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REINVENTING THE GOVERNMENT CORPORATION†

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In this article, Professor A. Michael Froomkin takes a comprehensive look at federal government corporations, focusing on the legal implications arising from their character as both public and private entities. Federal government corporations often enjoy public advantages, including national establishment, tax and securities law exemptions, sovereign immunity, and privileged access to capital. As a result, they face diminished market discipline and may not be as efficient as their proponents claim unless they have similarly situated competitors. Because some federal government corporations are owned wholly or partly by private parties, yet maintain control over public funds and functions, their legal status raises important constitutional questions concerning accountability, separation of powers, and nondelegation.

In his 1993 Reinventing Government *program, Vice President Al Gore encouraged the proliferation of federal government corporations, obscure government devices whose legal status remains unclear even after 200 years as part of our national life. Professor Froomkin suggests that some regulatory reform is needed before this suggestion is adopted. After a critical analysis of existing proposals, he offers alternatives designed to increase accountability to both government and market discipline, thus ensuring that private parties do not profit at public expense, and limiting taxpayer liability in the event of insolvency.*

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American concern about inefficiency in government dates back to the First Continental Congress.[1] In the 200 years since then, reorganization plans have come and gone, but the fundamental structures of government departments have changed only infrequently, although their jurisdictions have changed constantly, and usually have grown. Vice President Al Gore's *Reinventing Government* program[2] is only the latest in a long series of plans to reorganize or reinvigorate the federal government.

One of the many devices proposed by the Vice President to create a "government that works better and costs less" is an often tried yet little-known type of government entity called a federal government corporation (FGC). Congress has created a new government corporation every year or so since World War II. It created the United States Enrichment Corporation in 1992,[3] and the Corporation for National and Community Service (AmeriCorps) in 1993.[4] Congress recently has considered new federal corporations for everything from aid to small businesses[5] to the regulation of boxing,[6] and is now considering proposals for a Technology Transfer and Commercialization Financing Corporation.[7] *Reinventing Government* would add to the list by semiprivatizing much of the Federal Aviation Administration into the U.S. Air Traffic Services Corporation, an FGC that would, the administration hopes, borrow funds (which would not be counted towards the national debt) to modernize air traffic control.[8]

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1. Indeed, one of the first resolutions passed by the Continental Congress established an Inspector General to root out "abuses which prevail in the different departments." PAUL C. LIGHT, MONITORING GOVERNMENT 25 (1993).

2. ALBERT GORE, CREATING A GOVERNMENT THAT WORKS BETTER & COSTS LESS (1993) [hereinafter NATIONAL PERFORMANCE REVIEW]. For a skeptical analysis of the program, see Ronald C. Moe, *The Reinventing Government Exercise: Misinterpreting the Problem, Misjudging the Consequences*, 54 PUB. ADMIN. REV. 111 (1994).

3. *See* Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 (1993); *cf.* Sheila Kaplan, *Uranium-Enrichment Firm Enriches Lawyers*, LEGAL TIMES, Oct. 24, 1993, at 2 ("biggest beneficiaries . . . have been the law firms and consulting firms that received lucrative contracts").

4. *See* National and Community Service Trust Act of 1993, Pub. L. No. 103-82, 107 Stat. 785.

5. Small Business Credit Availability Act of 1993, H.R. 660, 103d Cong., 2d Sess. (1993) (proposing creation of Venture Enhancement and Loan Development Administration for Smaller Undercapitalized Enterprises ("Velda Sue")).

6. Professional Boxing Corporation Act of 1993, H.R. 2607, 103d Cong., 2d Sess. (1993).

7. Federal Technology Commercialization and Credit Enhancement Act of 1995, H.R. 80, 104th Cong., 1st Sess. (1995).

8. *See* NATIONAL PERFORMANCE REVIEW, *supra* note 2, at 149; GENERAL ACCOUNTING OFFICE, MANAGEMENT REFORM: IMPLEMENTATION OF THE NATIONAL PERFORMANCE REVIEW'S RECOMMENDATIONS 288-89 (1994) [hereinafter NPR II] (noting that the administration is drafting legislation to respond to congressional objections); GENERAL ACCOUNTING OFFICE, AIR TRAFFIC CONTROL: OBSERVATIONS ON PROPOSED CORPORATION (1994) (criticizing proposal); *Air Control System Needs Reform*, ATLANTA J. & CONST., May 5, 1994, at A14 (reporting that corporation will be named U.S. Air Traffic Services Corp. and "be free of red tape"); Greg Gordon, *Air Safety System Still on the Ground*; *New Proposals May Fuel FAA Overhaul That Never Took Off*, STAR TRIB., Jan. 24, 1995, at 4A (suggesting that proposal's popularity is in-

Although federal corporations have been a part of the national life for 200 years,[9] they remain obscure—a status they no doubt find convenient. Today more federal corporations exist than ever before in peacetime, and the number keeps growing. While toiling in obscurity, they manage communication satellites, museums, railroads, and power generation. They provide specialized credit and insurance for housing and agriculture. They exist as accounting devices to hide the true size of the budget deficit, as nonprofit organizations, and as highly profitable and highly leveraged economic colossi. The most profitable corporations, which provided a total of about $5 trillion in credit and insurance in 1995, also have approximately $1.5 trillion in securities and other debt outstanding. These organizations are capable of squirreling away $2 billion for a rainy day, while pleading poverty to Congress.[10]

This article seeks to shed some light on these organizations and asks some hard questions about whether these bodies are properly accountable for the vast sums they borrow, lend, and spend, and for the public power and benefits they enjoy. More is at stake than just money. Left to run loose, government corporations threaten to infringe basic principles of democratic accountability.

Some federal government corporations are wholly owned by the government and are clearly state actors, resembling ordinary agencies in many ways.[11] Others, however, are owned wholly or partly by private persons.[12] These mixed-ownership and private corporations enjoy

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creasing); Richard M. Weintraub & John Burgess, *U.S. to Shake Up Air Traffic Bureaucracy*, WASH. POST, May 2, 1994, at A1 (describing proposal). *But see* BNA Management Briefing, *Mineta Says House Transportation Panel to Reject Air Traffic Control Corporation* (Mar. 10, 1995) (describing opposition from Congress); Clyde Linsley, *Holding Pattern*, GOV'T EXECUTIVE, January 1994, at 32 (describing administration's second thoughts after opposition from users of general aviation).

9. The first national government corporation predates the Constitution. The Continental Congress chartered the Bank of North America in 1781, and the Superintendent of Finance purchased about 60% of the stock. *See* LAWRENCE LEWIS, JR., A HISTORY OF THE BANK OF NORTH AMERICA (1882). The United States established its first federal government corporation, the Bank of the United States, in 1791, but made relatively infrequent use of the device until the 20th century.

10. *See* UNITED STATES GOV'T, BUDGET OF THE UNITED STATES GOVERNMENT FOR FISCAL YEAR 1996: ANALYTICAL PERSPECTIVES 121 (1995) (totalling loans, loan guarantees, and insurance); Stephen Labaton, *Bailout Agency Squirrels Away Over $2 Billion*, N.Y. TIMES, Apr. 26, 1992, § 1, at 1 (describing how Resolution Trust Corporation hid $2 billion fund from Congress in order to be able to plead for extra appropriations). "I hate to say it, but $2 billion is not a lot of money," a spokesman said. *Id.*

11. The Supreme Court recently removed whatever doubt there may have been on this point by holding that Amtrak, a wholly owned and federally controlled government corporation, is subject to the same First Amendment restrictions as any other federal actor. *See* Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961 (1995).

12. *Public* as used in this article means traditionally and frequently entrusted to government in the United States. Although courts sometimes suggest that certain functions are inherently governmental or inherently private, the use of the terms *public* and *private* in this article is intended only to denote their traditional usages, or the result of an exercise in classification, and not to assert any inherent status. *See generally* David M. Lawrence, *Private Exercise of Govern-*

a combination of federal and private powers and obligations, and therefore may not be state actors in a constitutional sense. Thus, they may be less accountable for their actions even though they are creatures of a national policy.

By allowing private ownership and private control of publicly funded and ostensibly publicly directed activities, the structure of some federal government corporations weakens accountability. The powers granted to privately controlled federal government corporations are usually economic, but a few federal government corporations have more public functions. The uncertain legal status of some federal government corporations also raises separation of powers and nondelegation concerns because it weakens presidential, as well as congressional, control over the federal administrative machinery and over important sectors of the national economy. Placing public funds, public monopolies, or public power, in the hands of unelected, unappointed, almost certainly unimpeachable, and largely unaccountable private parties poses a serious and largely unexplored challenge to accountable, efficient, democratic national government.

The Vice President's report suggests that a government corporation can harness the efficiency of the private sector for the service of the public. Neither a privatized existing program, nor an ordinary government department, the corporation is supposed to combine the flexibility of a business with the public purpose and public duties of government. Reality is not always that simple. Federal government corporations enjoy public advantages unavailable to state-chartered firms, including national establishment, exemption from state taxes and from portions of the securities laws, privileged access to capital, and even sovereign immunity. These advantages effectively free some federal corporations from market discipline. In addition, uncertainty as to whether to characterize federal government corporations as private bodies or coordinate departments hampers federal regulation and bureaucratic control. Similarly, otherwise simple civil cases become complicated, as courts struggle to determine whether an entity is a private party, a state actor, or part of the state itself.[13]

This article concentrates on federal government corporations in which the federal government owns shares or appoints directors.[14] It

mental Power, 61 IND. L.J. 647, 647 n.1 (1986) (collecting cases and regulations attempting to define "traditional governmental functions").

13. *See, e.g.*, American Nat'l Red Cross v. S.G., 112 S. Ct. 2465, 2476 (1992) (holding, by only five to four, that federal charter conferred original "arising under" jurisdiction on the federal courts over all matters relating to that corporation).

14. Thus, this article does not discuss national banks, *see* 12 U.S.C. §§ 21, 35, 40, 41, 215c, 377, 501a, 1440, 1467a, 1817, 2254, 3102 (1988 & Supp. V 1993), which have federal charters but no government ownership or directors. In addition to the entities discussed in this article, there are also a large number of patriotic and charitable nonprofit organizations, such as the Red Cross, *see* 36 U.S.C. §§ 1-9, 13 (1988) (National Red Cross charter), and Veterans of Foreign Wars, *see*

begins with a brief description of the creation and powers of federal government corporations. The article then explains how some federal government corporations operate under a legal regime that enables them to escape accountability to Congress, the President, and the private market. As a result, their private investors, shareholders, and managers may benefit more than the public they are intended to serve. The article concludes with a critical analysis of previous regulatory reform proposals and offers alternative proposals designed to increase accountability to government discipline and market discipline, ensure that private parties do not profit at public expense, and nonetheless limit taxpayers' contingent liability if a federal corporation becomes insolvent.

