business. The privatization of selected facilities and services allows governments to better focus on their primary responsibilities.

There are four types of privatization:

□ *Privatization development.* The public/private finance and development of stand-alone public facilities, or public facilities within an otherwise private mixed-use development, or the private development of government-owned land in trade for a needed public facility or economic return. Stand-alone public buildings include facilities such as airports, prisons, hospitals, and schools. Public facilities that could be incorporated into a private, mixed-use development include: stadiums, arenas, convention centers, convention hotels, libraries, low-to-moderate income housing, etc.

□ *Privatization of services.* There are two types of government services that can be privatized: government operation and management of public facilities such as airports, stadiums, prisons, and services provided to the public, such as garbage collection and roadway maintenance.

□ *Privatization of infrastructure.* The infrastructure of America and most foreign governments has been badly neglected over the last decade. Infrastructure includes transportation systems, roadways,

bridges, water-treatment plants, and energy plants.

□ *Privatization of industry.* Many governments in the United States and overseas own and operate corporations and businesses which could possibly be better operated by that portion of the private sector which specializes in facility operation and management. Governments should structure the disposition of these corporations so as to participate in the upside of the companies' profits but not be burdened with ownership and daily operation.

There are several types of public facilities and infrastructure that are financed, designed, developed, constructed, and operated by private sector teams specifically tailored to meet all of the requirements of the facility or service, from project conception to daily management and operation.

Why Governments Use Privatization

To elaborate on the influences described above, there are specific economic and political forces at work that motivate governments to turn to privatization, or public/private joint ventures, to obtain needed facilities and improvements.

Economic Necessity

From the government's perspective, the most basic economic reason to use a public/private approach is a lack of funds. Governments simply do not have the funds in place, or the bonding capacity required, to finance fully all the public facilities, public services, and infrastructure they must provide.

In the United States, funds for the rehabilitation and replacement of facilities and infrastructure is woefully inadequate at all levels of government, from the federal level to local governments. At the local level, there are also a multitude of nonprofit and community groups that need funds. Combining public and private resources allows governments the opportunity to structure financing strategies to meet all of their public facility and infrastructure needs, and to meet them now. Other economic motivations might include:

- Distributing or spreading the cost of needed public facilities among applicable government agencies, the private developer, concerned private corporations, businesses, individuals, and citizens

- who want a specific facility in their community;
- Leveraging available public funds and real estate assets; and
- Creating a new long-term source of income for the government *from* the project, either by capturing the increased value of adjacent land, which results from the new development; or, by participating in the profits of private development associated with the new facility. In addition, some public facilities, such as new sports and entertainment arenas and convention centers, will create a multiplier effect: they generate new jobs and income to be expended throughout the economy, which, in turn, generate increases in tax revenues, property values, etc.

Profiting from Underutilized Real Estate

Most governments own an extensive amount of real estate. In some cases, the government owns a large amount of real estate that is perceived by the private market as extremely valuable. In others, the amount of publicly owned real estate is not extensive, but the location of the assets give them a high market value. This real estate is often vacant or terribly underutilized.

These assets could be leveraged as part of a public/private development solicitation, and then sold, groundleased, or swapped to help achieve capital building and improvement goals. A prime example of a government agency that is beginning to leverage its enormous real estate assets is the United States Postal Services (USPS). *Privatization Toward More Effective Government*, prepared by then-President Reagan's Commission on Privatization, estimated that USPS owned land holdings with a fair market value (FMV) exceeding \$3.6 billion as of 1984. Even that figure may be too low; the report goes on to state that "the FMV is still likely to be understated because it is based only on average asset-specific indices."

Governments are beginning to structure public/private development projects in which well-located, publically owned land is swapped to a private development team, which must then finance, design, develop and construct a needed public facility. Many governments built public facilities decades earlier in the original center of a city. The city has now grown up around these aging facilities, making the market value of these core sites extremely high. Governments need to assess whether these key facilities

could be located elsewhere on less valuable land or whether they could increase the building density of these sites. Depending on the land value, development market conditions and the structure of the public/private deal, the proceeds from the sale or groundleasing of the land could be used to partially finance a new facility elsewhere.

These are a few of the multitude of ways to use government-owned real estate. The major point here is that all levels of government can better use their underutilized or dormant land as a means of supplementing available public finance, or in combination with private sector resources, to build public facilities and infrastructure, or possibly to finance needed public service programs.

□ *Using the private sector as a joint venture partner.* Contrary to belief, the private sector is not necessarily better or faster at financing, building, or managing. Private developers simply are not burdened with the layers of government procedures, number of public participants, or the schedule requirements of many governments. Nor do they have the government's obligation to serve the public regardless of cost. For example, it would be difficult, if not impossible, to operate a typical transit system at a profit; the required passenger cost would eliminate most of the ridership — especially those in greatest need of the service. The private sector, on the other hand, is driven by profits. The responsibility of private developers is to get the project at hand completed faster and cheaper than their competition.

The private development industry is a prime example of a potentially advantageous joint venture partner for the government. Over the last few decades developers have become very proficient at financing, designing, developing, and constructing such facilities as office buildings and hotels. Governments should combine forces with private development teams to build government office buildings or convention hotels.

Joining forces with private developers at this time is particularly advantageous for both the government and developers. The speculative office building market in most cities is tremendously overbuilt. Moreover, private lenders want to place funds they have in hand which previously were allocated to this market. If the government would simply provide the required land and commit to a long-term office space

lease, a public/private joint venture could be formed to use the resources of the private sector in financing and developing the new city halls and other government office spaces that are so desperately needed worldwide.

Enhancing the Political Environment

When governments have to increase taxes or ask citizens to approve going deeper into debt in order to build a needed facility, most political environments can become quite volatile. This is particularly true if citizens do not perceive the facility to be critically important to the daily operation of their government, *e.g.*, a stadium or arena. Privatization is an effective means to build needed facilities in this political environment. In fact, if a public/private development is properly structured, the government sponsor can obtain the needed building and be perceived as creative, resourceful, and sensitive to the taxpayer's desire to reduce government costs.

A Combination of Reasons to Use Privatization

One of the most exciting aspects of privatization and the public/private development approach is that in many instances all of the reasons described in this section apply.

In other words, if government would work in partnership with the private sector, the two partners could combine forces to finance and build needed facilities by using excess government-owned real estate. By using underutilized assets and, therefore, not spending scarce funds, privatization can not only provide needed facilities, but also enhance voters' perception of government officials. After all, these government officials have met the public's need by using excess government-owned assets or assets previously unrecognized for their current market value.

Benefits to Private Developers and Lenders

Privatization and the public/private joint venture approach are emerging as long-term solutions, because the private sector has just as much to gain as does the public sector. If the partnership is well structured, both parties can benefit from this approach.

There are four primary reasons the private sector is actively pursuing and participating in privatiza-

tion. First, pre-development, development, and operational costs are significantly reduced, delayed, or eliminated. Second, project risk is significantly reduced.

Also, the development team forms a cooperative and constructive relationship with the public sector instead of an adversarial one. This allows a forum for the full utilization of available sources of public finance, public finance instruments, development incentives, and other ways governments can facilitate projects.

Finally, the private sector can participate in high-profile, civic-minded projects, and can create facilities that are desperately needed, but unlikely to be wholly financed with limited public funds.

Significant Cost Reductions

The feasibility and economic return of most privatization projects, be they public facilities, infrastructure, or services can be greatly enhanced by combining government assets and private specialization. If the partnership between the private and public sectors is well structured, the government, the developer, and the operator can reduce project costs in all phases of the project.

Pre-development costs such as the following can be reduced, delayed, or in some instances, eliminated:

- Costs to assemble land parcels for a project site are often eliminated.
- The cost of the land itself is typically delayed through a groundlease, or provided at a nominal cost.
- The cost of pre-development studies is often shared.
- Acquisition/disposition regulatory fees are sometimes waived.
- Utility "hook-up" costs are shared or eliminated for the private sector.

In the development phase, costs are often reduced or eliminated. The cost of finance is reduced by managing risk through long-term leases, agreements, or guarantees provided by the government. Leasing and marketing costs are substantially reduced because the government serves as the sole or anchor tenant. Furthermore, the development costs are often distributed to all of the parties benefiting from

the project or services, thereby reducing the cost to each participant.

Operational costs are also reduced by the government's involvement. Taxes are usually reduced or abated. The governments may also share in the required maintenance of the project, or assist with the cost of such maintenance. For example, maintenance of the "public space," or common area of a project, is often the government's responsibility. Also, the government will often assume responsibility for marketing costs over the life of the project.

Project Risk is Significantly Reduced

It is very difficult to manage risk in the current private speculative development market. Most privatization developments and infrastructure projects incorporate a user of part, or 100 percent of the product. If the public facility being privatized is part of a larger development, it can allow the private development team to enter into a new market with a more comfortable level of risk. For example, if the needed public facility is an administrative office building, the government could be the "anchor tenant" for two-thirds of the building and the remaining one-third of the building could be speculative space. The cash flow from the government office lease will serve to cover the debt service on the **entire** building, assuming the public/private split of cost, responsibilities and risk is well balanced.

Forming a More Cooperative and Constructive Relationship with Government

Many governments and private sector builders simply tolerate each other during the typical project approval process.

The government is typically skeptical of the private developer's methodology and motives. On the other hand, many developers perceive governments as multi-layered bureaucracies that only impede the development process. The public/private partnership approach has proved to be a forum for the public and private sectors to work together more effectively and more efficiently.

Instead of the typical adversarial relationship, the two parties establish a mutual trust to form an effective working partnership. The proposition, "United We Stand, Divided We Fall" is surely true in the privatization and public/private partnership approach to financing and developing projects.

At the Urban Land Institute 1989 Fall Conference in New York City, a California developer described how he had tried for years to build the first truly mixed-use development policies to the Mayor's office. The Mayor quickly adopted these policies. The developer, who had been struggling with his innovative mixed-use project for several years, received approval in *less than a week* after the policy was adopted. Working in partnership with the government could have saved years of frustration for the developer.

Public/private development projects provide the basis for the government to work closely with the private sector. This more cooperative working environment allows both parties to structure a fair and reasonable split of costs, risk, and responsibilities, which in turn allows innovative breakthroughs in finance, design, and construction, as well as a reduction in the time required to complete the project.

If the public and private sectors are in partnership to achieve a common objective, there is a greater likelihood that a full range of options for achieving that goal will remain open. There are hundreds of incentives, financing techniques, and sources of funds that can be used to structure a mutually beneficial deal between the public and private sectors. In most instances, when the private sector perceives the public sector partner to be cooperative and willing to share costs or save time, the private sector will reciprocate.

The Private Sector's Attraction to Public Projects

For most private developers and leaders, one of the major motivations for participating in the privatization process, besides making a profit, is simply to do good. Developers want to be part of the continued effort to create a better society.

In many instances, the public/private partnership approach is the only way certain public facilities will be built. Developers can use their creativity to bring about projects that are desperately needed, but unlikely to be built using a traditional approach.

These types of facilities include low profit margin, or non-revenue generating facilities, such as low- to moderate-income housing, elderly housing, community service facilities such as libraries or child care facilities, convention centers, and the rehabilitation of historic structures.

In addition to non-revenue generating facilities or those that typically operate at a deficit, there are public facilities that are high-profile projects. These are typically one-of-a-kind facilities for a city, county, or state government. They include central government office buildings, sports and entertainment arenas, stadiums, convention hotels, and mixed-use developments undertaken to rejuvenate a city's downtown or a government's capitol area. Because most of these projects are large in scope and require complex financing and development experience, they often require combining the strengths of the government and a private sector team that specializes in building these facilities.

