



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

November 2, 2001

The Honorable Kent Conrad
Chairman
Committee on the Budget
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman,

I am writing to respond to your request regarding my views on a proposal to allow the Air Force to establish a multi-year program for the lease of one hundred B-767 air refueling aircraft and to circumvent the scoring rules by waiving the lease-purchase rule. I appreciate your views regarding the need for these aircraft, but I believe it is more important than ever that we properly record the obligations and costs of the government.

We have reviewed the proposed lease and it would clearly qualify as a lease-purchase under the Budget Enforcement Act (BEA) scoring rules. Based on current information, the proposal would be a lease purchase because the present value of the lease payments would likely exceed 90 percent of the fair market value of the aircraft, ownership would transfer to the Air Force during or at the end of the lease period, and the aircraft would be specially modified for the government's use. Based on preliminary estimates, the lease should be scored with about \$13 billion of budget authority in 2002. The proposed waiver of the lease purchase rule would not change the obligation or the costs the government would incur and would distort the budget by reducing the recorded cost to only about \$18 million in 2002.

The BEA lease scoring rules were specifically designed to encourage the use of financing mechanisms that minimize taxpayers' costs, by eliminating the unfair advantage provided to lease-purchases by the previous scoring rules. Prior to the BEA, agencies only needed budget authority for the first year's lease payment, even though the agreement was a legally enforceable commitment to fully pay for the asset over time. In the late 1980s, GSA used this loophole to enter into 11 lease-purchase agreements with a total long-term cost of \$1.7 billion, but only budgeted the first year's lease payment. The scoring hid the fact that these agreements had a higher economic cost than traditional direct purchases, and in some cases allowed projects to go forward despite significant cost overruns. For example, the Ronald Reagan Building, which was acquired by lease-purchase and was originally estimated to cost \$362 million, ended up costing more than \$800 million to build.

If the proposed lease of B-767 aircraft includes a waiver of the lease-purchase scoring rule, I would view it as a violation of the agreement between the Congress and the President to limit appropriations to \$686 billion in FY 2002. For the reasons stated above, I would oppose its inclusion in any legislation presented to the President.

Sincerely,

A handwritten signature in cursive script, appearing to read "Mitchell".

Mitchell E. Daniels, Jr.

Tanker Preliminary Lease vs. Buy Analysis

Note: Calculations are based on sparse information and estimates of numbers that are not yet firm.

<u>Year</u>	<u># a/c</u>	<u>Procurement Leasing Costs</u>	<u># a/C</u>	<u>Direct Purchase Costs*</u>
FY02	0	0	0	0
FY03	0	0	0	120
FY04	0	0	4	600
FY05	4	80	11	1650
FY06	15	300	20	3000
FY07	35	700	20	3000
FY08	55	1100	20	3000
FY09	75	1500	20	3000
FY10	95	1900	5	750
FY11	100	2000		
FY12	100	2000		
FY13	100	2000		
FY14	100	2000		
FY15	100	2000		
FY16	96	1920		
FY17	85	1700		
FY18	65	1300		
FY19	45	900		
FY20	25	500		
FY21	5	100		
FY22	0	0		
Total		22000		15120
Net Present Value		11775		10965

Notes:

o Assumes that each airplane costs \$150 million. In this case, lease-purchase is over \$800 million, or about 7%, more expensive than than direct purchase.

o If the purchase price is higher than \$160 million then direct purchase is more expensive.

o This result means that the lease price quoted is a very good price. In such a situation the Air Force should be able to negotiate a very good direct purchase price.

Scoring Implications

In the first year \$13,428 million (the full cost of the program) would be scored on a net present value basis in accordance with the scoring rules, whereas the AF, using annual scoring, would score \$18 million (its first year cost for Milcon not shown above).