I. Creation of Federal Government Corporations

Today, more than forty[15] FGCs are directly chartered by Con-

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36 U.S.C. §§ 111-20 (1988) (Veterans of Foreign Wars charter), that have federal charters but receive no government funds, exercise no federal powers, and are entirely responsible for managing their own affairs. *See* 36 U.S.C. §§ 1-4815 (1988 & Supp. V 1993) (containing charters of 80 federal private nonprofit organizations, including National Academy of Sciences and Veterans of Foreign Wars of the United States); *see also* Pearl v. United States, 230 F.2d 243 (10th Cir. 1956) (holding Civil Air Patrol, charter codified at 36 U.S.C. §§ 201-08 (1988), is not a federal agency and its pilots are not federal employees). Otherwise private societies that participate as the U.S. representative in international organizations, such as the U.S. arm of the Red Cross and the U.S. Olympic Committee, are borderline cases not considered in detail in this article. *See, e.g.*, San Francisco Arts & Athletics, Inc. v. United States Olympic Comm., 483 U.S. 522, 543-45 (1987) (holding that neither the U.S. Olympic Committee's federal charter nor the fact that it represented U.S. in international athletic competitions made it a state actor). *But see id.* at 548-49 (Brennan, J., dissenting) (reaching opposite result). Further, the federal government owns, controls, or has caused to be established a small number of corporations not chartered directly by Congress, including the Corporation for Public Broadcasting, 47 U.S.C. §§ 396-99b (1988 & Supp. V 1993), and the American Institute in Taiwan, 22 U.S.C. §§ 3301-10 (1988 & Supp. V 1993). The American Institute in Taiwan substitutes for a U.S. Embassy since the United States no longer recognizes the government of the Republic of China.

This article also does not discuss the 40-plus federally funded research and development centers (FFRDCs), such as Rand Corporation and the Jet Propulsion Laboratories, although they are worthy of scrutiny. Together these entities have annual obligations of over $6 billion, and "experience . . . illustrates that institutions initially created to fulfill valid needs may be utilized for questionable purposes." Harold Seidman, *Government Corporations in the United States*, 22 Optimum 40, 43 (1991); *cf.* 48 C.F.R. § 35.017 (1994) (setting out policy and basic rules for FFRDCs).

15. The Government Corporation Control Act (GCCA), 31 U.S.C. §§ 9101-10 (1988 & Supp. V 1993) includes a list of wholly owned and mixed-ownership government corporations, but this list is not exhaustive. Some government corporations not subject to the GCCA have federal charters, which are found in various parts of the U.S. Code. Others are incorporated in the District of Columbia or in a state, and thus their existence is not always reflected in the GCCA. U.S. Gen. Accounting Office, 100th Cong., 2d Sess., Profiles of Existing Government Corporations 232 (Comm. Print 1989) [hereinafter GAO Profiles] contains a relatively inclusive list of 45 corporations including entities such as the U.S. Postal Service, which is officially "an independent establishment in the executive branch of the Government," 39 U.S.C. § 201 (1988), may sue and be sued in its own name, but does not have a corporate charter. *See* 39 U.S.C. §§ 101-5605 (1988 & Supp. V 1993). The GAO list does not include some corporations owned or controlled by the federal government that lack federal statutory charters.

gress,[16] including such diverse bodies as the Federal National Mortgage Association (Fannie Mae),[17] the Legal Services Corporation (LSC),[18] the Tennessee Valley Authority (TVA),[19] the National Endowment for Democracy,[20] the Commodity Credit Corporation,[21] the Student Loan Marketing Association (Sallie Mae),[22] and the Communications Satellite Corporation (COMSAT).[23] The recently created Resolution Funding Corporation (REFCORP),[24] charged with borrowing funds for the use of the Resolution Trust Corporation (RTC) which is recapitalizing insolvent savings and loans, is only the latest in a line of FGCs created to channel funds to a specific sector of the economy. Indeed, from 1965 to 1988, the outstanding credit assistance and insurance provided by FGCs grew by over 1000%, to about $5 trillion.[25] The General Accounting Office (GAO) has warned that much of the hundreds of billions in direct loans by FGCs is at risk, although the Treasury takes a more nuanced view.[26]

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16. *Congress* is used frequently in this article as a convenient shorthand for the various actors who make up the legislative process. Obviously, there is not a simple entity called Congress that can "think" something; in any case, Congress is not the only institution that decides national policy nor, arguably, even the most important one. Legislation originates in many places: the White House, the agencies, organized constituencies, and even Congress itself. *See generally* WILLIAM ESKRIDGE & PHILLIP FRICKEY, LEGISLATION: STATUTES AND THE CREATION OF PUBLIC POLICY (1988).

17. 12 U.S.C. §§ 1716b-23i (1988 & Supp. V 1993).

18. 42 U.S.C. §§ 2996-96k (1988 & Supp. V 1993).

19. 16 U.S.C. §§ 831-31dd (1988 & Supp. V 1993).

20. National Endowment for Democracy Act, 22 U.S.C. §§ 4411-15 (1988 & Supp. V 1993) (incorporating National Endowment for Democracy in 1983).

21. 15 U.S.C. § 714 (1988 & Supp. V 1993).

22. 20 U.S.C. § 1087-2(a)-(g) (1988 & Supp. V 1993).

23. 47 U.S.C. §§ 731-44 (1988).

24. REFCORP was created by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (codified as amended at 12 U.S.C. § 1441b (Supp. V 1993)). For a description of REFCORP's powers and duties see Marirose K. Lescher & Merwin A. Mace III, *Financing the Bailout of the Thrift Crisis: Workings of the Financing Corporation and the Resolution Funding Corporation*, 46 BUS. LAW. 507, 521-28 (1991).

25. U.S. GEN. ACCOUNTING OFFICE, FEDERAL CREDIT AND INSURANCE 16, 22-23 (1989) [hereinafter GAO CREDIT STUDY].

26. GAO CREDIT STUDY, *supra* note 25, at 25-27. *Compare* THOMAS H. STANTON, A STATE OF RISK (1991) (arguing that certain major government corporations could soon create federal losses on the order of the savings and loan (S&L) crisis) *with* SECRETARY OF THE TREASURY, REPORT ON GOVERNMENT SPONSORED ENTERPRISES 6 (1991) [hereinafter TREASURY GSE STUDY] (stating "there is no imminent financial threat" from the activities of five large FGCs surveyed) *and* UNITED STATES GOVERNMENT, FY 1990 BUDGET at II-227 [hereinafter 1990 U.S. BUDGET] (concluding direct risk to taxpayers is not large). *See also* UNITED STATES GOVERNMENT, BUDGET OF THE UNITED STATES GOVERNMENT: ANALYTICAL PERSPECTIVES FY 1995 134 [hereinafter 1995 BUDGET ANALYSIS] (estimating present value of losses from five largest GSE's at between zero and $1 billion, with variation depending on performance of Farm Credit System).

Recently, the Office of Federal Housing and Enterprise Oversight (OFHEO), part of HUD, announced that the Federal Home Loan Mortgage Corp. and the Federal National Mortgage Association were well capitalized. BNA's Banking Report, *Freddie, Fannie Receive High Marks from Safety and Soundness Regulator* (Feb. 4, 1994).

Meanwhile, the U.S. Office of Management and Budget has conducted individualized risk assessments for all federal agencies, including wholly owned FGCs, which it considers "high risk," rating them on a scale of 1 to 3. The Federal Crop Insurance Corporation (with $100 million at

A. *Federal Power to Create Corporations*

The federal government's authority to charter corporations derives from the Necessary and Proper Clause of the Constitution,[27] as expounded in Chief Justice Marshall's decisions in *McCulloch v. Maryland*[28] and *Osborn v. Bank of the United States.*[29] *McCulloch* established that, despite the lack of an applicable enumerated federal power, the Necessary and Proper Clause of the Constitution allows the federal government to charter and use a private entity for the public purpose of banking. The Second Bank of the United States, the subject of both cases, was a federally chartered corporation with 80% of its stock owned by private persons and 20% by the United States. The Bank had twenty-five directors, five of whom were appointed by the President from among the stockholders, subject to Senate confirmation. The remaining twenty directors were elected by the other shareholders.[30] The Second Bank, like its precursor, had extensive power over the money supply and, consequently, over the monetary

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risk) was rated "1," meaning that the FGC has a "corrective action plan [in place and showing results which] . . . will either eliminate the risk or reduce the risk to an acceptable level." Rated "2," meaning the FGC has a plan but it is too new to be evaluated, or to show results yet, were the Farm Credit Administration (including the Farm Credit Insurance Corporation), criticized for lack of control over improper expenditures and an internal control system that "cannot be salvaged," and the Pension Benefit Guaranty Corporation, criticized for "serious weaknesses . . . in all major financial systems and subsystems" putting premium collection at risk. No FGC was Rated "3," a category meaning "OMB has reservations" about the department's actions. In addition OMB noted that Ginnie Mae's oversight of its contractors was inadequate, but did not attempt to quantify the risk. 1995 BUDGET ANALYSIS, *supra*, at 275-98.

There are grounds for some concern about the Pension Benefit Guaranty Corporation (PBGC). According to one GAO report, although the PBGC faces no appreciable short-term risk of insolvency, its long-term prospects are more uncertain. In particular, the PBGC faces $12 billion to $20 billion in unfunded liabilities in single-employer plans which may result in future losses. GENERAL ACCOUNTING OFFICE, FINANCIAL AUDIT: PENSION BENEFIT GUARANTY CORPORATION'S 1992 AND 1991 FINANCIAL STATEMENTS 7 (1993).

27. U.S. CONST. art. I, § 8, cl. 18.

28. McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 409-12 (1819) (upholding constitutionality of Second Bank of the United States).

29. Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738, 859-60 (1824). Congress also based its authority on the Coinage Clause, U.S. CONST. art. I, § 8, cl. 5. *See* HOUSE WAYS & MEANS COMM., REPORT ON THE PRESIDENT'S MESSAGE, REGISTER OF DEBATES, app. at 104 (1830), *reprinted in* 1 PAUL SAMUELSON & HERMAN E. KROOSS, DOCUMENTARY HISTORY OF BANKING AND CURRENCY IN THE UNITED STATES 660 (1969). *See generally* RALPH C.H. CATTERALL, THE SECOND BANK OF THE UNITED STATES (1903); BRAY HAMMOND, BANKS AND POLITICS IN AMERICA (1957). More modern cases revisiting this issue include Federal Land Bank v. Bismark Lumber Co., 314 U.S. 95, 102-03 (1941) (holding Necessary and Proper Clause allows Congress to immunize corporation from state taxation) and Pittman v. Home Owners' Loan Corp., 308 U.S. 21, 33 (1939) (same).