Successful Privatization Requires an Enormous Pre-Development Effort

Privatization can be enormously beneficial to both the government (public sponsor) and the private sector. But privatization is complex. It requires intensive management, political aplomb, and stamina. In addition, both the public and private participants will have to resolve many issues and complete a multitude of tasks. Most of these tasks have to be completed simultaneously and early in the process in order to achieve an integrated and comprehensive resolution.

There is substantial effort required, from both parties, throughout the term of the project. However, the public sponsor is more likely to underestimate the effort it must expend, viewing the process as simply "turning over" a service or facility to the private sector. Also, the government's actions in the pre-development phase set the stage for the rest of the project. Accordingly, we focus on the public sponsor's pre-development role below.

The Public Sponsor Needs to Resolve Key Policy Issues

The public sponsor needs to resolve several key policy issues to establish the framework for the privatization process. These policies will lay the foundation for important features of the privatization process, such as the relationship between the public sponsor and the private sector team. Is the sponsor going to treat the private sector as a vendor, or as a partner? How aggressive is the public sponsor going to be throughout the process? These policies will also

determine what the public sponsor will provide the private sector and what the private sector will expect in return.

☐ *The interrelationship of the public and private sectors.* The sponsor has to come to grips with what kind of relationship is desired with the private sector. The spectrum of relationships between the two parties can range from a client-vendor or "arms length" relationship to a genuine partnership arrangement where both parties share costs, risk, and project responsibilities.

☐ *The level of commitment.* The government must be willing to commit any and all of its resources to creating the project. Most governments have limited funds to invest in a project, so government equity is assumed to be minimal. The government's willingness to supplement equity participation, if any, with sufficient financial and development incentives to attract the private sector is essential to the success of the privatization approach. The government sponsor has to develop a consensus among its decision-makers to share project risks, costs, and responsibilities with the private sector team.

☐ *Political support for the project.* Government sponsors must obtain sufficient political support to deliver the equity and/or incentives required to attract the private sector to the project. The majority of government participants, and, in some cases, a majority of the voters, must support proceeding with the project.

☐ *Expectations.* The leader, or key members of the public sponsor, have to temper unreasonably high expectations of privatization. This is particularly important for weak public/private project offerings. The sponsor has to be responsive to the strengths or weaknesses of a privatization solicitation; otherwise, all interaction with the private sector team will be adversely affected. Equally important, the credibility of the public sponsor will be in question.

Key Tasks to Be Completed

In addition to resolving key policy issues, there are a multitude of tasks to be completed by the public sponsor in the pre-development phase, such as the following.

☐ *Select a project manager.* The public sponsor needs to identify a person to lead government participants and orchestrate project activities. This person can be a member of the government staff or the private sector. He or she must be well-respected

by government colleagues and, ideally, by key members of the private sector. In addition, the project manager must have the authority to make decisions, select consultants, and control the project schedule.

☐ *Gain a consensus on privatization objectives.* The project manager needs to understand the objectives of key members of the public sponsor, document those objectives, and gain a consensus as to their priority of importance.

☐ *Understand the general value of the privatization offering.* The project manager needs to work with government staff and/or advisors to determine the perceived value of the offering from the private sector's perspective. Is the offering strong enough to attract the private sector? This will greatly affect the primary basis for structuring the solicitation.

☐ *Understand the value of government assets.* The public sponsor working with an advisor must determine what assets and incentives are needed to be incorporated into an offering. Once the needed number, type, and magnitude of assets and incentives are resolved, the general value of each must be determined.

Relationships and Balance

In order to execute a successful privatization project, two major features must be addressed: the relationship between the government and the private sector, and the balance of six primary project variables.

The Public and Private Sectors Must Create a Genuine Partnership

Both the public and private sectors must realize that in order to execute privatization, both need to treat each other as partners. If the government views the private sector as a means to that elusive free lunch, the privatization or public/private joint venture will collapse. In order to gain the full benefit of privatization, both parties need to think and work in tandem. If the government pushes all of the risk onto the private sector, the cost of private finance will increase significantly. On the other hand, if the private sector team requires too much of the government, key government participants and/or the voters

will view the project as a give-away for the private sector to enjoy.

Balancing the Project Variables

A fundamental principal of privatization, and especially the public/private joint venture approach, is for both the public sponsor and the private sector to bring something to the table. There are six key variables used to structure a public/private deal — project risk, project cost, project responsibility, economic return, project control, and a reasonable project schedule — and both parties have to realize that any one of these variables can kill the deal. Maintaining a balance requires each party to walk a fine line; an objective, third-party advisor is sometimes needed.

Each of the key variables has a multitude of subvariables, which can be fine-tuned to meet the needs and objectives of each party and maintain the needed balance. If one party wants to minimize its level of risk but is willing to, say, increase its project responsibilities, that imbalance could be balanced by the other four variables to structure a "doable deal."

Conclusion

There is a tremendous need for governments throughout the world to finance and develop public facilities and infrastructure, as well as to provide needed public services. Privatization is the answer to meet these worldwide needs, and offers benefits to the private sector as well.

There is a wide spectrum from which to establish a working relationship between government and the private sector. These were previously described as ranging from the arms-length client-vendor relationship to a genuine partnership. The author is convinced the partnership approach results in the best public/private deal structures.

Consequently, if the public sponsor and the private sector can work as a partnership to balance project risks, costs, responsibilities, controls, economic return, and a reasonable schedule, governments worldwide can work with the private sector to finance and implement any — indeed, possibly all — of the needed public facilities, infrastructure, and public services.

October 1, 1990

Pensions & Investments

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PRIVATIZATION

Investors, governments may 'marry'

■ Privatization might become the next hot investment area.

State and local governments need cash to rebuild their ailing infrastructures while Eastern European countries hunger for outside capital to reconstruct their sagging economies.

U.S. infrastructure needs alone are expected to cost between \$1 trillion and \$3 trillion during the next 20 years, while the total U.S. public works budget for 1989 was only \$95 million, said John Stainback, president and chief executive officer of Privatization International Inc., a new advisory firm.

The firm wants to marry governmental financing needs with institutional investors' sizable assets, Mr. Stainback said.

The Washington-based firm hopes to aid governments spin off public services and operations in a variety of public-private partnerships: helping to sell off state-owned enterprises, developing real estate, rebuilding the nation's infrastructure and providing pub-

lic services, such as waste collection.

Therein lies a great opportunity for institutional investors, who can take advantage of inefficiencies in the market, he said. His firm plans to develop a family of funds to invest in privatization opportunities. Public pension funds, already pressured to promote local development, could be natural investors.

Deals would be structured much like leveraged buy-outs, with several tiers of financing.

Privatization International has been named adviser to the U.S. Military Academy at West Point, N.Y., on restructuring its real estate assets to help finance a \$500 million building project. West Point, which owns raw land along the Hudson River, is \$300 million short of its financing needs.

The firm also is negotiating with the County of Albany, N.Y., for the lease/acquisition of the 18,500-seat, \$76 million Knickerbocker Arena.

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Please send
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✓ per 3 speech
writers

File privatization

Document Originally
Attached to
Following Page

J. P. GIRAUDO

5/13

Dear Richard

Many thanks for your help with the executive order and for the kind referrals. I think the order presents a golden opportunity to build a privatization policy for the inner cities. The City of Los Angeles owns four airports, a port, a water system and an electric utility. It ought to be possible for the City now to privatize these assets and utilize the proceeds to create a "Rebuild Los Angeles Fund" which could make loans to businesses destroyed by the riots. I outline the idea in a speech I gave Friday.

11 MAY 1992

But again, John

IS PRIVATIZATION A SOLUTION TO THE URBAN CRISIS?

BY JOHN P. GIRAUDO

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Commission on Privatization and a lawyer in
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May 8, 1992

IS PRIVATIZATION A SOLUTION TO THE URBAN CRISIS?

"THE LIGHTS ARE MUCH BRIGHTER THERE, YOU CAN FORGET ALL YOUR TROUBLES, FORGET ALL YOUR CARES, AND GO DOWNTOWN. . ."

FOR THOSE OF US WHO CAN REMEMBER, THAT WAS 1964 AND PETULA CLARK. THE LIGHTS DOWNTOWN ARE EVEN BRIGHTER NOW. LAST WEEK THEY WERE BURNING VERY BRIGHT -- AUGMENTED BY FIRES.

WE CAN'T SEEM TO FORGET ALL OUR TROUBLES ANYMORE. OR FORGET ALL OUR CARES. CERTAINLY NOT DOWNTOWN.

PERHAPS IF IT WERE POSSIBLE WE WOULD LIKE TO GO BACK TO 1964. MAYBE EVEN 1954. THE SUCCESS OF THE MOVIE BACK TO THE FUTURE SEEMED TO STEM IN LARGE PART FROM A NOSTALGIA ABOUT LESS COMPLICATED TIMES. CHILDHOOD FOR MOST OF US WAS AN ARMORIAL AGE. THE MUSIC WAS BETTER. THE KIDS BETTER BEHAVED.

UNFORTUNATELY, MR. PEABODY'S WAY BACK MACHINE DOESN'T WORK ANYMORE. WE ARE STUCK IN THE FUTURE. AND THE FUTURE REGRETTABLY IS NOW.

THE TITLE OF MY TALK THIS MORNING ASKS A QUESTION: IS PRIVATIZATION A SOLUTION TO THE INFRASTRUCTURE CRISIS? IN VIEW OF THE RECENT EVENTS IN OUR COUNTRY I

WOULD LIKE TO INVOKE A SLIGHTLY BIGGER THEME: IS PRIVATIZATION A SOLUTION TO THE CRISIS IN OUR CITIES?

I BELIEVE IT IS. PRIVATIZATION IS NOT A PANACEA AS MANY OF ITS CRITICS SAY. IT IS NOT A PANACEA. IT IS A SOLUTION. IT MAY BE THE ONLY ONE WE HAVE LEFT.

TO PARAPHRASE A PHILOSOPHER, THE QUESTION IS NOT SO MUCH "IS GOD DEAD?" BUT, FOR THOSE OF US LESS ONTOLOGICALLY INCLINED "IS GOVERNMENT DEAD?"

AS THE EVENTS OF LAST WEEK UNFOLDED ON OUR TV SCREENS THE ANSWER MUST SEEM TO BE YES.

OUR SCHOOLS ARE THE WORST IN THE DEVELOPED WORLD -- BOTH THE STUDENTS AND THE BUILDINGS. OUR BRIDGES ARE FALLING DOWN. OUR SEWERS ARE BACKING UP. AND WHEN THEY ARE NOT BACKING UP, THE RIVERS FLOW OUT OF THEM INTO THE STREETS. OUR PRISONS ARE OVERCROWDED. OUR STREETS FULL OF HOLES. ONCE PROUD CITIES AND STATES TEETER ON THE EDGE OF BANKRUPTCY.

FOR ANYONE WHO TRAVELS EXTENSIVELY OVERSEAS, PARTS OF AMERICA SURELY RESEMBLE THE THIRD WORLD.

CONFIDENCE IN GOVERNMENT AT ALL LEVELS IN AMERICA HAS FALLEN TO RECORD LOWS. ONLY FIVE PERCENT OF AMERICANS SURVEYED SAY THEY WOULD CHOOSE A CAREER IN GOVERNMENT. WHY SHOULD THEY? OUR CITIES AND STATES ARE

LAYING OFF THOUSANDS OF PUBLIC EMPLOYEES. THOSE THAT REMAIN DON'T SEEM TO CARE MUCH ABOUT THE REST OF US.

THE EASTERN BLOC IS NO MORE. BUT THE NEW YORK BLOC STILL REIGNS. IF YOU DOUBT ME, TAKE A MORNING OFF AND GO GET YOUR DRIVERS LICENSE RENEWED FROM THE DEPARTMENT OF MOTOR VEHICLES. I RECENTLY HAD THIS EXPERIENCE IN THE DISTRICT OF COLUMBIA. THREE HOURS AND FOUR LINES LATER YOU WILL HAVE IT, AND YOUR PHOTOGRAPH WILL LOOK LIKE IT WAS TAKEN OFF OF THE REFLECTION OF A DENTED HUB CAP. SOVIET AGRICULTURE WORKS MUCH THE SAME WAY.