30. Act of Apr. 10, 1816, 3 Stat. 266, 269 (chartering the Second Bank of the United States), *reprinted in* 1 SAMUELSON & KROOSS, *supra* note 29, at 460, 466. The President was forbidden to nominate any person who was already the director of another bank. *Id.* The procedure for weighing votes was complex and progressive among those wealthy enough to find the $100 per share offering price. Each individual's first share got one vote, the next eight got a half vote, the next twenty got a quarter vote, the next thirty got a sixth, and so on. Every share above 100 got a tenth of a vote, but no person could cast more than thirty votes regardless of the number of shares they hold. *Id.* § 11, ¶ 1.

policy of the United States.[31] Although the President could remove any of the five directors he appointed, he had no such power over the privately elected directors who constituted a comfortable majority. The Bank, therefore, ensured that monetary policy remained in the control of the wealthy citizens and private banks, who could afford to purchase shares.[32] Neither *McCulloch* nor *Osborn* stated that Congress has a general power to create corporations for any purpose. Instead, those cases held that Congress's power to create a Bank derives from, and exists in order to effectuate, its power to manage the fiscal affairs of the United States.[33]

Today, as in the eighteenth and nineteenth centuries, FGCs are separate legal persons chartered directly by an act of Congress or by persons acting pursuant to congressional authorization. The statute creating the corporation may provide a federal charter or may specify incorporation under the laws of the District of Columbia.[34] Every FGC, however created and governed, enjoys a separate legal personality,[35] and, unless there is legislation to the contrary, its investors, in-

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31. The Second Bank was structurally similar to its predecessor, the first Bank of the United States, established in 1791. *See* Act of Feb. 25, 1791, 1 Stat. 191. However, the first Bank's directors were elected by all the stockholders, and the President had no special power of appointment.

32. *See* Act of Apr. 10, 1816, 3 Stat. 266 (chartering the Second Bank of the United States), *reprinted in* 1 SAMUELSON & KROOSS, *supra* note 29, at 460, 466.

33. McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 421 (1819). "Let the end be legitimate, let it be within the scope of the constitution, and all means which are appropriate, which are plainly adapted to that end, which are not prohibited, but consist with the letter and spirit of the constitution, are constitutional." Similarly,

> the bank is not considered as a private corporation, whose principal object is individual trade and individual profit; but as a public corporation, created for public and national purposes. That the mere business of banking is, in its own nature, a private business, and may be carried on by individuals or companies having no political connection with the government, is admitted; but the bank is not such an individual or company. It was not created for its own sake, or for private purposes. It has never been supposed that congress could create such a corporation.

Osborn, 22 U.S. (9 Wheat.) at 859-60.

The Supreme Court later relied on a similar reasoning, if weaker facts, when upholding the creation of the Federal Land Banks system in which the federal government held stock. Following *McCulloch* and *Osborn*, the Supreme Court stressed the Land Banks' function as "depositaries of public moneys and purchasers of Government bonds" to bring them within Congress's Necessary and Proper Clause power. Smith v. Kansas City Title & Trust Co., 255 U.S. 180, 211 (1921). Neither of these objects were among the chief purposes of the act, and the banks had not actually been used as public depositaries. JOHN THURSTON, GOVERNMENT PROPRIETARY CORPORATIONS IN THE ENGLISH-SPEAKING COUNTRIES 27 (1937).

34. Although a federal statute of incorporation preempts the D.C. corporate law, incorporation in Washington, D.C. can give a corporation powers that may extend beyond what a well-informed Congress would desire, e.g., powers to make loans to employees and others, and distribute assets upon dissolution. *See* RONALD C. MOE, CONGRESSIONAL RESEARCH SERV., ADMINISTERING PUBLIC FUNCTIONS AT THE MARGIN OF GOVERNMENT: THE CASE OF FEDERAL CORPORATIONS 35-36 (1983).

35. Bank of the United States v. Planters' Bank of Ga., 22 U.S. (9 Wheat.) 904, 907 (1824) (Second Bank of the United States); *see also* United States *ex rel.* Skinner & Eddy Corp. v. McCarl, 275 U.S. 1, 11 (1927) (United States Shipping Board Emergency Fleet Corp.); Olson v. United States Spruce Prod. Corp., 267 U.S. 462, 462-63 (1925) (describing the FGC as "a distinct corporate entity [that] may be sued as any private corporation"); Sloan Shipyards Corp. v.

cluding the United States, presumably enjoy limited liability.[36] Therefore, the United States is not legally responsible for the debts of even a wholly owned FGC unless there is a constitutional, statutory, or federal common-law rule to the contrary.

B. *Types of Federal Government Corporations*

Congress ordinarily charters a federal corporation by legislation rather than delegating the power to an executive branch official. If the legislation specifies incorporators, they are usually government officials. The legislation incorporating an FGC ordinarily sets out its purposes, powers, structure, and obligations.[37]

Although the exact mix of powers granted to FGCs varies, almost every FGC has permanent succession and the following capacities: to sue and be sued[38] (and to settle cases without Justice Department authorization[39]), to make contracts, to hold property, and to borrow.[40] Almost all FGCs are governed by a board of directors elected by the shareholders or appointed by the President, sometimes subject to Senate confirmation.[41] In keeping with the long-held theory that FGCs should be run on "business-like" principles, many FGCs are exempted from civil service rules regarding pay,[42] employee ten-

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United States Shipping Bd. Emergency Fleet Corp., 258 U.S. 549 (1922) (Fleet Corp.); United States v. Strang, 254 U.S. 491, 493 (1921) (same); Panama R.R. v. Bosse, 249 U.S. 41 (1919).

Separate legal personality does not, however, necessarily imply that the corporation may be subject to a *Bivens* action. *See* Federal Deposit Ins. Corp. v. Meyer, 114 S. Ct. 996 (1994) (holding that *Bivens* action cannot be brought against FDIC).

36. *See infra* text accompanying notes 56, 60, 276-85 (discussing implicit guarantee).

37. *E.g.*, 12 U.S.C. §§ 1716-1723i (1988 & Supp. V 1993) (establishing Fannie Mae).

38. *See Meyer*, 114 S. Ct. at 1000-04 (reading FSLIC sue-and-be-sued clause as "broad" waiver of sovereign immunity); United States v. Nordiz Village, 503 U.S. 30, 34 (1992) (same); Reconstruction Fin. Corp. v. Menihan Corp., 312 U.S. 81, 85 (1941) (deciding on equitable grounds to read sue-and-be-sued clause in corporate charter as broad waiver of sovereign immunity); Federal Housing Admin. v. Burr, 309 U.S. 242, 245 (1940) (stating that effect of sue-and-be-sued clause is to make agency "not less amenable to judicial process than a private enterprise under like circumstances would be"). In addition, the power of a government corporation to sue and be sued has been implied in the absence of a specific legislative enactment. Keifer & Keifer v. Reconstruction Fin. Corp., 306 U.S. 381, 389-93 (1939). However, many wholly owned government corporations rely on the Justice Department to conduct their litigation. *See* GAO PROFILES, *supra* note 16.

39. Ordinarily, only the Attorney General may represent the United States in court unless a statute provides otherwise. 28 U.S.C. § 516 (1988 & Supp. V 1993); *see also* 5 U.S.C. § 3106 (1988).

40. The power to borrow is usually subject to the limits in the GCCA. *See supra* note 15.

41. Some FGCs that are wholly owned by the federal government have a board of directors composed of federal officials who serve ex officio. For example, the Neighborhood Reinvestment Corporation, 42 U.S.C. §§ 8101-07 (1988 & Supp. V 1993), has six directors, all ex officio. Ex officio FGC directors sometimes delegate the task of sitting on the board to their subordinates. *See* 6 Op. Off. Legal Counsel 257, *Delegation of Cabinet Members' Functions as Ex Officio Members of the Board of Directors of the Solar Energy and Energy Conservation Bank* (1982).

42. David E. Lilienthal & Robert H. Marquis, *The Conduct of Business Enterprises by the Federal Government*, 54 HARV. L. REV. 545, 566, 576 (1941) (Lilienthal was then director and vice-chairman of the TVA).

ure,[43] and other rules such as the Freedom of Information Act. Indeed, some FGCs are exempted from the Government Contract Control Act which is supposed to regulate how federal corporations are created and supervised.[44] From a bureaucratic point of view, most government corporations enjoy budgetary freedoms denied to ordinary federal agencies.[45] Unless limited by specific provisions in its statute, an FGC is not subject to the "use it or lose it" rule that requires most agencies to return unexpended funds to the Treasury at the end of a fiscal year.[46] Similarly, FGCs, unlike agencies, can enter into multi-year commitments, conduct long-term planning,[47] and buy or sell assets without complying with federal procurement and disposal regulations. Some FGCs may ignore government personnel ceilings, and, in general, escape federal budget restraints while retaining some of the advantages of this government link.[48]

Many, but by no means all, FGCs issue stock, some or all of which is owned by legal or natural private (nongovernmental) persons. Congress usually defines an FGC as "wholly owned," "mixed-ownership," or "private," although Congress has chartered a number of corporations without specifying their status.[49]

In *wholly owned federal corporations*, such as the Commodity Credit Corporation, the federal government holds 100% of the equity and exercises 100% of the votes on the board of directors or other governing body.[50] Several statutes creating wholly owned government

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43. *Id.* at 549-50 (corporate form attractive due to autonomous character). Employees of wholly owned FGCs ordinarily do not have the right to strike. NATIONAL ACADEMY OF PUB. ADMIN., CONSIDERATIONS IN ESTABLISHING THE PATENT AND TRADEMARK OFFICE AS A GOVERNMENT CORPORATION 16 (1989). For a discussion of the complex issue of labor relations in government corporations, see Eric J. Pelton, *Privatization of the Public Sector: A Look at Which Labor Laws Should Apply to Private Firms Contracted to Perform Public Services*, 3 DET. C.L. REV. 805 (1986).

44. 31 U.S.C. §§ 9101-10 (1988 & Supp. V 1993).

45. 1 NATIONAL ACADEMY OF PUB. ADMIN., REPORT ON GOVERNMENT CORPORATIONS 24-25 (1981) [hereinafter NAPA].

46. Lilienthal & Marquis, *supra* note 42, at 564.

47. *Id.* at 562.

48. For a chart summarizing the FGC's own views of which rules apply to them, see GAO PROFILES, *supra* note 15, at 236-51. A comparison of the FGC's views summarized in this chart with the statutes themselves reveals some puzzling anomalies. For example, the Federal Property and Administrative Services Act, 40 U.S.C. §§ 471-544 (1988 & Supp. V 1993), applies to federal agencies, *see id.* § 472(a), subject to the exceptions in *id.* § 474. Nevertheless, the GAO survey demonstrates that of the 45 federal corporations responding, 30 do not consider themselves subject to the act, and an additional 5 adopted the act's requirements administratively, thus finessing the issue of whether it applied directly.

49. The GAO identifies 16 FGCs as not classified by Congress. *See* GAO PROFILES, *supra* note 15, at 15.

50. *See, e.g.*, 31 U.S.C. § 9101(3)(A) (1988) (identifying Commodity Credit Corp. as a wholly owned government corporation); *see also* 15 U.S.C. § 714e (1988) (stock subscription by federal government); *id.* § 714g (composition of board of directors); JOHN MCDIARMID, GOVERNMENT CORPORATIONS AND FEDERAL FUNDS 39 (1938).

corporations identify the body as an "agency,"[51] and most wholly owned FGCs are subject to large portions of the Administrative Procedure Act.[52]

In *mixed-ownership federal corporations*,[53] such as the RTC and REFCORP,[54] the United States may own some or none of the equity. A mixed-ownership FGC's charter often guarantees that the President will appoint at least a minority of the directors even if the federal government does not own shares. The market ordinarily assumes that securities and other debt instruments issued by mixed-ownership FGCs carry an implicit guarantee from the Treasury, and prices them accordingly.

In *private federal corporations*, such as COMSAT, the federal government holds no stock but may have a statutory right to select members of the board of directors.[55] A private federal corporation is, formally, little different from a corporation chartered by a state although it may have publicly appointed directors and tax advantages, and its debts may carry an implicit guarantee from the federal government.

Approximately one-fifth of the FGCs in existence[56] benefit from specialized lending powers coupled with an explicit or implicit federal guarantee which allows them to provide subsidized credit to, or for the use of, a target group. These FGCs, collectively known as Govern-

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51. *E.g.*, the Rural Telephone Bank, 7 U.S.C. §§ 941-50b (1988); the Export-Import Bank of the United States, 12 U.S.C. § 635(a)(1) (1988 & Supp. V 1993) ("There is created a corporation with the name Export-Import Bank of the United States, which shall be an agency of the United States of America."); the Inter-American Foundation, 22 U.S.C. § 290f(a) (1988) ("There is created as an agency of the United States of America a body corporate to be known as Inter-American Foundation.").

Some FGCs are not defined as an "agency" but have a board of directors made up entirely of government officials (often serving ex officio). For example, the Federal Financing Bank is defined as "a body corporate" and as "an instrumentality of the United States Government." 12 U.S.C. § 2283 (1988). Its five directors consist of the Secretary of the Treasury and four presidential appointees "from among the officers or employees of the Bank or of any Federal agency." *Id.* § 2284(a); *see also id.* § 24 (1988 & Supp. V 1993) (corporate powers of federally chartered financial institutions); *id.* § 2281ff (1988) (Federal Financing Bank declaration of purpose). Other wholly owned FGCs issue no stock and are run by officials appointed by the President or a Cabinet member. *See, e.g.*, 16 U.S.C. § 831a (1988 & Supp. V 1993) (providing that three directors of the TVA shall be appointed by the President with the advice and consent of the Senate).

52. *See* 5 U.S.C. § 551 (1988) (defining *agency* for APA as "each authority of the Government of United States"); *id.* §§ 103(1), 105 ("Executive agency" includes a corporation "owned or controlled by the Government of the United States"); *id.* § 552(f) (applying public records provision to "government controlled corporations," *id.* § 103(2), as well as "government corporations," *id.* § 103(1)).

53. 31 U.S.C. § 9101(2) (1988 & Supp. V 1993) (listing "mixed-ownership" FGCs).

54. *Id.* § 9101(2)(L)-(M) (identifying RTC and REFCORP as "mixed-ownership" FGCs).

55. Although all shares in COMSAT are now privately held, the President retains the right to appoint 3 of the 15 directors. *See* 47 U.S.C. § 733 (1988).

56. These are (1) the Central Bank for Cooperatives, (2) Farm Credit System Banks (comprised of the Farm Credit Banks and the Banks for Cooperatives), (3) the Federal Home Loan Banks (FHLBanks), (4) Fannie Mae, (5) Freddie Mac, (6) Sallie Mae, (7) Connie Lee, (8) Farmer Mac, (9) FICO, (10) FAC, and (11) REFCORP. *See* GAO Credit Study, *supra* note 25, at 39.

ment Sponsored Enterprises (GSEs),[57] are limited by Congress to lending to a particular constituency (farmers, students, homeowners), or for a particular purpose (such as recapitalizing insolvent savings and loans). Because some of these constituencies are very large, the GSEs designed to serve them play a dominant role in certain primary and secondary credit markets. Together, the eleven GSEs have about $1 trillion in obligations outstanding, with two-thirds of it concentrated in mortgages and mortgage-backed securities.[58] In 1989 alone, the GSEs collectively raised about $114.5 billion in the credit markets—about 12% of all funds raised in the credit markets that year.[59] In the same year, the GSEs collectively disbursed about $531 billion—about 40% of the amount disbursed by all on-budget federal agencies.[60] Five GSEs are dedicated to some aspect of home lending: the Federal Home Loan Banks (FHLBanks),[61] Fannie Mae,[62] the Federal Home Loan Mortgage Corporation (Freddie Mac),[63] the Financial Assistance Corporation (FICO),[64] and the Resolution Funding

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57. The term *government sponsored enterprise* is itself malleable. For example, in a 1990 report the GAO identified the 11 GSEs listed in note 56, *supra*. By contrast, in an excellent publication, the Congressional Budget Office chose a narrow definition: "a GSE is a privately owned, federally chartered financial institution that has nationwide operations and specialized lending powers and that benefits from an implicit federal guarantee that enhances its ability to borrow" and found that only five entities (the Farm Credit System, Fannie Mae, Freddie Mac, the Federal Home Loan Banks, and Sallie Mae) met this definition. CONGRESSIONAL BUDGET OFFICE, CONTROLLING THE RISKS OF GOVERNMENT-SPONSORED ENTERPRISES 2 (1991) [hereinafter CBO STUDY].

The definition used in this article, that a GSE is an FGC that has specialized lending powers coupled with an implicit (or, in some cases, explicit) federal guarantee, is most consistent with the definition used in THOMAS H. STANTON, ASSOCIATION OF RESERVE CITY BANKERS, GOVERNMENT SPONSORED ENTERPRISES: THEIR BENEFITS AND COSTS AS INSTRUMENTS OF FEDERAL POLICY 14-17 (1988). It is slightly broader than that used in 2 U.S.C. § 622(8) (1988 & Supp. V 1993), which defines GSE for purposes of budget process as a corporate entity created by federal law, with private stockholders, at least a majority of private directors, employees whose salaries it pays and who are not federal employees, and which is a financial institution with power to make or guarantee loans for limited purposes, raise funds by borrowing without full faith and credit, but which exercises no sovereign powers.

58. U.S. DEPARTMENT OF THE TREASURY, U.S. SECURITIES & EXCHANGE COMMISSION, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, JOINT REPORT ON THE GOVERNMENT SECURITIES MARKET 1-6 (1992) [hereinafter 1992 JOINT REPORT] (stating six GSEs had $1 trillion in obligations outstanding as of December, 1990, of which $616 million was in mortgage-backed securities); STANTON, *supra* note 26, at 34, Figure 2-1 (1991 estimate). Most of these obligations are held by banks, savings and loans or credit unions. CBO STUDY, *supra* note 57, at 7.

59. *See* TREASURY GSE STUDY, *supra* note 26, at 4, tbl. 3.

60. U.S. GENERAL ACCOUNTING OFFICE STAFF STUDY, BUDGET ISSUES: PROFILES OF GOVERNMENT SPONSORED ENTERPRISES 8 (1991) [hereinafter GAO STAFF STUDY].

61. 12 U.S.C. §§ 1421-49 (1988 & Supp. V 1993).

62. The Federal National Mortgage Association, 12 U.S.C. §§ 1716-23h (1988 & Supp. V 1993).

63. 12 U.S.C. §§ 1451-59 (1988 & Supp. V 1993). Freddie Mac now advertises itself as "Steady Freddie$_{SM}$—The Idea Behind One In Eight American Homes." *See, e.g.*, Advertisement, LEGAL TIMES, Feb. 24, 1992, at 36.

64. *See infra* note 367. For a concise description of FICO's powers and duties, see Lescher & Mace, *supra* note 24, at 510-20.

Corporation (REFCORP).[65] Four GSEs are agricultural lenders: the Farm Credit Banks,[66] the Central and Regional Banks for Cooperatives,[67] the Farm Credit System Financial Assistance Corporation (FAC),[68] and the Federal Agricultural Mortgage Corporation (Farmer Mac).[69] Two GSEs are primarily involved in higher education lending: the Student Loan Marketing Association (Sallie Mae),[70] and the College Construction Loan Insurance Corporation (Connie Lee).[71] Congress ordinarily identifies GSEs as mixed-ownership FGCs, but the degree of private ownership varies from 0 to 100%.

C. *Federal Government Corporations as a Policy Choice*

Since 1945 Congress has usually created FGCs for one of four reasons: efficiency, political insulation, subsidy, and subterfuge.[72]

1. *Efficiency*

The classic reason given for creating an FGC instead of an agency, one echoed in the Vice President's proposals, is that an FGC will be more efficient at achieving a specific national goal, especially if the program envisioned involves market transactions. The national goal is ordinarily stated in the FGC's charter. Thus, the Farm Credit System, for example, exists to improve "the income and well-being of American farmers and ranchers by furnishing sound, adequate and constructive credit and closely related services."[73] One of Sallie Mae's

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65. *See infra* text following note 369.

66. 12 U.S.C. §§ 2001-2279aa-14 (1988 & Supp. V 1993).

67. *Id.* §§ 2121-34, 2151-60.

68. *See infra* note 368.

69. 12 U.S.C. § 2279aa-1 (1988 & Supp. V. 1993). Unlike other GSEs Farmer Mac is not authorized to purchase mortgages or otherwise make direct loans. STANTON, *supra* note 57, at 3.

70. 20 U.S.C. § 1087-2 (1988 & Supp. V 1993).

71. Connie Lee deserves an article of its own. Created in 1986, Connie Lee is a mixed-ownership, for-profit joint venture of the Department of Education and Sallie Mae, which owns 75% of Connie Lee's stock. CBO STUDY, *supra* note 57, at 15, 246. Connie Lee cannot borrow from the Treasury, and the CBO has concluded that it is not perceived to have an implicit guarantee of its obligations. *Id.* at 2, 15-16. It has not been uncontroversial. *See, e.g.*, Aaron L. Task, *Connie Lee Defends Expansion, Feels Abandoned by Industry*, THE BOND BUYER, Nov. 30, 1993, at 1 (describing political fight with bond insurance agency).

As this article went to press, House Republicans introduced legislation proposing to fully privatize Connie Lee. The proposals also would remove existing restraints on its ability to diversify its business. The government would be required to sell its common stock, currently 14% of the outstanding shares, within one year of the proposal's enactment. *See* House Economic and Educational Opportunities Committee Summary of Careers Act, Daily Labor Report, May 12, 1995, *available in* LEXIS, News Library, Curnws File.

72. There have been other motives for the creation of FGCs. The government created large numbers of FGCs to cope with national emergencies such as the Depression and both World Wars. Another motive for an FGC may be to regulate a so-called natural monopoly. The government may decide to become the *rentier*, or to produce at other than the profit-maximum, rather than regulating a private monopolist. *See* Lilienthal & Marquis, *supra* note 42, at 553.