MORE DANGEROUS IS THE INEPTITUDE OF GOVERNMENT. REPORTS HAVE IT THAT THE LAPD WAS SLOW TO RESPOND LAST WEEK. THAT THE NATIONAL GUARD COULD NOT DEPLOY BECAUSE IT LACKED EQUIPMENT. THAT FIRE TRUCKS BROKE DOWN. SOME HAD TO BE TOWED TO THE FIRES.

THROUGHOUT THIS RECESSION OUR POLITICAL LEADERS HAVE DEBATED THE SAME OLD OPTIONS: FEWER SERVICES OR HIGHER TAXES. WE HAVE GOTTEN BOTH.

AS A RESULT, PUBLIC ANGER ALTERNATES WITH APATHY.

WE HOPE THAT EASTERN EUROPE AND THE SOVIET REPUBLICS MIGHT SUCCESSFULLY THROW OFF THE DEADENING HAND OF BUREAUCRACY AND OPPRESSION. BUT AT HOME WE FEEL HELPLESS.

OUR CITIES SUCCUMB TO CRIME AND POVERTY AND COURT ANARCHY AND LAWLESSNESS. OUR STATES ARE HANDCUFFED BY FISCAL CRISES. AND WASHINGTON -- IMMOBILIZED BY A \$ 350 BILLION DEFICIT OF ITS OWN -- DRIFTS THROUGH IT ALL LIKE 30 SQUARE MILES OF DISNEYLAND BOUNDED BY REALITY.

PERESTROIKA, MY FRIENDS, IS WHAT IS REQUIRED HERE AT HOME, NOT JUST OVERSEAS.

THE TIME HAS COME FOR AN AMERICAN PERESTROIKA. I DON'T KNOW THE RUSSIAN WORD FOR IT, BUT IN ENGLISH THE WORD IS: PRIVATIZATION.

SOCIALISM DIED IN THE SOVIET UNION ON DECEMBER 31, 1990 WHEN THE HAMMER AND SICKLE WERE TAKEN DOWN FROM THE RAMPARTS OF THE KREMLIN. BUT IT LIVES ON IN CITIES AND STATES ACROSS AMERICA.

MUNICIPAL SOCIALISM IN AMERICA PREDATED THE SOVIET ONE BY SEVERAL YEARS. LIKE THE SOVIET KIND IT SPRANG FROM THE SAME WELL-SPRING OF IDEALISM WHICH HELD SWAY AT THE TURN OF THE CENTURY.

AMERICA HAD ERUPTED IN AN EXPLOSION OF CAPITALISM WHICH TRANSFORMED THE FACE OF THE NATION IN THE SECOND HALF OF THE 19TH CENTURY. NO NATION HAS COME CLOSE TO THAT RECORD OF ECONOMIC EXPANSION.

BUT WITH THAT RAPID INDUSTRIALIZATION CAME PROBLEMS. EXPLOITATION BY THE PRIVATE SECTOR. CORRUP-

TION IN THE PUBLIC SECTOR. THE ROBBER BARONS AND BOSS TWEED MADE COMMON ALLIES AND COMMON ENEMIES.

SO THE PROGRESSIVE ERA SWEEPED ACROSS AMERICAN GOVERNMENT. IT REPLACED PATRONAGE WITH CIVIL SERVICE. TO KEEP ESSENTIAL SERVICES OUT OF THE HANDS OF MISCREANTS, IT CREATED PUBLIC BOARDS AND AUTHORITIES TO RUN THE SEWERS, THE RESERVOIRS AND THE BRIDGES AND ROADS. EVEN TEDDY ROOSEVELT -- ONE OF MY HEROS -- GAVE BUREAUCRACY A RESPECTABLE NAME.

THIS WAS A WORLD WIDE PHENOMENON. AS MAX WEBER, THE GERMAN SOCIOLOGIST, PUT IT: "THE DECISIVE REASON FOR THE ADVANCE OF BUREAUCRATIC ORGANIZATION HAS ALWAYS BEEN ITS PURELY TECHNICAL SUPERIORITY OVER ANY OTHER FORM OF ORGANIZATION." LEWIS MULFORD MAY HAVE BEEN THE FATHER OF THE MODERN CITY. BUT NORMAN THOMAS WAS ITS POLITICAL HEIR.

BUREAUCRACY CAME OF AGE AFTER THE FIRST WORLD WAR. FUELED IN LARGE MEASURE NOT MERELY BY THE PROGRESSIVE MOVEMENT BUT BY THE GOOD INTENTIONS OF UNCLE SAM.

IT IS NOT WIDELY REMEMBERED, BUT IN THE LAST CENTURY MOST CITY SERVICES IN THE UNITED STATES WERE PRIVATELY PROVIDED -- FROM TRASH COLLECTION TO FIRE PROTECTION.

THE TURNPIKES, THE ROADS AND CANALS WERE, AS THEY ARE TODAY, THE THOROUGHFARES TO NEW MARKETS. THE ONLY DIFFERENCE IS THAT THEY WERE UNDER PRIVATE OWNERSHIP. EVEN IN THIS CENTURY, THE FIRST COMMERCIAL SERVICE AIRPORT, WHICH OPENED IN COLLEGE PARK, MARYLAND IN 1909 WAS A PRIVATE VENTURE SPONSORED, IN PART, BY THE WRIGHT BROTHERS. SIMILARLY, WATER AND SEWER SYSTEMS WERE BUILT, OWNED AND OPERATED BY PRIVATE COMPANIES. THE SAME IS TRUE OF HOUSING.

THAT ALL CHANGED WITH THE COMMENCEMENT OF THE FEDERAL GRANT PROGRAMS FOR INFRASTRUCTURE DEVELOPMENT. THE SIXTEENTH AMENDMENT TO THE CONSTITUTION IN 1913 (TO PERMIT A FEDERAL INCOME TAX) GAVE THE FEDERAL GOVERNMENT A SOURCE OF REVENUE WHICH WOULD, IN TIME, DWARF EVERY OTHER POSSIBLE SOURCE OF REVENUE IN THE COUNTRY. IT PRODUCED MORE MONEY THAN THE FEDERAL GOVERNMENT ALONE COULD SPEND. FEDERAL GRANT PROGRAMS WERE DEVISED AS THE MEANS OF SHARING THAT MONEY WITH CITIES AND STATES.

BEGINNING IN 1916 WITH THE FEDERAL AID TO ROADS ACT, THE FEDERAL GRANT PROGRAMS TODAY AMOUNT TO \$112 BILLION ANNUALLY, HALF OF WHICH IS FOR INFRASTRUCTURE. THE PERNICIOUS PROBLEM HAS NOT BEEN THE SUBSIDIES OR EVEN THEIR SIZE. ONE COULD MAKE THE ARGUMENT THAT THE MONEY

HAS NOT BEEN ENOUGH. THE PROBLEM HAS BEEN THEIR BENEFICIARIES.

UNTIL RECENTLY, IN FACT, UNTIL LAST NOVEMBER WITH THE PASSAGE OF THE INTERMODAL SURFACE TRANSPORTATION EFFICIENCY ACT OF 1991, FEDERAL GRANT MONEY WITH RARE EXCEPTION WENT EXCLUSIVELY TO STATE AND LOCAL GOVERNMENTS FOR THE CONSTRUCTION OF GOVERNMENT-OWNED FACILITIES. IN OTHER WORDS, IT HAS GONE TO SUBSIDIZE MUNICIPAL SOCIALISM. LENIN HIMSELF COULD NOT HAVE PLANNED THE REVOLUTION BETTER. THE PRIVATE SECTOR, UNABLE TO COMPETE WITH FREE FEDERAL MONEY, WAS WIPED OUT OF THE INFRASTRUCTURE BUSINESS. ONLY GOVERNMENTS HAVE REMAINED TO PROVIDE MONOPOLY SERVICES.

WE'VE ALL SEEN THE CONSEQUENCES. CITY AND STATE GOVERNMENTS HAVE ERECTED COMMAND AND CONTROL ECONOMIES WHICH ARE MORE EASTERN THAN WESTERN IN THEIR RESPONSIVENESS TO THE PUBLIC WEAL AND, LIKE THEIR COUNTERPARTS IN LATIN AMERICA, THEY'VE TURNED OUR INNER CITIES INTO POCKETS OF THE THIRD WORLD -- AND TOO OFTEN LINED THE POCKETS OF THE WRONG PEOPLE.

MERCIFULLY, THE CYCLE MAY BE REVERSING ITSELF. BECAUSE THE FEDERAL GOVERNMENT HAS RUN OUT OF GRANT MONEY. THE MONEY MACHINE CREATED BY THE FEDERAL INCOME TAX

HAS GROUND TO A HALT. AND THAT, I CONTEND, IS A SILVER LINING IN THE CLOUD WHICH HANGS OVER OUR NATION.

CITY AND STATE GOVERNMENTS ARE BANKRUPT. THE RIOTS IN LOS ANGELES HAVE GIVEN THAT CONCLUSION A MORAL DIMENSION AS WELL AS A FISCAL ONE.

WHEN THEY BECOME BANKRUPT, GOVERNMENTS DO NOT GO INTO RECEIVERSHIP LIKE ORDINARY BUSINESSES. THEY ARE NOT LIQUIDATED WITH THEIR ASSETS RETURNED TO THE SHAREHOLDERS. THEY ARE SIMPLY AND SADLY IGNORED. IF THE BANKRUPTCY GOES ON LONG ENOUGH, THEY ARE DEFIED -- WITH DANGEROUS CONSEQUENCES.

THIS VERY THREAT OF BANKRUPTCY WHICH THREATENS CITY LIFE ALL ACROSS AMERICA MAY HAVE A BENEFICIAL EFFECT. WITH THEIR BACKS UP AGAINST THE WALL, CITY AND STATE GOVERNMENTS HAVE NO CHOICE BUT TO BECOME MORE RESOURCEFUL.

MORE TAXATION WILL NOT SAVE THEM. NEITHER WILL MORE FEDERAL MONEY. BUT MORE ENTREPRENEURSHIP MAY.

I AM NOT ALONE IN BELIEVING THIS. A RECENT BOOK, REINVENTING GOVERNMENT, CHRONICLES THE REVOLUTIONARY CHANGES ALREADY TAKING PLACE ACROSS AMERICA. DAVID OSBORNE, A DEMOCRAT AND TED GAEBLER, A REPUBLICAN, OFFER NOTHING LESS THAN A LIBERATION THEOLOGY. JUST LISTEN TO SOME OF THE BOOK'S CHAPTER HEADINGS:

- *COMMUNITY-OWNED GOVERNMENT
- *COMPETITIVE GOVERNMENT
- *MISSION-DRIVEN GOVERNMENT
- *MARKET-ORIENTED GOVERNMENT
- *DECENTRALIZED GOVERNMENT
- *ENTERPRISING GOVERNMENT
- *CATALYTIC GOVERNMENT

IN A WORD: PRIVATIZED GOVERNMENT. GOVERNMENT WHERE THE PEOPLE TAKE BACK CITY HALL. GOVERNMENT WHERE THE PUBLIC ARE REAL OWNERS, NOT THE SHADOW OWNERS OF STATE ENTERPRISES, AS THEY HAVE BEEN IN EASTERN EUROPE AND THE SOVIET UNION.

AN AMERICAN PERESTROIKA, LIKE THE ONE ABROAD, MUST INCLUDE PRIVATIZATION AS ITS CENTRAL REFORM.