73. 12 U.S.C. § 2001(a) (1988 & Supp. V 1993).

public purposes is to assure nationwide liquidity and insurance for student loans.[74] In the abstract, FGCs seem to promise an alternative that everyone, from fiscal conservatives to democratic socialists, might find attractive.[75] FGCs conjure up an image of business efficiency as opposed to the traditional bureaucratic cabinet department. Proponents of small government may welcome the introduction of an element of private control into most realms of public administration as a means of preparing for the privatization of federal functions. Democratic socialists may view wholly or even partly owned government corporations as a means of capturing the rents and profits from public activities or natural monopolies for the benefit of the public fisc.

2. *Political Insulation*

Like independent agencies, FGCs allow Congress to insulate a program from the cabinet department that would normally have jurisdiction over it. Congress may feel that a small single-mission agency will be more zealous in furthering a given goal than a department in a multimission agency.[76] Because FGCs may have more independence from Congress, the executive, and the public than comparable public or private institutions, an FGC may be the vehicle of choice for coalitions seeking to insure a political victory against the vicissitudes of electoral politics.[77]

3. *Subsidy*

An FGC may be designed to create a captive agency for a constituency.[78] How better to capture an agency than to own it? The eight privately owned GSEs are a particularly effective means of delivering subsidies through the credit markets.[79] They borrow at lower

74. *See* 20 U.S.C. § 1087-2(a) (1988 & Supp. V 1993).

75. It also seems to appeal to neo-liberals. *See* David Osborne & Ted Gaebler, Reinventing Government (1992); National Performance Review, *supra* note 2.

76. *See* General Accounting Office, Government Sponsored Enterprises: The Government's Exposure to Risks 127 (1990) [hereinafter GAO GSE Study] (letter from two executives of Farm Credit System, noting that "Congress wanted a single-purpose entity devoted to making credit available to farmers" *because* this is perceived as a risky activity); *see also* Letter of James C. Cruse, Vice President for Policy Analysis, Export-Import Bank of the United States, to Erasmus H. Kloman, National Institute for Policy Administration (Aug. 7, 1981), *reprinted in* NAPA, *supra* note 45, at app. 3 at 1.

77. *Cf.* Edward Mortimer, *NGOs Rule OK*, Fin. Times, Sept. 21, 1994, at 20 (criticizing use of similar organizations, called "quangos" [QUAsi-Non-Governmental Organizations], in the United Kingdom).

78. *See* Richard A. Posner, *Theories of Economic Regulation*, 5 Bell J. Econ. 335 (1974); NAPA, *supra* note 45, at 31.

79. The three publicly owned GSEs—FICO, REFCORP, and FAC—are really little more than accounting tricks designed to hide federal spending and debt. *See infra* text accompanying notes 364-65.

rates than private corporations, even though little GSE debt carries a formal federal guarantee.[80] GSEs that are not backed by the full faith and credit of the United States are nonetheless widely believed to have an implicit guarantee, if only because some of them are too big to be allowed to fail.

4. *Subterfuge*

FGCs classified as either mixed-ownership or private tend to be given "off budget" status.[81] Once excluded from the national accounts, their borrowing is not counted as part of the official measure of the federal deficit. When Congress operates under spending caps or deficit reduction targets, pursuant to the Gramm-Rudman-Hollings budget reduction process for example, off-budget items are usually excluded from the official total "spent" by the government.[82] As a result, a few GSEs were created as little more than accounting devices designed to allow the federal government to borrow funds without appearing to increase the deficit.[83]

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80. FAC's debt is backed by the full faith and credit of the United States. FAC had more than $1 billion in obligations outstanding in 1994. UNITED STATES GOVERNMENT, FY 1996 BUDGET, App. 973 [hereinafter 1996 BUDGET APPENDIX]. The United States has also guaranteed the payment of the interest on certain REFCORP obligations. *See* 12 U.S.C. § 1441b (1988 & Supp. V 1993).

81. Off budget spending and debt are not part of the official federal total and do not count towards the federal spending and debt limits which, if exceeded, trigger the deficit-reduction process. STANLEY E. COLLENDER, THE GUIDE TO THE FEDERAL BUDGET: FISCAL 1996, at 12-13 (15th ed. 1995). Off budget FGCs include FICO, REFCORP, the Federal Financing Bank, the Rural Telephone Bank, USRA, and the LSC. Debts incurred by these and other federal corporations usually are not backed by the full faith and credit of the United States, providing a rationale for their exclusion from the official national debt. On the other hand, the economic activities of at least government-controlled FGCs are governmental in the sense that an economist would ordinarily use the term. The decision to call debt or expenditure off budget "is almost always political and can be changed depending on the year and the situation." *Id.* at 13.

82. *See, e.g.*, Balanced Budget and Emergency Deficit Control Reaffirmation Act of 1987, Pub. L. No. 100-119, tit. I, 101 Stat. 754, *amended by* Budget Enforcement Act of 1990, Pub. L. No. 101-508, tit. XIII, 104 Stat. 1388-1573 (current version at 2 U.S.C. §§ 901-09 (1988 & Supp. V 1993)). The Gramm-Rudman-Hollings targets are no longer in effect. *See* Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, 107 Stat. 312; Budget Enforcement Act of 1990, 2 U.S.C. §§ 901-09 (1988 & Supp. V 1993); *see generally* COLLENDER, *supra* note 81, at 19-50.

83. The Federal Financing Bank is a good example of the successful use of this technique. Agencies borrowed money from the bank, then repaid their loans at book value rather than market value. Because the Bank had borrowed at market value, this action left it holding a deficit of $2 billion, which it may be unable to pay. *See* GENERAL ACCOUNTING OFFICE, FINANCIAL AUDIT: FEDERAL FINANCING BANK'S 1993 AND 1992 FINANCIAL STATEMENTS 2-3 (1994). The deficit may be carried on the Treasury's books as an account receivable, *id.* at 3, but because the Bank is off budget, *see supra* note 81, this sum is not considered part of the national debt—instead the "asset" *reduces* the national debt.

II. The Accountability Gap

Whether an FGC is characterized *public* or *private* affects its legal relationship with the rest of the world: the President, Congress, the public, and even its own directors. Its status as a public or private body shapes the rights and remedies of any person who has a legal or commercial relationship with the corporation, whether she is employed by it, transacts with it, competes with it, makes a contract with it, is injured by it, or commits a fraud upon it. Either way, an FGC's liberty to abuse its powers faces fewer practical or even theoretical constraints than comparable institutions. Because FGCs are federal, they are not subject to regulation by the states. Because they are governmental, and often have special powers or access to cheaper capital, they are largely immune from market forces. Because they are corporations, they are exempt from most constraints ordinarily applied to federal agencies. Self-financing FGCs can even evade Congress's power of the purse. A self-funding, self-perpetuating, profit-making corporation enjoys a degree of potential, and perpetual, independence undreamed of in most agencies.[84]

Different accountability mechanisms appear appropriate depending on whether an FGC is treated as public, as private, or as a hybrid. Ordinary state-chartered corporations exist to further privately selected goals, often the quest for private profit. Their liberty to abuse their powers is curbed by market forces and by public and private laws enacted by both the state and federal governments. Ordinary federal agencies are established to further publicly selected goals, defined, in at least a general fashion, by Congress and the President. The federal agencies' liberty to abuse their powers is curbed by political forces, federal statutes, and the Constitution. In practice, neither public nor private accountability mechanisms are necessarily effective when applied to many FGCs.[85] FGCs in which the President appoints only a minority of the directors or that are financially self-sustaining are structured in a way that attenuates their accountability to elected officials.

Currently, there are few litmus tests to distinguish a public FGC from a private one in order to determine which accountability system

84. An illustration of the independence available to a self-financing corporation can be found in Lt. Col. Oliver North's plan to create a "stand-alone" entity that would channel funds from foreign governments to the *contras* and elsewhere. The plan contemplated the creation of a covert, self-financing, federally owned corporation, albeit with a state charter, in order to immunize its activities from congressional interference or control. *See* H.R. Rep. No. 100-433, 100th Cong., 1st Sess. 327, 332 (1987).

85. Wholly owned FGCs that are in effect part of a cabinet department, such as the Pension Benefit Guaranty Corp. (PBGC), which is under the direction of the Department of Labor, are as accountable as any other unit in a department. *See* 31 U.S.C. § 9101(3)(I) (1988) (identifying PBGC as a wholly owned government corporation); 29 U.S.C. § 1302(a) (1988) (characterizing PBGC as "a body corporate" within the Department of Labor).

is appropriate. Nor are there any visible limits on the powers that may be granted to private FGCs. The courts have had few occasions to consider whether private or public FGCs undermine the separation of powers or whether the Appointments Clause of the Constitution applies to directors of an FGC. Similarly, because no laws set out the duties of FGC directors appointed by the President, whether they have the same duties as FGC directors elected by shareholders is unclear. In practice, because both market discipline and federal regulatory activity are limited, many FGCs remain free to operate as they wish, regardless of how they are classified.

A. Limited Constitutional Constraints

McCulloch and *Osborn* remain the starting points for any modern inquiry into the constitutional status of FGCs, whether an FGC is viewed as public, private, or both. These two cases, together with federal government practices before World War I, establish three clear principles concerning FGCs. First, the federal government may charter private corporations.[86] Second, the presence of a minority of directors appointed by the President, or federal ownership of a minority of shares, does not necessarily make an otherwise private corporation an agency. Third, the federal government may give special advantages and powers, such as state and federal tax exemptions or control of the money supply, to a private federal corporation. No subsequent court decision has seriously questioned any of these general principles. The Supreme Court's recent decision in *Lebron v. National Railroad Passenger Corp.*[87] adds a fourth principle to the list: A corporation created for public purposes over which the government retains permanent control is a federal actor.[88]

Constitutional limits can apply to FGCs in either of two ways. If an FGC is considered public, then it shares a number of features with traditional agencies. A public FGC must be part of the executive branch of government. Therefore, a public FGC has to comply with rules imposed by the separation of powers that shape the executive

86. Writing almost 75 years after *McCulloch*, the Supreme Court described the creation of a federal corporation chartered to build a bridge as resting "upon principles of constitutional law, now established beyond dispute." Luxton v. North River Bridge Co., 153 U.S. 525, 529 (1894); *see also* Smith v. Kansas City Title & Trust Co., 255 U.S. 180, 208-09 (1920) (relying on *McCulloch* and *Osborn* to conclude that Congress enjoyed constitutional power to create Federal Land Banks and Joint Stock Land Banks). Any doubt as to the federal government's authority to charter public corporations was removed in Ashwander v. Tennessee Valley Auth., 297 U.S. 288, 338-39 (1936) (rejecting challenge to congressional chartering of TVA).

87. Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961 (1995).

88. In *Lebron* the Court held: "We hold that where, as here, the Government creates a corporation by special law, for the furtherance of governmental objectives, and retains for itself permanent authority to appoint a majority of the directors of that corporation, the corporation is part of the Government for purposes of the First Amendment." *Id.* at 974-75.

branch's relationship with the legislative branch. Similar rules also may affect a public FGC's relationship with private stockholders. Thus, although a public FGC presumably must observe due process,[89] it is unlikely to face a shareholder derivative suit.

On the other hand, if an FGC is considered private, then the Constitution does not apply to most of its activities, unless Congress has exceeded its powers in creating the FGC. Otherwise, the Constitution applies as it would to any other private transaction.[90] Thus, for example, although the federal government must observe procedural and substantive due process,[91] the conduct of private persons is not subject to such restraint, "no matter how unfair that conduct may be."[92]

1. State, State Actor, or Private Actor?

A congressional declaration that a body is an "agency" or a "private" body may be entitled to great weight, but it cannot be the final word on the subject. Even if Congress can make a heretofore private activity public, it certainly cannot label a public agency private, thus taking it and its employees outside due process and other constitutional restraints.[93] In addition, a congressional declaration that a body is of "mixed-ownership" indicates that even Congress is uncertain as to its character and offers little guidance as to the entity's constitutional status.

The Supreme Court has addressed the specific legal status of government corporations several times, starting with *McCulloch* and *Osborn*. Five years after *Osborn*, the Supreme Court confronted the following argument: A suit against a bank owned solely by a state government was, in fact, a suit against the state government itself and, therefore, forbidden by the Eleventh Amendment. Holding that the Eleventh Amendment did not apply, the Court ruled that the president and directors of the corporation "alone constitute[d] the body

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89. *But see* Roberts v. Cameron-Brown Co., 556 F.2d 356, 358-60 (5th Cir. 1977) (holding that Fannie Mae is not required to observe Fifth Amendment due process). The validity of the *Roberts* decision, which was dubious on general principles, is very doubtful in light of the Supreme Court's decision in *Lebron*. *See supra* notes 87-88 and accompanying text.

90. Almost all of the Constitution concerns governmental powers; only the 13th Amendment directly regulates private behavior.

91. *Cf.* Mathews v. Eldridge, 424 U.S. 319, 332 (1976) (regarding due process requirements for termination of social security benefits).

92. NCAA v. Tarkanian, 488 U.S. 179, 191 (1988).

93. *See* Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961, 971-72 (1995) (rejecting Amtrak's argument that the congressional charter's disclaimer of federal status determined its constitutional status and holding that Amtrak is a federal actor for the purpose of individual rights guaranteed against the government by the Constitution).

corporate, the metaphysical person liable to suit."[94] The presence of a (state) government among the incorporators or shareholders of a bank did not give the bank corporation immunity from suit and did not pierce the veil and transform the suit into one against the government.[95]

Some guidance as to when an FGC is public can be gained from the state/federal action doctrine.[96] Under the state action doctrine, the actions of a putatively private party can be ascribed to the state when there is "a sufficiently close nexus between the [government] and the challenged action of the regulated entity so that the action of the latter may be fairly treated as that of the [government] itself."[97] The current test focuses on three factors: the extent to which the actor

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94. Bank of Ky. v. Wister, 27 U.S. (2 Pet.) 318, 323 (1829). The view that a corporation remained a private entity even when harnessed to a public end, put strongly by Chief Justice Marshall in McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 400-37 (1819), and again in Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738, 866-67 (1824), dovetailed well with the fiction-concession theory of corporate existence that continued to dominate 19th century legal thinking. Under the fiction-concession theory, the state alone can create business corporations and endow them with the capacity to act as legal entities. As a result, the state can condition its grant of the corporate "privilege" in whatever manner best serves the interests of all. *See* Sutton's Hosp. Case, 10 Co. Rep. 23a (1613); *see also* Louis K. Liggett Co. v. Lee, 288 U.S. 517, 544-45 (1933) (Brandeis, J., dissenting in part):

> Whether the corporate privilege shall be granted or withheld is always a matter of state policy. If granted, the privilege is conferred in order to achieve an end which the State deems desirable. . . . Similarly, if the privilege is denied, it is denied because incidents of like corporate enterprise are deemed inimical to the public welfare . . . .

For a statement of the contrary view that corporations are merely private arrangements among individuals with whose structure the state has little business interfering, see Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416 (1989); Robert Hessen, *A New Concept of Corporations: A Contractual and Private Property Model*, 30 HASTINGS L.J. 1327 (1979). The resulting entity is an independent legal person. Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 636 (1819).

95. Bank of the United States v. Planters' Bank of Ga., 22 U.S. (9 Wheat.) 904, 906 (1824) (Marshall, C.J.).

96. The federal action doctrine is the state action doctrine applied at the federal level. Both due process and equal protection restraints are the same. *See* Weinberger v. Wiesenfeld, 420 U.S. 636, 638 n.2 (1975) (noting that federal action under the Fifth Amendment is tested under the same equal protection standard as state action under the Fourteenth Amendment); Bolling v. Sharpe, 347 U.S. 497, 499 (1954) (holding that the Fifth Amendment equal protection requirements apply to the federal government); Warren v. Government Nat'l Mortgage Ass'n, 611 F.2d 1229, 1232 (8th Cir. 1980) (holding Ginnie Mae foreclosure not government action under the Fifth Amendment), *cert. denied*, 449 U.S. 847 (1980); Geneva Towers Tenants Org. v. Federated Mortgage Invs., 504 F.2d 483, 487 (9th Cir. 1974); *see also* LAWRENCE TRIBE, AMERICAN CONSTITUTIONAL LAW 1688 & n.2 (2d ed. 1988) (equating state and federal action).

97. Jackson v. Metropolitan Edison Co., 419 U.S. 345, 351 (1974) (Rehnquist, J.); *see also* Lugar v. Edmondson Oil Co., 457 U.S. 922, 937 (1982) (describing a two-part "fair attribution" analysis for the requisite nexus). More recently, the Court has described this inquiry in the following terms:

> In the typical case . . . the question is whether the State was sufficiently involved to treat [the] decisive conduct as state action. This may occur if the State creates the legal framework governing the conduct; if it delegates its authority to the private actor; or sometimes if it knowingly accepts the benefits derived from unconstitutional behavior. Thus, in the usual case we ask whether the State provided a mantle of authority that enhanced the power of the harm-causing individual actor.

NCAA v. Tarkanian, 488 U.S. 179, 192 (1988) (citations omitted).

relies on government assistance and benefits; whether the actor is performing a traditional government function; and, whether the injury caused is aggravated in a unique way by the incidents of governmental authority.[98]

FGCs present a threshold problem that is usually absent from state action cases. The issue is not simply whether the FGC's conduct can be traced to the government, but more fundamentally whether the FGC *is* part of the government.[99] An FGC owes its existence to an act of Congress. In some cases it owes its funding to Congress as well. In other cases, some or all of its directors are appointed by the President. An FGC thus may fit the profile of "state"—not just "state actor"—much better than, say, a private parking lot operated on municipal property.[100] Federal incorporation alone, however, does not make an FGC a state actor.[101]

Although the recent *Lebron* decision has clarified some questions, the Supreme Court's decisions relating to FGCs do not follow a consistent pattern except that most of the decisions have been brief and, when taken as a group, contradictory. As a result, although the federal government's power to create private corporations and to own shares or bonds in such corporations remains unquestioned,[102] the legal status of many FGCs remains unclear. For example, the Court held that the Fleet Corporation, a wholly owned FGC,[103] was legally

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98. Georgia v. McCollum, 505 U.S. 42 (1992); Edmonson v. Leesville Concrete Co., 500 U.S. 614 (1991). Previously, the Supreme Court stated that state action will be found in private activities only when they are traditionally and "exclusively" governmental, *Jackson*, 419 U.S. at 352-53 (private utility with franchise not public function). *But see* Central Hudson Gas v. Public Serv. Comm'n, 447 U.S. 557, 587 (1980) (Rehnquist, J., dissenting) ("for purposes of First Amendment analysis, a utility is far closer to a state-controlled enterprise than is an ordinary corporation"). *See generally* Henry C. Strickland, *The State Action Doctrine and the Rehnquist Court*, 18 HASTINGS CONST. L.Q. 587 (1991) (arguing that the Rehnquist court has, in practice, adopted a "restrictive" view of state action, characterizing much arguably state conduct as private conduct). If nothing else, it is clear that the Court has no intention of adopting the Berle thesis that all corporate activities should be regarded as "state action" because a corporation owes its existence to the state. Adolf A. Berle, *Constitutional Limitations on Corporate Activity—Protection of Personal Rights from Invasion Through Economic Power*, 100 U. PA. L. REV. 933 (1952).

99. *See* San Francisco Arts & Athletics, Inc. v. United States Olympic Comm., 483 U.S. 522, 542 (1987).

100. *See* Burton v. Wilmington Parking Auth., 365 U.S. 715 (1961).

101. In *San Francisco Arts & Athletics, Inc.*, the Supreme Court decided that federal incorporation and subsidy, absent any federal control, did not transform a private nonprofit federally chartered corporation into a federal actor. 483 U.S. at 542-45. The U.S. Olympic Committee's charter appears at 36 U.S.C. § 375 (1988). *See also supra* note 14 (discussing similar corporations). Because the Court held that the U.S. Olympic Committee did not exercise any functions that were traditionally exclusively governmental, and because the U.S. Olympic Committee has no publicly appointed directors, the decision leaves open the status of the FGCs discussed in this article.

102. *See supra* note 86.

103. The United States Shipping Board Emergency Fleet Corporation, incorporated by the President in the District of Columbia pursuant to executive order, built and acquired ships for use in World War I and, after the war was over, sold its ships to the Merchant Marine. *See* Act of June 15, 1917, Pub. L. No. 65-23, 40 Stat. 182; United States *ex rel.* Skinner & Eddy Corp. v.

independent from the United States in *United States v. Strang*,[104] *Sloan Shipyards*,[105] and in *United States ex rel. Skinner & Eddy Corp. v. McCarl*.[106] Yet the Court held that, despite the technicality of incorporation, the Fleet Corporation and other wholly owned FGCs were functionally identical to the United States in *United States Grain Corp. v. Phillips*,[107] *United States v. Walter*,[108] *Emergency*

McCarl, 275 U.S. 1, 5-6 (1927) (describing history of Fleet Corporation); Sloan Shipyards Corp. v. United States Shipping Bd. Emergency Fleet Corp., 258 U.S. 549, 564-65 (1922) (same).

104. United States v. Strang, 254 U.S. 491, 493 (1921) (McReynolds, J.) (holding that Fleet Corporation employee was not agent of government within the meaning of federal criminal code prohibition of conflicts of interest). A related statute, 18 U.S.C. § 209(a) (1988 & Supp. V 1993), and somewhat similar facts arose in Crandon v. United States, 494 U.S. 152, 168 (1990) (holding that a prohibition on receiving payments as a contribution, or supplement, to a salary for service in the federal government did not apply to large bonus payments made to senior employees about to enter government service).