TO UNDERSTAND JUST HOW POWERFUL A FORCE OWNERSHIP CAN BE, I WANT TO DESCRIBE TO YOU ONE PARTICULAR PRIVATIZATION EXAMPLE; THE CHANGE THAT OCCURS WHEN A GROUP OF TENANTS IN A PUBLIC HOUSING PROJECT TAKE OVER THEIR LIVING SPACE.

PUBLIC HOUSING BEGAN AS A NEW DEAL ERA SOLUTION TO THE HOUSING SHORTAGE. IT WAS INTENDED TO FUNCTION AS A WAY STATION FOR FAMILIES WHICH HAD BEEN EVICTED DURING THE DEPRESSION. WITH THIS LIMITED OBJECTIVE, PUBLIC HOUSING WORKED REASONABLY WELL, AS FAR AS CENTRALLY

PLANNED, BUREAUCRATIC SOLUTIONS GO. BUT THEN THE DAM BROKE.

AS THE IMMIGRATION OF THE SOUTHERN POOR BEGAN IN THE 1950s, PUBLIC HOUSING MOVED FROM BEING TRANSITIONAL HOUSING TO PERMANENT HOUSING. BEFORE LONG PUBLIC HOUSING PROJECTS WERE FUNCTIONING AS TRAPS, NOT SAFE HAVENS FROM TROUBLED ECONOMIC TIMES. THE SAFETY NET BECAME A SNARE. NOW LARGE NUMBERS OF OUR CITIZENS ARE STUCK IN PLACES NONE OF US WOULD EVEN DREAM OF VISITING, MUCH LESS LIVE -- POWERLESS TO FIGHT THE DRUGS AND CRIME.

THEIR ONLY OPTION HAS BEEN TO COMPLAIN TO THE PUBLIC HOUSING AUTHORITY. AND A LOT OF GOOD THAT HAS DONE THEM. LIKE THE DEPARTMENT OF MOTOR VEHICLES, THREE HOURS AND FOUR LINES LATER, WITH LUCK, SOMEONE MIGHT BE AVAILABLE TO TAKE DOWN THE COMPLAINT.

BUT IN PARTS OF OUR COUNTRY THE RESIDENTS ARE SKIPPING THE COMPLAINTS AND TAKING BACK THE INFRASTRUCTURE. THE KENILWORTH-PARKSIDE DEVELOPMENT IN NORTHEAST WASHINGTON HAS BEEN A STUPENDOUS SUCCESS. IN 1980 IT WAS AN OPEN AIR DRUG MARKET. TODAY, THE DRUG DEALERS HAVE GONE, CRIME IS NEGLIGIBLE AND THE BUILDINGS ARE IN BETTER SHAPE THAN THEY'VE BEEN IN DECADES.

THE PERSON RESPONSIBLE FOR THIS CHANGE IS A REMARKABLE WOMEN -- KIMI GRAY.

SHE BELIEVED THAT A FAMILY'S HOME WAS TRULY THEIR CASTLE AND SHE SET OUT TO PROVE IT. IN 1982 SHE PERSUADED THE D.C. PUBLIC HOUSING AGENCY TO LET THE TENANTS MANAGE THE PROPERTY. THEY TOOK IT OVER AND REWROTE THE RULES. THEY HELD MONTHLY MEETINGS OF ALL THE TENANTS. SET UP FINES FOR THOSE WHO LITTERED OR LOITERED OR FAILED TO CUT THE GRASS, HIRED A SECURITY SERVICE TO CHASE THE DRUG DEALERS AWAY. RENT COLLECTION WENT UP 60%. THIS CAME ABOUT LARGELY THROUGH AN INCREASE IN TENANT INCOME. NOT AS A RESULT OF THE EVICTION OF POORER FAMILIES AND THEIR REPLACEMENT WITH OTHERS, BUT BY THE ESTABLISHMENT OF A THRIFT STORE, A DAY CARE CENTER, A CLEANING BUSINESS AND A SANDWICH SHOP -- ALL BUSINESSES AND JOBS CREATED BY THE TENANT ASSOCIATION.

OWNERS TAKE CARE OF A HOME BETTER THAN RENTERS TAKE CARE OF A HOUSE.

NO WONDER KIMI GRAY PROUDLY EMBRACED QUEEN ELIZABETH WHEN THE QUEEN RECENTLY STOPPED BY KENILWORTH. SHE TOO NOW HAS A CASTLE.

OWNERSHIP IS A POWERFUL STIMULUS. THE BOOK IN SEARCH OF EXCELLENCE RECOUNTED AN EXPERIMENT IN WHICH AN INDUSTRIAL PSYCHOLOGIST BROUGHT A GROUP OF ADULT SUBJECTS TO A LAB, SUPPOSEDLY TO TAKE PART IN AN INVESTIGATION FOCUSING ON THE EFFECTS OF NOISE ON PRODUCTIVITY. ALL OF

THEM WERE GIVEN SOME DIFFICULT PUZZLES TO SOLVE AND SOME RATHER DULL PROOFREADING TO DO. WHILE THEY ATTEMPTED THESE TWO CHORES, A RAUCOUS AUDIO TAPE CONSISTING OF ONE PERSON SPEAKING SPANISH, TWO PEOPLE SPEAKING ARMENIAN, A MIMEOGRAPH RUNNING, A CHATTERING TYPEWRITER AND STREET NOISE RAN IN THE BACKGROUND. HALF THE SUBJECTS WERE GIVEN A BUTTON THEY COULD PUSH TO SUPPRESS THE NOISE. THE OTHER HALF WERE NOT. THE RESULTS? AS YOU MIGHT EXPECT, THOSE WITH BUTTONS TO PUSH SOLVED FIVE TIMES MORE PUZZLES AND MADE ONE-QUARTER FEWER AS MANY PROOFREADING ERRORS AS THOSE WHO HAD NO BUTTON. THE INCREDIBLE FACT, HOWEVER, WAS THAT NOT A SINGLE ONE OF THOSE WITH BUTTONS ACTUALLY PUSHED THEM. THE EXPERIMENT WAS REPEATED SEVERAL TIMES WITH THE SAME RESULT. THE MERE FACT THAT PEOPLE PERCEIVED THAT THEY HAD A MODICUM OF CONTROL OVER THEIR LIVES -- THE OPTION OF PUSHING THE BUTTON -- MADE AN ENORMOUS DIFFERENCE IN PERFORMANCE.

THE TENANTS AT KENILWORTH-PARKSIDE EXPERIENCED THE SAME PHENOMENON. BEFORE THE TENANTS HAD TAKEN OVER, THEY WERE HELPLESS SUBJECTS TO AUTHORITY -- LEGAL AND ILLEGAL ALIKE. THEY EXPECTED TO BE VICTIMIZED. THEY EXPECTED THEIR SONS AND DAUGHTERS TO BECOME DRUG ADDICTS. THEY EXPECTED TO HAVE NO POWER OVER THEIR LIVES.

NOW THEY ARE SELF-RELIANT AND HAVE A NEW VIEW OF THEMSELVES AND THE WORLD AROUND THEM. THEY HAVE GAINED THE SELF-RESPECT SO LONG DENIED THEM. MANY MORE SUCH PROJECTS ARE NEEDED.

IF PRIVATE OWNERSHIP COULD BE HARNESSSED TO REBUILD LOS ANGELES AND THE REST OF AMERICA IT COULD INTRODUCE AN AWESOME NEW DYNAMIC. THE DYNAMIC OF TALENT, ENTERPRISE AND INNOVATION. MARX WAS CORRECT WHEN HE SAID WE SHOULD NOT UNDERESTIMATE THE POWER OF PRIVATE PROPERTY TO GENERATE PRODUCTION AND BRING ABOUT SOCIAL TRANSFORMATIONS. THE DYNAMICS OF OWNERSHIP AND THE MARKET, AND THE FEEDBACK OF PROFIT -- NOT THE CORPORATE FORM -- MAKE PRIVATE ENTERPRISE THE MOST EXCITING INSTRUMENT OF RENEWAL MEN AND WOMEN HAVE EVER INVENTED.

FOR SOCIETY TO BENEFIT FROM THIS DEEP-SEATED DESIRE TO FULFILL HUMAN NEEDS, IT IS THE SOCIAL RESPONSIBILITY OF GOVERNMENT TO UNLEASH OWNERSHIP AND CHANNEL IT TO THOSE NEEDS. THE TASK OF GOVERNMENT IS TO ESTABLISH INCENTIVES IN SUCH A WAY THAT THE PROFIT MOTIVE IS MADE TO DO WHAT SOCIETY MOST REQUIRES.

IT IS NOT A FOOTRACE WE ARE AFTER BUT A PARTNERSHIP. A PUBLIC/PRIVATE PARTNERSHIP IN WHICH GOVERNMENT DOES WHAT IT DOES BEST -- WHICH IS STEER; AND PEOPLE DO WHAT THEY DO BEST, WHICH IS PRODUCE. THE BEST OF EACH

IS CERTAIN TO COME FORTH. RATHER THAN DISCOURAGE THE INITIATIVE AND DRIVE OF THE INDIVIDUAL, GOVERNMENT MUST SEEK TO HARNESS INDIVIDUAL INITIATIVE FOR THE COLLECTIVE GOOD.

HOW THEN IS THIS AMERICAN PERESTROIKA TO COME ABOUT, ON A WIDE SCALE? THE KENILWORTH EXPERIENCE IS A MICROECONOMIC CHANGE. CAN WE HAVE A MACROECONOMIC POLICY FOR PRIVATIZATION?

A MONTH AGO 100 ECONOMISTS, INCLUDING SIX NOBEL PRIZE WINNERS, WROTE A LETTER TO PRESIDENT BUSH, THE FEDERAL RESERVE AND CONGRESS. I KNOW THIS SOUNDS LIKE THE BEGINNING OF A BAD JOKE -- BUT FOR ONCE, IT WASN'T. INSTEAD, THE 100 ECONOMISTS SUGGEST AN UNCONVENTIONAL PROGRAM FOR ECONOMIC RECOVERY. A KEY FEATURE OF THAT PROGRAM WAS A PROPOSAL TO INCREASE FEDERAL GRANTS TO STATE AND LOCAL GOVERNMENTS BY \$ 50 BILLION TO REBUILD OUR CRUMBLING INFRASTRUCTURE. ACCORDING TO THESE ECONOMISTS, SPENDING FOR INVESTMENT OF THIS KIND IS VERY DIFFERENT THAN SPENDING FOR CONSUMPTION. IT GOES TO INCREASE THE NATION'S PRODUCTIVE CAPACITY.

PREDICTABLY, THE SUGGESTION TO INCREASE FEDERAL SPENDING BY \$50 BILLION HAS FALLEN ON DEAF EARS IN WASHINGTON. WITH FEDERAL INTEREST PAYMENTS ON THE DEFICIT RUNNING NOW AT NEARLY 23% OF ALL FEDERAL OUTLAYS,

SOON TO BECOME THE SINGLE LARGEST DOMESTIC PROGRAM, AND THE BUDGET AGREEMENT IN LIMBO PENDING THIS YEAR'S ELECTIONS, IT IS HARDLY SURPRISING THAT 100 LEADING ECONOMISTS MADE NO IMPACT AT ALL ON OUR PUBLIC OFFICIALS.

THEIR PROPOSAL, HOWEVER, SHOULD NOT BE DISREGARDED. I HAVE A SUGGESTION.

OUR PRESENT INFRASTRUCTURE REPRESENTS A GIGANTIC POOL OF UNTAPPED CAPITAL. THIS CAPITAL LIES IDLE IN LARGE TRACTS OF REAL ESTATE OWNED BY STATE AND LOCAL GOVERNMENTS UP AND DOWN THE COUNTRY: PORTS, AIRPORTS, WASTE WATER PLANTS, HIGHWAYS, HOUSING, MUNICIPAL POWER SYSTEMS AND A HOST OF SIMILAR KINDS OF PROPERTY. BECAUSE THESE ASSETS ARE IN STATE OR LOCAL GOVERNMENT OWNERSHIP, THEY EARN A ZERO RETURN ON THEIR EQUITY. BECAUSE THEY HAVE NO REAL OWNERS, THEY ARE POORLY UTILIZED. IT OUGHT TO BE POSSIBLE TO EMPOWER PEOPLE TO RUN THESE ENTERPRISES, BY MAKING THEM OWNERS -- THROUGH MUNICIPAL BUYOUTS. THIS WOULD HAVE A DUAL EFFECT.