105. *Sloan Shipyards*, 258 U.S. at 569-70 (citing Fleet Corporation's separate corporate identity as the reason that claims against it should be heard in state court or federal district court rather than the Court of Claims; and holding under the same reasoning that the shipping corporation's claims in bankruptcy were not entitled to preference as a claim of the United States).

106. 275 U.S. 1, 11 (1927). The Court held that even though the United States was the owner, either as principal or as assignee, of all the assets of Fleet Corporation, the corporation's separate personality meant that contracts to which it was a party generally were not subject to federal audit or control except for the amorphous category of contracts entered into pursuant to power delegated by the President. *Id.* The issue of audit and control arose as a petition for a writ of mandamus against the Comptroller General, who had disclaimed jurisdiction over the Fleet Corporation. Skinner & Eddy Corporation wished to set off credits it believed the corporation owed it in a lawsuit threatened by the United States regarding transactions with the corporation. The applicable statute required that potential setoffs of this type be presented to the appropriate federal official. *Id.* at 2.

107. 261 U.S. 106, 113 (1923). The Court stated that the Grain Corporation's corporate structure, "although in form a private corporation" was "an agency for public service" and hence so "clothed with such a public interest" that a Navy officer who transported gold for it should not receive the extra pay permitted and specified for commanding officers taking charge of private (as opposed to government) valuables. *Id.* at 111, 113. The fact that the gold was payment for emergency food aid, and that the Navy officer in question would have been entitled to $52,000 if he prevailed, may have influenced the result.

The corporate charter of the U.S. Grain Corporation was for relevant purposes indistinguishable from that of the Fleet Corporation, *see supra* note 103. The U.S. Grain Corporation was formed pursuant to an Executive Order dated August 14, 1917. *United States Grain Corp.*, 261 U.S. at 110. Even the shares necessary to qualify the directors were held by the United States, endorsed by the federal government. *Id.* A second Executive Order, dated June 21, 1918, designated it an agency of the United States. *Id.*

108. 263 U.S. 15, 17-18 (1923) (Holmes, J.). In flagrant contradiction to *Strang*, the Court held that because fraud against the shipping corporation would have diminished the value of the United States's investment and "impaired the efficiency of its very important instrument[,]" *id.* at 18, conspiracy to commit fraud against the corporation was within a statute punishing conspiracy "to defraud the United States in any manner or for any purpose." *Id.* at 17; *cf.* Westfall v. United States, 274 U.S. 256, 259 (1927) (Holmes, J.) (holding that Congress may make fraud against state banks that are members of Federal Reserve system a federal crime, and also that "Congress may employ state corporations with their consent as instrumentalities of the United States").

The Supreme Court later held that a criminal statute originally passed in 1884 that made it a federal crime to defraud while impersonating officers or employees of the United States did not extend to fraud committed while impersonating a TVA employee because no government corporations existed in 1884. Pierce v. United States, 314 U.S. 306, 310-11 (1941). *Pierce* distinguished *Walter*, 263 U.S. 15, on the unconvincing grounds that the statute in the *Walter* case concerned frauds that interfered with the successful operation of the government, whereas the antifraud statute at issue in *Pierce* did not. *Pierce*, 314 U.S. at 312-13.

Fleet Corp. v. Western Union Telegraph Co.,[109] *Inland Waterways Corp. v. Young*,[110] *Cherry Cotton Mills v. United States*,[111] and now again in *Lebron v. National Railroad Passenger Corp.*[112] Moreover, all the parties to *Ashwander v. TVA* apparently assumed the identity of interest between the United States and the wholly owned nonstock TVA.[113]

Most recently, in *Lebron*, the Supreme Court relied on the confluence of a number of factors to conclude that Amtrak, a federally chartered for-profit corporation, is "part of the government"[114] for "the purpose of individual rights guaranteed against the Government by the Constitution."[115] Amtrak is wholly owned by the United States, and the government controls its board of directors.[116] In incor-

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109. 275 U.S. 415, 421-22, 426 (1928) (holding Fleet Corporation, a department of government, eligible for discounted telegraph rates under the Post Roads Act).

110. Inland Waterways Corp. v. Young, 309 U.S. 517, 523 (1940) (four-to-three decision). *Inland Waterways Corp.* concerned the authority of banks to give security for deposits made by two wholly owned FGCs. If the deposits were private, the banks had no authority to give security. The Court's opinion found that banks could give security for all federal deposits, but the dissent argued that banks could give security only for deposits under the Secretary of the Treasury's control. *Id.* at 525-27 (Roberts, J., dissenting). Writing for a four-man majority, Justice Frankfurter's opinion echoed *Phillips*, *see supra* note 107, in displaying no patience for legal fictions as to separate legal personality when it came to the federal government's agents:

> [T]he form which Government takes—whether it appears as the Secretary of the Treasury, the Secretary of War, or the Inland Waterways Corporation—is wholly immaterial. . . . The true nature of these modern devices for carrying out governmental functions is recognized in other legal relations when realities become decisive. The funds of these corporations are, for all practical purposes, Government funds; the losses, if losses there be, are the Government's losses.

Inland Waterways Corp., 309 U.S. at 523-24 (citations omitted).

111. 327 U.S. 536, 539 (1946) (Black, J.). In *Cherry Cotton Mills*, much as in United States *ex rel.* Skinner & Eddy Corp. v. McCarl, 275 U.S. 1 (1927), the question was whether a debt to the Reconstruction Finance Corporation (RFC), another wholly owned FGC with separate legal personality, was anything other than a debt to the United States. *Cherry Cotton Mills*, 327 U.S. at 537-38. If it were a debt to the United States, then the payment could be set off against a tax refund. *Id.* at 538. Otherwise, the government would have to pay the refund and the RFC would, in the case of an insolvent or recalcitrant debtor, have had difficulty collecting its debt. The Supreme Court ruled that the claim by the RFC was "on the part of the Government" and that the government could therefore apply the tax refund to the sums owed to the RFC. *Id.* at 538-39 (explaining that just because Congress calls it a corporation "does not alter its characteristics so as to make something other than what it actually is, an agency selected by the Government to accomplish purely governmental purposes"). The Court distinguished *Skinner & Eddy* as relating to the authority of the Comptroller General, whereas *Cherry Cotton Mills* concerned the jurisdiction of the Court of Claims. *Id.* at 538. As for *Sloan Shipyards*, the Court said that "[n]or is this congressionally granted power to plead a counterclaim to be reduced because in other situations, and with relation to other statutes, we have applied the doctrine of governmental immunity or priority rather strictly." *Id.* at 539-40. The *Cherry Cotton Mills* decision agreed with a decision four years earlier describing the RFC as "a corporate agency of the government, which . . . acts as a governmental agency in performing its functions [albeit with transactions] akin to those of private enterprises[,]" for which the government had waived sovereign immunity. Reconstruction Fin. Corp. v. J.G. Menihan Corp., 312 U.S. 81, 83 (1941).

112. 115 S. Ct. 961 (1995).

113. *See* 297 U.S. 288 (1936).

114. *Lebron*, 115 S. Ct. at 974.

115. *Id.* at 972.

116. The Supreme Court summarized the convoluted selection procedures for Amtrak's board as follows:

porating Amtrak, Congress declared that it "will not be an agency . . . or establishment of the United States Government,"[117] although it subjected Amtrak to the Government Corporation Control Act, and classified it as a mixed-ownership government corporation.[118]

Justice Scalia, writing for eight members of the Court,[119] began his analysis of Amtrak's legal status by rejecting the contention that Congress's designation of Amtrak as a private body controls.[120] After canvassing the Court's own precedents, Justice Scalia found that the test for determining an FGC's status remained open.[121] Finding no controlling statute or precedent, Justice Scalia turned to what he termed the "public and judicial understanding of the nature of Government-created and -controlled corporations over the years."[122] The opinion characterized the prevailing view among post-Depression political scientists as one in which wholly owned government corporations such as Amtrak were ordinarily part of the government;[123] a view that, according to Justice Scalia, also accorded with congres-

> [Amtrak has] a board of nine members, six of whom are appointed directly by the President of the United States. The Secretary of Transportation, or his designee, sits ex officio. [45 U.S.C.] § 543(a)(1)(A) [(1988 & Supp. V 1993)]. The President appoints three more directors with the advice and consent of the Senate, § 543(a)(1)(C), selecting one from a list of individuals recommended by the Railway Labor Executives Association, § 543(a)(1)(C)(i), one "from among the Governors of States with an interest in rail transportation," § 543(a)(1)(C)(ii), and one as a "representative of business with an interest in rail transportation," § 543(a)(1)(C)(iii). These directors serve 4-year terms. § 543(a)(2)(A). The President appoints two additional directors without the involvement of the Senate, choosing them from a list of names submitted by various commuter rail authorities. § 543(a)(1)(D). These directors serve 2-year terms. § 543(a)(2)(B). The holders of Amtrak's preferred stock select two more directors, who serve 1-year terms. § 543(a)(1)(E). Since the United States presently holds all of Amtrak's preferred stock, which it received (and still receives) in exchange for its subsidization of Amtrak's perennial losses, § 544(c), the Secretary of Transportation selects these two directors. The ninth member of the board is Amtrak's president, § 543(a)(1)(B), who serves as the chairman of the board, § 543(a)(4), is selected by the other eight directors, and serves at their pleasure, § 543(d). Amtrak's four private shareholders have not been entitled to vote in selecting the board of directors since 1981.

Lebron, 115 S. Ct. at 967-68.

117. 45 U.S.C. § 541 (1988).

118. 31 U.S.C. § 9101(2)(A) (1988).

119. Justice O'Connor dissented on the grounds that Lebron had disclaimed the argument that Amtrak was a government entity and that if one accepted that Amtrak was a private entity, its action should not be imputed to the Government. *Lebron*, 115 S. Ct. at 975.

120. *Id.* at 971.

121. *See id.* at 972. Justice Scalia distinguished National Railroad Passenger Corp. v. Boston & Maine Corp., 112 S. Ct. 1394, 1398 (1992) (describing Amtrak as "not an agency or instrumentality of the United States Government") on the grounds that the remark was the weakest dictum. *Lebron*, 115 S. Ct. at 971. He also distinguished National Railroad Passenger Corp. v. Atchison, T. & S.F.R. Co., 470 U.S. 451, 470 (1985) (stating that contracts at issue were "not between the railroads and the United States but simply between the railroads and the nongovernmental corporation, Amtrak") on grounds that Amtrak's nongovernmental status was not contested by the parties and was not a necessary element of the decision because the result would have been the same even if Amtrak were considered part of the government. *Lebron*, 115 S. Ct. at 971-72.

122. *Id.* at 972.

123. *Id.*

sional practice until recently.[124] Given the Court's previous decision that Congress's *declaration* that Amtrak was private did not resolve the issue, Justice Scalia did not explain why it mattered that Congress and the public *understood* Amtrak to be public.