FOR THOSE OF US WHO BELIEVE THAT OWNERSHIP MAKES A DIFFERENCE IT WOULD LIBERATE THIS INFRASTRUCTURE FROM ITS PRESENT STATE OF NEGLECT. SELLING THESE ASSETS WOULD ALSO PRODUCE A PILE OF CASH FOR CITIES AND STATES TO REBUILD THE INNER-CITIES. THE REASON FOUNDATION IN LOS ANGELES ESTIMATES THAT PRIVATIZATIONS OF SUCH A KIND

WOULD FETCH MORE THAN \$200 BILLION DOLLARS FOR STATE AND LOCAL GOVERNMENTS TO REBUILD AMERICA. EVEN IN WASHINGTON, WHERE I AM FROM, THAT IS A LOT OF MONEY. BEST OF ALL, UNLIKE THE PROPOSAL MADE BY THE 100 LEADING ECONOMISTS, RAISING MONEY THIS WAY WOULD NOT COST THE FEDERAL TREASURY A SINGLE PENNY.

BECAUSE THIS MONEY WOULD BE A ONE-TIME WINDFALL, IT SHOULD NOT BE FRITTERED AWAY. IT SHOULD BE RECYCLED. RECYCLE THE PROCEEDS OF SUCH INFRASTRUCTURE SALES BY REINVESTING IT -- IN ADDITIONAL INFRASTRUCTURE.

LET ME GIVE YOU AN EXAMPLE. THE CITY OF LOS ANGELES OWNS FOUR AIRPORTS, A PORT, A WATER SYSTEM, AN ELECTRIC POWER COMPANY; AND DOUBTLESS A VARIETY OF OTHER ASSETS I KNOW NOTHING ABOUT. THE CITY DOES NOT NEED TO BE IN THESE BUSINESSES. SELLING ALL OF THESE ASSETS COULD ENDOW AN INFRASTRUCTURE FUND -- A REBUILD LOS ANGELES FUND -- WITH BILLIONS OF DOLLARS. MAYBE \$5 BILLION! JUST IMAGINE HOW MUCH LEVERAGE SUCH A FUND COULD GENERATE. IT MIGHT BE POSSIBLE TO LIVE OFF OF THE INTEREST ALONE, RECYCLING IT OVER AND OVER AGAIN AS LOW INTEREST BUSINESS LOANS INTO THAT DEVASTATED ECONOMY.

PRIVATIZATION IS THE KEY TO UNLOCKING OUR SLUMBERING WEALTH AND PUT IT INTO PRODUCTIVE SERVICE.

THE IDEA IS SO SIMPLE IT ALMOST SEEMS SELF-EVIDENT. WHY HASN'T THIS ALREADY BEEN DONE? WELL, THERE HAVE BEEN OBSTACLES.

LAST WEEK PRESIDENT BUSH TOOK THE FIRST STEP TOWARD MAKING IT POSSIBLE. HE SIGNED AN EXECUTIVE ORDER WHICH ELIMINATED A SUBSTANTIAL BARRIER TO PRIVATIZATIONS BY STATE AND LOCAL GOVERNMENTS OF ASSETS SUCH AS AIRPORTS, PORTS, HIGHWAYS AND WASTE WATER TREATMENT PLANTS. BECAUSE THESE ASSETS WERE BUILT IN LARGE PART WITH FEDERAL GRANTS, OMB HAD LONG REQUIRED THAT THE FEDERAL GOVERNMENT BE REPAID ITS PAST GRANTS IN THE EVENT THE INFRASTRUCTURE WAS SOLD. THE EXECUTIVE ORDER DOES AWAY WITH THIS DISINCENTIVE. STATE AND LOCAL GOVERNMENTS WILL BE ABLE TO KEEP THE LION'S SHARE OF THE PROCEEDS OF SUCH PRIVATIZATIONS. IN EFFECT, THE PRESIDENT'S EXECUTIVE ORDER PERMITS STATE AND LOCAL GOVERNMENTS TO CASH IN ON THEIR PAST FEDERAL GRANTS.

THE BILLIONS OF DOLLARS THEY NEED TO REBUILD AMERICA IS THUS ALREADY AVAILABLE TO THEM. NOW STATE AND LOCAL GOVERNMENTS MUST SHOW HOW TRULY RESOURCEFUL THEY CAN BE. IT IS FOR THEM TO ACT AND DEMONSTRATE THEY CARE. IT IS A CRIME THAT STATE AND LOCAL GOVERNMENTS FIDDLE WITH BILLIONS OF DOLLARS IN ASSETS WHICH COULD BE USED TO REBUILD CITIES -- WHILE THE CITIES BURN.

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So, I think, we have come to a time for choosing. I suggest to you that there is no left or right, only up or down. Up to the heights which personal effort and ownership can bring or down to the depths of despair and subordination which bureaucracy offers and enforces.

I am convinced we are not yet bankrupt. In the words of the old Scottish ballad, "For those defeats that we have had so far, we are hurt; we are not slain. We'll lie us down and rest a bit, and then we'll fight again." For true believers in the redemptive power of ownership, risk is inevitable, but failure is not. There is great work ahead in rebuilding America and empowering its people. Work that is not unlike the building of a great cathedral. The work is slow, complicated and painstaking. It is work not only of leaders, but ordinary people. The cathedral evolves as it is created, with each generation adding its own vision -- but the initial spark of vision remains constant, and the faith that drives the vision persists. Eventually the spires and arches of the cathedral ascend to soaring heights.

So let it be with us.

PRIVATIZATION INTERNATIONAL, INC.*copied to
speeches***FAX TRANSMITTAL SHEET****To:**Richard Porter**Date:**5/7/92**Company:****City:****Fax No.:**202 456 6216**From:****Acct #:****Comments:**

Richard — See the Financial Model
on Page 10 of the
Manuscript. The Assumptions
are described on Page 9.
There are other minor
changes

This fax consists of 17 pages including this sheet.

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PRIVATIZATION INTERNATIONAL, INC.

THE NEW EXECUTIVE ORDER ON INFRASTRUCTURE PRIVATIZATION INCREASES STATE AND LOCAL GOVERNMENTS' ECONOMIC RETURN FROM THE DISPOSITION OF \$2 TRILLION OF PUBLIC ASSETS

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John Stainback, Chairman and CEO, Privatization International, Inc., an advisory company based in New York City.

AN OVERVIEW OF THE EXECUTIVE ORDER AND IT'S FINANCIAL IMPLICATIONS

On April 30, 1992, President Bush signed an Executive Order: Infrastructure Privatization, which provides state and local governments a window of opportunity to facilitate privatization transactions and allow them a larger share of the nontax revenue from the disposition of public assets. The value of these public assets is estimated to be between \$1.1 and \$2 trillion. This order serves state and local governments in three ways:

- The order facilitates state and local governments ability to seize the value of existing assets obtained with federal assistance.
- By disposing of public assets, governments will induce private sector investment, in the form of capital infusions from acquisitions, and by returning the assets back to the tax roll, thereby creating continuous income streams.
- By reducing, and in some circumstances, waiving the federal governments share of the proceeds from a sale or lease of public assets, state and local governments can capture a larger share of the assets' value.

In addition to the nontax revenue from the disposition of their public assets, governments will also have the option to sell the assets and place them back on the tax rolls to gain property and corporate income tax.

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The financial implications of the new Executive Order are potentially enormous. According to the Tax Foundation, the cumulative total debt incurred up to 1991 by all state and local governments is \$648.6 billion. In order to assess the potential economic return to state and local governments from selling their public assets under the new Executive Order, an economic model with a series of assumptions was developed. The model and assumptions are described later in the text. Based on the current value of \$2 trillion for the nation's infrastructure assets and these assumptions, the 83,000 state and local governments in the U.S. would realize \$1.8 trillion. Consequently, they would only have to sell one-third of their assets to eliminate their entire outstanding debt. To give a sense of the magnitude of \$1.8 trillion, state and local governments could not only eliminate 100 percent of their debt (\$648 billion), but take the remaining funds (\$1.15 trillion) and issue a tax credit, or payment, of \$4,600 to every man, woman, and child in the United States.

GOVERNMENTS HAVE FOUR WAYS TO BALANCE THEIR BUDGETS AND FINANCE NEEDED FACILITIES, INFRASTRUCTURE, AND SERVICES

State and local governments are being squeezed financially from several directions. Their dilemma is compounded by a greater need to build and rehabilitate infrastructure and public facilities, as well as deliver a greater number and higher quality of services.

Over the last several years, state and local governments are feeling the substantial reductions in economic aid from the federal government. In parallel, states and local governments are reeling from one of the worst recessions in history.

States and cities have four alternative means to balance their budgets:

- Increase taxes,
- Institute cutbacks,
- Reduce operational costs, or
- Generate additional nontax revenue.

Voters have reached their limit when it comes to taxes, so while the first alternative of increasing taxes continues to be used by government, the political consequences have been disastrous.

When governments elect to institute major cutbacks, the impact on the local economy takes one giant step backwards, as does the level of employment. Part of this often used solution is to also defer needed rehabilitation and expansion of public facilities and infrastructure. The current condition of the nation's infrastructure is increasingly dangerous and the cumulative result of twenty years of deferring maintenance. Continuing to defer critically needed investment in infrastructure only compounds the problem.

Governments have recently begun to reduce their operational costs, but in most instances the cost savings are not adequate to cover the increasingly larger deficits. By developing and signing into law the Executive Order on Infrastructure Privatization, the Bush administration is providing state and local governments across the nation with far more than a one time increase in economic aid. They are facilitating one of the strongest types of privatization - governments ability to maximize the value of their physical assets. By carefully disposing or transferring selected public assets to the private sector, governments not only realize infusions of private capital, but by returning the assets to the private sector, they create additional income streams from property tax and corporate income tax.

Before some governments and private sector parties pigeon-hole the disposition of public assets as selling the governments "crown jewels", they need to realize that there are many alternative disposition techniques. Only one of which is the technique of an outright sale. Long term lease acquisitions by the private sector provide governments with an economic return and allows them to retain ownership.

THE EXECUTIVE ORDER IN MORE DETAIL

The Executive Order on Infrastructure Privatization is well structured, comprehensive in scope, yet concise and clear. There are five major components to the Order.

- Identifying the types of public asset to be privatized.
 - Facilitating the privatization of infrastructure.
 - Defining the basis for participating governments to share the proceeds from privatization.
 - Outlining the use of the proceeds.
 - Documenting the restrictions on the assets once the privatization process is completed.
-
- **Type of Public Asset to be Privatized**
"Infrastructure asset means any asset financed in whole or in part by the federal government and needed for the functioning of the economy." Examples of such assets include: roads, tunnels, bridges, electricity supply facilities, mass transit, rail transportation, airports, ports, waterways, water supply facilities, solid waste disposal facilities, housing, schools, prisons, and hospitals.

- **Facilitating the Privatization of Infrastructure**

To facilitate the privatization of infrastructure, the Order provides three directives.

- 1) The head of each executive department and agency is directed to *"review those procedures affecting the management and disposition of federally financed infrastructure assets owned by state and local governments and modify those procedures to encourage appropriate privatization of such assets consistent with this order."*
- 2) *"Assist state and local governments in their efforts to advance the objectives of this order."*
- 3) *"Approve state and local governments' requests to privatize infrastructure assets, consistent with the criteria (described later in this article) and where necessary, grant exceptions to the disposition requirements of the 'Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments' common rule, or other relevant rules or regulations, for infrastructure assets."*

- **Basis for Participating Governments to Share the Proceeds from Privatization**

The proceeds from privatization has been defined as the "transfer price", or *"the amount paid, or to be paid by a private party for an infrastructure asset, if the asset is transferred as a result of competitive bidding; or the appraised value of an infrastructure asset, as determined by the head of the executive department or agency and the Director of the Office of Management and Budget (OMB), if the asset is not transferred as a result of competitive bidding."*

The transfer price or proceeds from the disposition of the public asset will be distributed as follows: *"State and local governments shall first recoup in full the unadjusted dollar amount of their portion of total project costs (including any transaction and fix-up costs they incur) associated with the infrastructure asset involved; if proceeds remain, then the federal government shall recoup in full the amount of federal grant awards associated with the infrastructure asset, less the applicable share of accumulated depreciation of such asset (calculated using the Internal Revenue Service (IRS) accelerated depreciation schedule for the categories of assets in question), and finally the state and local governments shall keep any remaining proceeds."*

- **Use of Proceeds**

The requirements for using the proceeds from the disposition of infrastructure assets are minimal and provide a clear indication that the federal government is making every effort to assist state and local governments to balance their budgets. In order to gain approval for asset disposition from the head of an executive department or agency, state and local governments are only required to use the proceeds in one of three ways: investment in additional infrastructure, reduction of debt, or tax reductions.

- **Restrictions on Assets Once Privatization is Completed**

In agreement with the philosophy of privatization, the federal government's requirements were developed from the perspective of the government allowing the private sector to come forth and serve the public, and entrust the government with the task of steering, not rowing, as Steve Savas, a noted privatization specialist in the area of public services, states so well.

The only stipulations required for approval are to "demonstrate that a market mechanism" is in place to ensure that the "assets will continue to be used for their originally authorized purposes, as long as needed for these purposes, even if the purchaser becomes insolvent or is otherwise hindered from fulfilling the originally authorized purposes; and user charges will be consistent with any current federal conditions that protect users and the public by limiting changes."

AN OVERVIEW OF THE FEDERAL GOVERNMENT'S GENERAL OWNERSHIP POSITION OF INFRASTRUCTURE ASSETS

Because the ultimate amount of proceeds allocated to state and local governments will also be determined by the federal government's ownership position, an overview of the federal government's declining investment in infrastructure over the last two decades might be helpful.

The nation's 83,000 local governments have been financially squeezed by the federal government over the last twenty to twenty-five years, especially when it comes to economic aid for infrastructure.

Table 1 illustrates the distribution of federal aid to state and local governments for "physical infrastructure" has been significantly reduced from 45.8 percent in 1960 to an estimated 21.6 percent in 1989. The table also reveals the reverse trend for human services. In 1960, 54.2 percent of all federal aid went to human services. By 1989, the allocation increased to 78.4 percent.

Table 1 - Distribution of Federal Aid to State and Local Government by Major Category (in percent)

	<u>1960</u>	<u>1975</u>	<u>1989</u>
Physical Infrastructure			
Natural resources and environment ¹	1.5	4.9	2.9
Transportation	42.7	11.8	15.0
Community and regional development ²	1.6	5.7	3.7
Human Service			
Education, training, employment, and social services	7.5	24.4	18.2
Health ³	3.0	17.7	29.5
Income security ⁴	37.5	18.8	27.2
Other	<u>6.2</u>	<u>16.7</u>	<u>3.5</u>
Total	100.0	100.0	100.0

Source: Office of Technology Assessment, 1990, Office of Management and Budget, Historical Tables: Budget of the United States Government Fiscal Year 1989 (Washington, DC: 1988)

State and local municipalities assumed greater financial responsibility during the last 20 years, but by the mid-1980's it was clear they could not continue to cover the difference between the increasing cost of infrastructure and the continuing reductions in Federal aid for infrastructure. This was compounded by the shift in national priorities from investing in infrastructure to higher governmental expenditures for social programs. In 1990, state and local governments allocated 29% of their Federal grant monies on health care, and in 1960 the allocation was 3%. In parallel, OMB studies also reveal that in 1990 15% of Federal grants were directed to transportation compared to 43% in 1960.

¹ Primarily Environmental Protection Agency construction grants

² Primarily Housing and Urban Development grants; small portions were used for infrastructure improvements.

³ Primarily grants for medicaid

⁴ Primarily grants for child nutrition, family support, and housing assistance

Even though federal public works funds when adjusted for inflation have decreased during the 1980's, according to the Office of Technology Assessment, Federal grants to State and local governments still financed 40 to 50% of their annual capital spending during that time. So the federal government's ownership position for State and local infrastructure assets is significant, which means the New Executive Order, reducing the federal governments share of the proceeds from privatization, has substantial implications for cities, counties, and states. They now have the opportunity to capture an inordinate share of the value of infrastructure investments made by the federal government over the last twenty to thirty years.

THE VALUE OF PUBLIC ASSETS AT STAKE

There are numerous types of assets covered by the new Executive Order. The potential nontax and tax revenue from the privatization of these assets could provide state and local governments with substantial infusions of private capital and additional income streams from taxes.

Three types of revenue can be generated from the privatization of infrastructure: 1) The book value of each asset paid at the closing of the sale, or paid through lease payments; 2) Property tax from putting assets back on the tax rolls if sold (depending on the lease agreement property tax may or may not be realized); and 3) Corporate income tax from the private operation of infrastructure assets.

In 1989, the National Realty Committee estimated the value of the nation's tangible capital assets to be \$12 trillion. Of the nation's land and building assets, they estimated that the 20 percent share owned by the government is equal to \$2.4 trillion. Most is owned by state and local governments, which hold \$1.5 trillion worth of infrastructure such as roads, bridges and sewers as well as social service buildings such as schools, public housing, hospitals, etc. America's land supports some \$8 trillion (valued at replacement cost, 1987) in permanent structures. Of this amount, they classify 25 percent, or \$2 trillion as "structures other than buildings." In this category of "U.S. nonbuilding structures" they identify four types of assets, three of which are public streets and highways (32%) \$634 billion; utility structures (37%) \$745 billion; and other nonbuilding structures (25%) \$492 billion. They defined the latter types of assets as "dams, reservoirs, railroad tracks and structures, airfields, parks, and private streets." So the total value of public streets and highways, utility structures and other nonbuilding structures is \$1.87 trillion.

In order to estimate the 1992 nontax value of these assets, an annual inflation factor of two percent was applied for the five years since 1987. Consequently, the value of these assets, is currently \$2.064 trillion, excluding the potential tax revenue from privatization.

In a 1988 study by the National Council on Public Works Improvement, the U.S. Department of Commerce estimated the nation's "Public Works Net Capital Assets" had a value of over \$950 billion (1984 dollars). In order to estimate the 1992 value, an annual inflation factor of 2 percent was applied.

Table 2 - The Nation's Public Works Net Capital Assets

	<u>1984 (\$ billion)</u>	<u>1992 (\$ billion)</u>
Highways	\$475	\$556
Water Resource Facilities	\$150	\$176
Water Supply Facilities	\$120	\$140
Wastewater Facilities	\$136	\$159
Aviation Facilities	\$ 40	\$ 47
Mass Transit	\$ 34	\$ 40
Solid Waste Facilities	\$ 2.3	\$ 2.7
Total	\$957	\$1,121

- Highway System**

The nation's highway system consist of almost 3.9 million miles of roads and bridges:

	<u>Total System</u>	<u>Total Vehicular Miles</u>
<u>Federal Aid Highway System</u>	21.8%	80.5%
Interstate (43,600 miles)		
Primary highways (257,400 miles)		
Collector routes (398,200 miles)		
Urban system (144,100 miles)		
<u>Off Federal Aid Highway System</u>	78.2%	19.5%
3,018,625 miles of roadway	100%	100%

Note: Only 226,157 miles (5.9 % of all route-miles) are under direct federal jurisdiction (mostly roads in national forests and parks, military and indian reservations).

The U.S. Department of Commerce believes the accumulated asset value of the nation's highways, streets, roads and bridges increased from \$250 billion in 1960 to \$480 billion in 1984. This value in 1992 dollars is \$561 billion.

- Bridges**

In 1985 there were 575,607 bridges in the U.S. Of this total, 304,307 bridges, or 53 percent were not part of the federal aid system.

- **Airports**

In 1990, the Department of Transportation (DOT) identified 21 major airports subject to heavy delays - 20,000 plane-hours or more per year - and predicted that another 20 will join the list by 1998.

Of the nation's 5,900 airports open to the public, 75 percent are privately owned and operated although they handle less than one-half of one percent (.005 percent) of all air passengers.

In 1990, The Reason Foundation estimated that the nation's 50 largest air carrier airports were worth nearly \$24 billion. In addition, they estimated that these airports, if privately owned, would generate an estimated \$391 million annually in property tax revenue.

The Potential Economic Return for State and Local Governments From Selling Their Public Assets Depends on a Variety of Factors

There are a variety of factors which will have an impact on a state and local government's share of the proceeds from the privatization of a public asset. In order to provide a general magnitude of the financial implications of the new Executive Order the following assumptions were developed.

- The current value of the nation's public assets is \$2 trillion.
- The initial capital cost of the nation's infrastructure assets was nearly \$1 trillion.
- State and local governments shared the capital costs of the nation's assets on a 50-50 basis with the federal government.
- The average age of U.S. infrastructure assets appears to be 24 years.
- Annual appreciation was assumed to be 3.5 percent.
- The interest rate, or cost of finance was assumed to be 10 percent.
- Straight-line depreciation (31.5 years) was assumed.

Based on these assumptions, the generic financial model (Table 3) reveals that state and local governments will capture 90 percent of the proceeds from privatization of the nation's infrastructure assets. The total amount of proceeds for state and local governments resulting from selling all of their infrastructure assets would be approximately \$1.8 trillion. Their share of the total proceeds would not only cover their total debt service of \$893 billion for all assets, but also provide a net gain of approximately \$900 billion!

Table 3
U.S. Public Infrastructure Assets
Financial Analysis

Assumptions

Average Age of Infrastructure = 24 Years

Average Term of Debt = 15 Years

Average Interest Rate = 10%

Average Annual Increase in Market Value of Infrastructure = 3.5%

Straightline Depreciation

Privatization International, Inc.

07-May-92

(In Millions)

	Infrastructure Cost	Market Value	Total Debt Service	State/Local Funds	Federal Funds	Depreciation	Federal Share	Net State/Local Proceeds	Total State/Local Proceeds
1	\$906,000	\$906,000	\$119,115	\$59,558	\$59,558	\$28,762	\$30,796	\$815,647	\$875,204
2		937,710	238,230	119,115	119,115	57,524	61,591	757,003	876,119
3		970,530	357,346	178,673	178,673	86,286	92,387	699,470	878,143
4		1,004,498	476,461	238,230	238,230	115,048	123,183	643,085	881,316
5		1,039,656	595,576	297,788	297,788	143,810	153,979	587,889	885,677
6		1,076,044	714,691	357,346	357,346	172,571	184,774	533,924	891,269
7		1,113,705	833,807	416,903	416,903	201,333	215,570	481,232	898,135
8		1,152,685	952,922	476,461	476,461	230,095	246,366	429,858	906,319
9		1,193,029	1,072,037	536,019	536,019	258,857	277,161	379,849	915,868
10		1,234,785	1,191,152	595,576	595,576	287,619	307,957	331,252	926,828
11		1,278,002	1,310,268	655,134	655,134	316,381	338,753	284,116	939,250
12		1,322,733	1,429,383	714,691	714,691	345,143	369,549	238,493	953,184
13		1,369,028	1,548,498	774,249	774,249	373,905	400,344	194,435	968,684
14		1,416,944	1,667,613	833,807	833,807	402,667	431,140	151,997	985,804
15		1,466,537	1,786,729	893,364	893,364	431,429	461,936	111,237	1,004,601
16		1,517,866	1,786,729	893,364	893,364	460,190	433,174	191,328	1,084,692
17		1,570,991	1,786,729	893,364	893,364	488,952	404,412	273,215	1,166,579
18		1,625,976	1,786,729	893,364	893,364	517,714	375,650	356,962	1,250,326
19		1,682,885	1,786,729	893,364	893,364	546,476	346,888	442,633	1,335,997
20		1,741,786	1,786,729	893,364	893,364	575,238	318,126	530,296	1,423,660
21		1,802,749	1,786,729	893,364	893,364	604,000	289,364	620,020	1,513,384
22		1,865,845	1,786,729	893,364	893,364	632,762	260,602	711,878	1,605,243
23		1,931,149	1,786,729	893,364	893,364	661,524	231,841	805,945	1,699,309
24		2,000,000	1,786,729	893,364	893,364	690,286	203,079	903,557	1,796,921

SUMMARY

The Bush administration in conjunction with Vice President Quayle's Council of Competitiveness, has provided state and local governments with the vehicle to seize a major portion of the nontax revenue from the privatization of public assets estimated in value to be between \$1 and \$2 trillion.

In addition, if state and local governments choose to sell these assets, versus structuring long term lease acquisitions with the private sector, they will capture the substantial property tax revenue from putting these assets back on the tax rolls. The tax revenue for governments for the largest 50 airports alone is an additional \$391 million annually.

A third source of additional revenue now more readily available to state and local governments because of the Executive Order, is the corporate income tax which would result from transferring these assets to the private sector.

According to The Tax Foundation, the cumulative outstanding debt for all state and local governments as of 1990 totaled \$648.6 billion. Assuming the nation's infrastructure assets are worth \$2 trillion, state and local governments would realize \$1.8 trillion. Consequently, if they privatize only **one-third** of their infrastructure assets they would eliminate 100 percent of their outstanding debt.

If state and local governments privatize **all** of their infrastructure assets, they could not only eliminate 100 percent of their outstanding debt, but they could use the remaining revenue to issue a tax credit, or direct payment of \$4,600 to every man, woman, and child in the U.S.

The federal government has taken the initiative to structure the framework for state and local governments to privatize their infrastructure assets. Now the nation's cities, counties, and states need to implement the transfer of these assets in order to capture a major portion of the combined nontax and tax revenue from the privatization of their infrastructure assets.

M E M O R A N D U M

May 14, 1992

Via FAX

TO: Richard Porter

FROM: John Giraudo

Re: Privatization/Infrastructure Executive Order

The President's Executive Order offers the Administration a timely answer to the rising voices clamoring for more federal grants for the inner cities. The Administration has already given them the money -- in spades. What is now needed is a weed, seed and grow program.

The Administration needs to do two things to implement the Executive Order's cure for the problems of the inner cities. The first is to publicize the Executive Order by raising both official and public awareness of the opportunity it presents. The second is to actively promote the Executive Order by tying federal "seed" money to city resourcefulness in utilizing their untapped idle capital to grow inner city investment.

I. Raise Official and Public Awareness

- * Most mayors and governors do not know about the Executive Order. Even if they do, they are

avoiding it and parading to Congress for more federal money.

- * Mayors already have the federal money they are asking for -- billions of dollars has been made available to them by the Executive Order. The federal government is going to let cities and states cash in on the past federal grants they received.
- * With a \$350 billion federal deficit, city governments must become more resourceful. Self-reliance must be practiced by big city mayors just as much as it must be practiced by everyone else in hard times. The onus is on city government to show it cares, not just the federal government.
- * The City of Los Angeles owns a giant port, four airports, a water company, an electric utility and a number of wastewater plants. If these were sold, billions of dollars could be raised to provide small business loans to rebuild the South-Central community.
- * We talk a lot about getting our priorities straight. Here is an opportunity for cities to get their priorities straight. They do not need to be in the port business, electric business, water business. They need to show they care about places like South-Central.
- * It is a crime for City governments to sit on billions of dollars in assets while inner cities burn. The public needs to see how remiss city governments are. LA should sell its assets for the billions they are worth, not raise sales taxes, as they are contemplating, for the few nickles that will provide for inner city investment.

II. "Seed" Privatization Transactions

- * Federal dollars are scare. We must maximize their leverage. Federal seed money must be used to pry open the idle capital cities and states sit on and get them to use it for investment in the inner cities.

- * Tie federal seed money to asset sales which raise capital to grow inner city investment.
- * "SWAT" teams from the Administration should provide necessary briefings and technical assistance to help cities mine their balance sheets for assets to sell.
- * A Rebuild American Fund with federal seed money should be set-up to encourage a Rebuild LA fund containing privatization proceeds. Together, the commingled funds could make small business loans to match and encourage private investment being offered by Peter Ueberroth's private Rebuild LA Fund for South-Central. Private investment will be easier and faster if public investment goes in first.

**SKADDEN
ARPS
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MEAGHER &
FLOM**

1440 New York Avenue, N.W.

Washington, D.C. 20005

Main Telephone No. (202) 371-7000

Main Fax No. (202) 393-5760

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Washington, D.C. 20005

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FACSIMILE TRANSMITTAL SHEET

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City: _____

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PRIVATIZATION INTERNATIONAL, INC.**FAX TRANSMITTAL SHEET**

To: Richard Porter Date: 6/1/92
Company: The White House City: _____
Fax No.: 202-456-6216 From: Steinbeck
Acct #: _____

Comments:

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Phone: (212) 385 0067 / Fax: (212) 385 0069

14 Wall Street New York, New York 10005

PRIVATIZATION INTERNATIONAL, INC.

A 'PUBLIC/PRIVATE' URBAN AID PLAN TO LEVERAGE THE PROPOSED FEDERAL GRANT

by John Stainback

The federal legislation for a truly effective Urban Aid Plan, which would be financed and implemented on a public/private partnership basis is already in place. The Bush Administration and Congress should not write another \$2 billion check for aid to the nation's cities without requiring the nation's mayors to also utilize two pieces of legislation — the Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA), and the recently signed Executive Order: "Infrastructure Privatization" (No. 12803).

With the national debt approaching \$4 trillion, the Federal government cannot afford to write another unaccountable \$2 billion check. If they could afford it, or if the Urban Aid Plan is seen as "emergency aid" to the cities, it should be granted as an equity investment to be eventually paid back from the implementation of public/private finance and development plans for the redevelopment of central cities.

The Executive Order on Infrastructure Privatization was designed for cities and states to generate nontax revenue from the privatization of public assets. The proceeds from these privatization projects, which based on my research could be up to \$1.8 trillion, should be used to finance the needed redevelopment, and to pay back the Federal government if the projected economic returns are achieved.

ISTEA was also designed to facilitate the public/private finance and development of desperately needed infrastructure repairs and new infrastructure. The Federal government has allocated \$151 billion over the next five years towards this program.

Governors and mayors have been given the legislative foundation to help themselves. What are they waiting for? Why are they waiting for "Urban Aid", which in perspective of their budgets and the enormous infrastructure investment required is equivalent to a grain of sand? The maximum allocation for New York City under the proposed Urban Aid Plan will be one-fifth of one percent, or .17% of the City's annual budget.

Mayors need to recognize that ISTEA and the Executive Order on Privatization not only allows their cities to finance redevelopment, or new infrastructure and facilities on a public/private basis, but implementation will also generate jobs and increase productivity. If cities need additional incentives to implement projects using these legislative actions, they should also recognize that the privatization of selected assets eliminates any remaining interest payments on the assets and also any operational subsidies. Equally important, these assets go back on the property and corporate tax rolls, which will provide cities with a long term income stream.

A Public/Private Urban Aid Plan in combination with the full utilization of ISTEA, and the monetization of public assets will also provide cities with capital to reinforce and expand the "weed and seed" program and the urban enterprise zone concept.

It is the synergy among the integrated use of ISTEA, the privatization of public assets, the "weed and seed" program and the urban enterprise zones, which will differentiate the "Public/Private" Urban Aid Plan from previous piecemeal attempts by the Federal government to redevelop our nation's central cities.

John Stainback is the Chairman and CEO of Privatization International, Inc. based in New York City.

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Collection:

Record Group: Quayle Vice Presidential Records
Office: Deputy Chief of Staff's Office
Series: Porter, Richard, Files
Subseries: Subject Files
WHORM Cat.:
File Location: Privatization [3]

Date Closed: 3/20/2023	OA/ID Number: 21803-022
FOIA/SYS Case #: 2021-0094-F	Appeal Case #:
Re-review Case #:	Appeal Disposition:
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AR Disposition:	MR Disposition:
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Co. OFC. OF V.P.	Co. Privatization Council	
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Fax # 395-1754	Fax # 223-4579	

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202/857-1142
Updated:
April 21, 1992

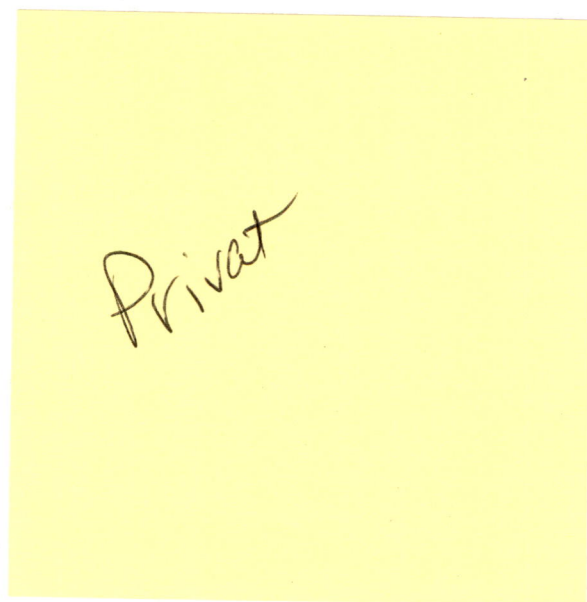
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THE WHITE HOUSE

WASHINGTON

June 8, 1992

MEMORANDUM FOR CLAYTON YEUTTER

FROM: DIANA FURCHTGOTT-ROTH *DEFR*

SUBJECT: Follow-up on Privatization Executive Order

I have had many calls regarding the President's Executive Order on Privatization, both from persons interested in selling infrastructure, and from those asking how the President is planning to implement the directive. On Friday, June 5, I visited Alfred DelliBovi, Deputy Secretary of HUD, to discuss possible ways to move the initiative forward at the agency level.

Mr. DelliBovi suggested that the most effective way to implement the executive order would be to have the President or the Vice President send a letter to all Cabinet Secretaries regarding the order. The letter could remind the Secretaries that the order was issued over a month ago; it could ask if any progress had been made within the agency to comply with the order's provisions; and it could ask each Secretary to assign one person from the agency to deal with privatization.

Once the letter were sent out, and individuals responsible for privatization designated, then I and the staff of the Competitiveness Council could hold meetings to coordinate the effort. Mr. DelliBovi said that he thought that one reason that the regulatory reform effort has been so successful is that agency representatives have been invited to regular meetings and asked for progress reports.

I would like to propose that the President send out such a letter, and that in that letter he ask the Vice President to take the lead in coordinating the privatization effort. This would show that the Administration is serious about the privatization effort. Under the order, each agency head is responsible for privatization in that agency's area, and so it is especially important to have some central coordination.

I and staff from the Competitiveness Council could begin to organize a series of meetings with agency representatives soon after the letter is sent out. The object of these meetings would be to identify ways in which agencies could help state and local governments to privatize, and to help speed privatization requests from these governments.

I have asked Sharon if I could meet with you to discuss this proposal.

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Sixth National Conference
April 27 & 28, 1992

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FYI

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Attached to
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PRIVATIZATION INTERNATIONAL, INC.**FAX TRANSMITTAL SHEET**

To: Richard Porter Date: July 8, 1992
Company: _____ City: _____
Fax No.: _____ From: John Stainback
Acct #: _____

Comments:

This fax consists of 3 pages including this sheet.

Phone: (212) 385 0067 / Fax: (212) 385 0069

14 Wall Street New York, New York 10005

PRIVATIZATION INTERNATIONAL, INC.

JOHN STAINBACK
President and CEO

July 8, 1992

Mr. Richard Porter
Counselor to the Vice President
The White House
Washington, D.C. 20501

Via Fax

Dear Richard:

I would like to propose that Privatization International, Inc. be hired by the Bush Re-Election Campaign Committee to leverage the President's accomplishments in the area of privatization and infrastructure. Our work would be focused on:

- Intermodal Surface Transportation Efficiency Act (ISTEA),
 - The Executive Order on Infrastructure Privatization, and
 - Enterprise Zones.
- We would serve as advisors to officials of the re-election campaign and/or the White House Staff.
 - We would prepare "white papers" on privatization. The focus would be on how state and local governments can use the legislation, (ISTEA and the Executive Order), which through the Administration's efforts is now in place, to generate enormous amounts of nontax revenue, as well as tax revenue, if assets were put back on the taxrolls.

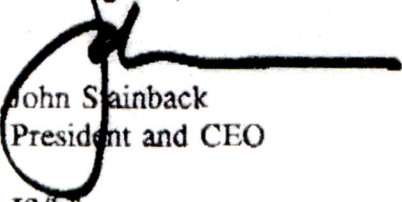
An additional primary objective will be to determine the potential economic impact of the legislation.

- We could also focus on developing implementation strategies to facilitate state and local governments' use of ISTEA and the Executive Order.
- We would expand the knowledge of privatization of the President and Vice President. The focus would be on the advantages for state and local governments from using the Comprehensive Privatization Program (CPP) approach. In other words, that there are nine types of privatization and that the privatization of services, and the sale or lease of government assets are only two of the nine types of privatization available to state and local governments.

The bottom line to our request for your consideration for our company to be an advisor is to provide the Administration with the expertise and documentation to demonstrate to the media, the various government-related associations, and the voters that the Administration has provided state and local governments with the means to solve their economic dilemma.

If you like our concept, I will be glad to work with you to refine our Scope of Work in order to start work immediately. As you know, November is rapidly approaching. I am in and out of Washington, D.C. regularly, so let me know if you want to further discuss our proposal.

Best regards,



John Stainback
President and CEO

JS/bf

7/13

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JOHN STAINBACK
President and CEO

July 8, 1992

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Counselor to the Vice President
The White House
Washington, D.C. 20501

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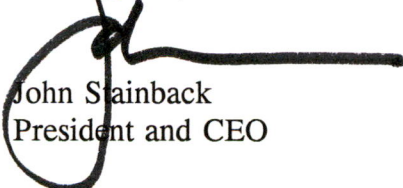
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Best regards,



John Stainback
President and CEO

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SUMMER 1992

INFRASTRUCTURE FINANCE

Journal for global development

**Road Blocks to
Toll Roads**

**The World of
Gordon Wu**

**MEXICO
BUILDS A
NEW MODEL
FOR
DEVELOPMENT**

José Angel Gurría
Undersecretary for
International
Financial Affairs

Privatization is the watchword from Washington to Kazakhstan

Bush Moves on Privatization

President Bush signed an Executive Order on infrastructure privatization at the end of April which aims to facilitate privatization transactions by state and local governments by allowing them a larger share of nontax revenues from the disposition of public assets valued between \$1.2 trillion and \$2 trillion. The order encourages conversion of public infrastructure assets into privately owned or leased facilities that will be supported by user charges.

By inducing private sector investments, the order also returns assets to the tax roll and creates a continuous stream of income for state and local governments. It would also greatly remove federal grant repayment

requirements and permit the creation of potentially large pools of public funds that could be used to finance new projects.

The potential implications of this order are enormous. According to the Tax Foundation, a nonprofit public policy organization, the cumulative total debt incurred up to 1991 by the 83,000 state and local governments in the U.S. is \$648.6 billion. Based on a current value of \$2 trillion, the 24-year average age of the nation's infrastructure, and a 50-50 split with the federal government of the \$900 billion initial capital cost, the nation's state and local governments could realize \$1.8 trillion by selling their public assets under the new Executive Order. Consequently, they would have to sell only one third of their assets to eliminate their total outstanding debt. One of the most immediate applications being discussed concern the possible privatization of airports in L.A. and Boston.

There are five major components in the Executive Order:

- Identifying the types of public assets to be privatized.
- Facilitating the privatization of infrastructure.
- Defining the basis for participating governments to share the proceeds from privatization.
- Outlining the use of the proceeds.
- Documenting the restrictions on the assets once the privatization process is completed.

— John Stainback, Chairman and CEO, Privatization International, Inc., New York. □

Distribution of Federal Aid to State and Local Government by Major Category (In Percent)

	1960	1975	1989
Physical Infrastructure			
Natural resources and environment ¹	1.5	4.9	2.9
Transportation	42.7	11.8	15.0
Community and regional development ²	1.6	5.7	3.7
Human Service			
Education, training, employment and social services	7.5	24.4	18.2
Health ³	3.0	17.7	29.5
Income security ⁴	37.5	18.8	27.2
Other	6.2	16.7	3.5
Total	100.0	100.0	100.0

¹ Primarily Environmental Protection Agency construction grants

² Primarily Housing and Urban Development grants; small portions were used for infrastructure improvements.

³ Primarily grants for Medicaid

⁴ Primarily grants for child nutrition, family support and housing assistance

Sources: Office of Technology Assessment, 1990; Office of Management & Budget,

Historical Tables; Budget of the U.S. Government Fiscal Year 1989



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SLATE
MEAGHER &
FLOM***Privatization*

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From:

Name: John P. Giraudo, Esq. Floor/Rm. 6-29
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April 27, 1992

The Honorable Dan Quayle
Vice President of the United States
The White House
Washington, D.C. 20005

Dear Mr. Vice President:

On behalf of my client, Viggo Butler of Lockheed Air Terminal, Inc. and myself, I want to thank you for taking the time to meet with us this morning about the privatization initiative you are considering. You and the President will do the nation a great service with this initiative.

In following up on our conversation, I would like to bring to your attention two serious problems I perceive will stem from requiring state and local governments to repay even a portion of their past federal grants as a condition to undertaking privatizations. The enclosed memorandum discusses the problems in greater detail.

As I understand it, at present some federal officials are asking that the proposed executive order require state and local governments to repay their past federal grants with respect to an asset less some accumulated depreciation of that asset. Such an approach is fraught with complexities which will only increase the transaction costs of privatizations. Firstly, land is typically not a depreciable asset. Hence, the full value of grants utilized to purchase land will need to be repaid. Secondly, not all assets can be depreciated on an accelerated basis under present law. Thirdly, a facility such as an airport or wastewater treatment plant is not normally treated as a single asset for depreciation purposes. Therefore, it will be necessary, in such cases, to identify individually the many hundreds, if not thousands of assets at an airport or wastewater treatment

The Honorable Dan Quayle
April 27, 1992
Page Two

plant which were purchased with federal grants, and ascertain the depreciation of the specific asset in question over its applicable useful life period. Finally, there will doubtless be some assets, such as runways, which simply will not be found in the IRS schedules since they have not usually been in private ownership and subject to depreciation.

The second problem I anticipate that may result from requiring recoupment of past federal grants is the legal cloud this could place on existing federal grant agreements. State and local governments sign a federal grant agreement when they receive federal grants. The grant agreement typically contains numerous conditions to the grant. The federal agencies exercise control over their state and local government grantees through these grant agreement conditions. For example, grant agreements administered by the FAA with respect to airports contain conditions which permit the FAA to regulate user fees at airports. If the federal government intends to recoup the undepreciated portion of its past federal grants, it will raise a question as to whether such recoupment extinguishes the grant conditions attached to the asset. Since the conditions were made binding on the state or local government by the receipt of the federal grants, it is at least arguable that repayment of the grants discharges the state or local government, as well as any potential new owner of the asset, from any further obligation to abide by the conditions. I assume this is not an intended policy outcome.

Mr. Butler and I remain available to answer any questions you may have about the foregoing or any other matter.

Very truly yours,


John P. Giraud

Enclosure

cc: William Kristol
Richard Porter
Viggo Butler

SHAW, PITTMAN, POTTS & TROWBRIDGE
A PARTNERSHIP INCLUDING PROFESSIONAL CORPORATION

MEMORANDUM

DATE: April 27, 1992
TO: Viggo Butler
FROM: Jim Burnley
Sam Chappell *JMC*

As you requested this morning, this memorandum summarizes current law on two issues: the accelerated depreciation schedules available under current federal tax law and the effect of repayment of federal grants on the grant assurances agreed to by the grantee when the grants were made.

I. Depreciation

We understand that it is the perception of some that the types of assets which may be transferred to the private sector would be subject to accelerated Internal Revenue Service depreciation schedules which provide for greater than straight line depreciation.^{1/} Under current law, however, real property is generally depreciated on a straight line basis. Residential rental property (including public housing) is subject to a straight line depreciation schedule over a period of 27.5 years, while the depreciation schedule for non-residential real property (i.e., office buildings, warehouses and industrial facilities) is straight line over 31.5 years. In each case only the cost of improvements may be depreciated; in no event may the cost of the underlying land be depreciated.

Certain exceptions apply to the foregoing rules relating to real property. For example, the cost of municipal sewers, telephone central office buildings, electric utility hydraulic

^{1/} In recent years federal tax law relating to depreciation schedules has undergone significant changes. Therefore, if the depreciation schedules to be utilized were determined based upon the federal tax law in effect on the date each asset purchased with grant funds was placed in service rather than current federal tax law, the result would prove administratively burdensome and possibly unworkable.

production plants (including the cost of dams, flumes, canals and waterways), and electric utility steam production plants may be depreciated over twenty years using a 150 percent declining balance schedule. Real property qualifying for a 150 percent declining balance depreciation schedule over fifteen years includes waste water treatment plants, telephone distribution plants, service station buildings, liquefied natural gas plants, electric utility nuclear production plants, electric utility combustion turbine production plants, pipeline transportation facilities, water transportation facilities, railroad wharves and docks, and industrial steam and electric generation and/or distribution systems. Land improvements such as sidewalks, roads, canals, and bridges also generally qualify for a fifteen-year 150 percent declining balance depreciation schedule.

Most other classes of assets would fall under the most rapid depreciation schedule (200 percent declining balance) over shorter time periods. These classes include automobiles, trucks, office equipment, manufacturing equipment, waste reduction resource recovery plants, and single purpose horticultural structures.

II. Grant Assurances May Be Voided Upon Repayment

You have repeatedly indicated that Lockheed is willing to accept whatever grant assurances have been agreed to by the public entity from which you would buy or lease an airport. Specifically, you are agreeable to a requirement that any such airport remain a public use airport.

However, some federal officials are reportedly arguing that a sale of a federal aid facility should trigger repayment of federal grants which were invested in that facility. In the event of repayment of federal aid, a strong argument would be made that the grant assurances would no longer be effective.

For example, grant assurances given to the FAA by publicly-owned airports expire after 20 years. There is no statutory provision or FAA regulation that requires this arrangement. Rather, an FAA "order" requires such a provision in all grant agreements. Thus, grant assurances given to the FAA by publicly-owned airports should be considered contractual obligations. If the consideration paid by the federal government (i.e., grant funds) is repaid in full, then the contract should be considered dissolved, and the grantee should have no further contractual obligation to adhere to the grant assurances.