Once the Court disposed of the congressional declaration that Amtrak was private, Amtrak's strongest remaining argument for claiming that it was not a public body rested on one paragraph of the *Regional Rail Reorganization Act Cases*.[125] In that paragraph, which forms part of a much longer discussion of other matters, the Supreme Court held that the Consolidated Rail Corporation (Conrail),[126] a Pennsylvania for-profit corporation, was not a federal instrumentality despite the federal government's power to appoint a majority of its directors.[127] Writing for seven members of the Court, Justice Brennan explained that

> Conrail is not a federal instrumentality by reason of the federal representation on its board of directors. That representation was provided to protect the United States' important interest in assuring payment of the obligations guaranteed by the United States. Full voting control of Conrail will shift to the shareholders if federal obligations fall below 50% of Conrail's indebtedness. The responsibilities of the federal directors are not different from those of the other directors—to operate Conrail at a profit for the benefit of its shareholders. Thus, Conrail will be basically a private, not a governmental, enterprise.[128]

Justice Brennan's distinction between a corporation that the government controls "as a creditor," as in the case of Conrail, and one that it controls "as a policymaker," as in the case of Amtrak, permitted Justice Scalia to distinguish the *Regional Rail Reorganization Act Cases*. Justice Scalia noted that Amtrak's charter, unlike Conrail's,

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124. *Id.* at 973.

125. Blanchette v. Connecticut Gen. Ins. Corp. (Regional Rail Reorganization Act Cases), 419 U.S. 102 (1974).

126. *See* 45 U.S.C. §§ 741-94 (1988 & Supp. V 1993). Conrail was formed in 1976, after the failure of seven northeastern railroads, in order to provide freight services in the northeast rail corridor. Conrail suffered major operating losses totalling $1.6 billion by 1980. PRESIDENT'S COMM'N ON PRIVATIZATION, PRIVATIZATION: TOWARD MORE EFFECTIVE GOVERNMENT 170 (1988) [hereinafter PRIVATIZATION]. Conrail was incorporated as a private state-incorporated entity. 45 U.S.C. § 741(a) (1970 ed. Supp. III); *Regional Rail Reorganization Act Cases*, 419 U.S. at 111. In 1981, Congress passed the Northeast Rail Service Act of 1981, Pub. L. No. 97-35, Subtitle E, 95 Stat. 643-87 (codified as amended at 45 U.S.C. § 1102 (1988)), which called for the privatization of Conrail. *Id.* § 1133. In order to make Conrail profitable, the act exempted Conrail from state taxes and certain labor laws. *Id.* § 1106. Conrail became profitable and the federal government's 85% share was sold in 1987 for more than $1.6 billion. PRIVATIZATION, *supra*, at 162-63; *see also* 45 U.S.C. §§ 1301-47 (1988 & Supp. V 1993) (procedure for privatization of Conrail).

127. *See Lebron*, 115 S. Ct. at 974 (citing Amtrak's argument based on *Regional Rail Reorganization Act Cases*, 419 U.S. at 152).

128. *Regional Rail Reorganization Act Cases*, 419 U.S. at 153.

establishes public-interest goals for the railroad,[129] and concluded that "Amtrak is worlds apart from Conrail: the Government exerts its control not as a creditor but as a policymaker, and no provision exists that will automatically terminate control upon termination of a temporary financial interest."[130]

Although Justice Scalia reached the correct result—Amtrak is clearly part of the government under the tests advocated in this article—his reliance on Justice Brennan's distinction in the *Regional Rail Reorganization Act Cases* is unfortunate because Justice Brennan misapplied his own test.[131] A valid distinction exists between a corporation in which the federal government has taken an active role in management or control, and a corporation in which the government finds itself temporarily holding the debt or equity of a going concern as the result of a civil forfeiture[132] or the government's action as a creditor or trustee.[133] If the previous management remains in control for a short time while the government seeks to dispose of the asset, it is reasonable to conclude that the corporation does not automatically become a federal actor for the period that the government owns the company. In the *Regional Rail Reorganization Act Cases*, however, the government did far more than passively hold Conrail stock. The federal government created Conrail.[134] The incorporators were led by a government official.[135] The government named a majority of Con-

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129. *Lebron*, 115 S. Ct. at 974 (citing 45 U.S.C. § 501a). In fact, this public interest goal seems irrelevant to the issue of whether Amtrak is a public body. Many nongovernmental corporations, including most nonprofits, have such goals in their charters.

130. *Id.* at 974.

131. Reliance on the *Regional Rail Reorganization Act Cases* is also unfortunate because its assertion that Conrail's federally appointed directors have "responsibilities . . . [that] are not different from those of the other directors," *Regional Rail Reorganization Act Cases*, 419 U.S. at 153, shows a limited understanding of the role of those directors. It is not at all clear whether any federally appointed director of any FGC, including Amtrak, has duties that differ from those of the directors selected by other shareholders; before *Lebron* there was no reason to believe that the nature of the public directors' duties turned on whether or not the FGC had public purposes in its charter. *See supra* notes 86-88 and accompanying text.

132. *E.g.*, Austin v. United States, 113 S. Ct. 2801 (1993) (holding that the Excessive Fines Clause of Constitution applied to seizure of appellant's auto body shop); Robert G. Morvillo, *Forfeiture and Its Constitutional Dimensions*, N.Y.L.J., June 1, 1993, at 3 (reporting that U.S. Attorney for the Southern District of New York obtained warrants to seize 23 supermarkets in a case involving the redemption of clipped, rather than customer returned, coupons).

133. For example, the Resolution Trust Corporation (RTC), *see supra* note 54, appears before the courts in a bewildering variety of guises, including creditor, *see, e.g.*, Resolution Trust Corp. v. SPR Corp., 45 F.3d 70 (4th Cir. 1995); conservator, *see, e.g.*, Recoveredge L.P. v. Pentecost, 44 F.3d 1284 (5th Cir. 1995); receiver, *see, e.g.*, Resolution Trust Corp. v. Dunmar Corp., 43 F.3d 587 (11th Cir. 1995); and government beneficiary of the *D'Oench, Duhme* doctrine, *see, e.g.*, *id.* It thus can avail itself of whatever private law or public law remedies best suit its interests under the circumstances.

134. Conrail was incorporated as a Pennsylvania corporation by a group of incorporators acting under the direction of the United States Railway Association, itself a federally chartered wholly owned FGC. *See supra* note 126.

135. *See People and Business*, N.Y. TIMES, Dec. 21, 1974, at 35, 41 (reporting that Arthur D. Lewis, Chairman of the United States Railway Association, would chair the incorporators of Conrail).

rail's directors, who in turn selected the corporation's management.[136] In the case of Conrail, the government really ran the railroad from its inception until it was privatized in 1987.[137]

The only potentially significant difference between Conrail while under federal control and Amtrak today is that the government's control of Conrail was destined to end if and when Conrail's federal indebtedness fell to less than 50% of its total debt;[138] in fact, the government still controlled Conrail when it sold the corporation.[139] This, however, did not mean that the federal government's loss of control was inevitable; it certainly had no obvious or fixed date. Indeed, Justice Douglas's dissent in the *Regional Rail Reorganization Act Cases* noted that "all the parties concede, that Conrail, though dubbed 'a for-profit corporation' . . . shows no prospect of being an enterprise operating on a profitable basis."[140]

As Justice Scalia noted in *Lebron*:

> It surely cannot be that government, state or federal, is able to evade the most solemn obligations imposed in the Constitution by simply resorting to the corporate form. On that thesis, *Plessy v. Ferguson* can be resurrected by the simple device of having the State of Louisiana operate segregated trains through a state-owned Amtrak.[141]

Had Conrail run segregated trains while a majority of federal appointees sat on its board, the offense to the Constitution would have been no less.

Lebron was actually an easier case than the Court made it seem.[142] The Court previously held, in what is now known as the federal action doctrine,[143] that entities that display "a sufficiently close nexus" to the government to "be fairly treated as [the actions] of the government itself" must be considered part of the government. Under this holding, a wholly owned FGC such as Amtrak (and probably Conrail despite the contrary holding in the *Regional Rail Reorgani-*

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136. *See Spence Named Conrail President*, N.Y. TIMES, Sept. 27, 1975, at 41 (reporting appointment of Richard Spence as successor to Richard Jordan, the first president, who was also the president of the United States Railway Association).

137. *See supra* note 126.

138. 45 U.S.C. § 741(d) (Supp. V 1970).

139. *See supra* note 126.

140. *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 163-64 (1974) (Douglas, J., dissenting); *see also* Robert E. Bedingfield, *Rail-Trackage Plan Criticized by I.C.C.*, N.Y. TIMES, May 3, 1974, at 1 (describing regulatory obstacles to formation of Conrail); A. H. Raskin, *From Pennsy To Conrail Is a Long, Hard Trip*, N.Y. TIMES, Mar. 28, 1974, § IV, at 2 (describing how expected SEC fraud charges against Penn Central Railroad depress Conrail's prospects).

141. Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961, 973 (1995) (citation omitted).

142. The Supreme Court presumably granted certiorari to reverse the peculiar decision of the Second Circuit, Lebron v. National R.R. Passenger Corp., 12 F.3d 388 (2d Cir. 1993), *rev'd*, 115 S. Ct. 961 (1995).

143. *See supra* text accompanying notes 96-98.

zation Act Cases) is a federal actor because the government owns and controls it. Indeed, Justice Scalia stated that "reason itself" compelled the conclusion that the federal government cannot hide behind a corporate form "to evade the most solemn obligations imposed in the Constitution"[144] for the same reasons the Court previously held that a state cannot evade constitutional strictures by acting through a private trust operated and controlled by state officials.[145]

The Brennan-Scalia distinction will be difficult to extend to future cases. Other than the rule that permanent control for the foreseeable future amounts to ownership in the nature of a "policymaker,"[146] it provides no guidance for determining whether the government's ownership interest is just that of "a creditor," or whether it rises to the level of "policymaker" as in Amtrak. *Lebron* thus represents a missed opportunity to link FGC case law to the federal actor test. Relying on the federal actor test would not necessarily solve every problem,[147] but it would provide a principled distinction between, on the one hand, cases such as Conrail and Amtrak, and on the other hand, the RTC's management of an insolvent savings and loan which is soon to be sold off.

Unfortunately, not every case involving an FGC is likely to be as simple as *Lebron*. Neither the state action doctrine nor whatever principles that can be extracted from precedent provides a sufficiently clear standard for determining whether an FGC that is not wholly owned by the government is public or private.[148]

In mixed-ownership FGCs and privately owned FGCs the government appoints only a minority of the directors, causing two valid public policies to conflict. On one hand, Congress chooses the instruments that are necessary and proper to achieve valid ends. Because private enterprise is a valid means to valid ends, the fact that the government facilitates the creation of private enterprise does not render that enterprise either public or invalid. If an FGC most closely resembles a private contractor that provides a government service, it

144. *Lebron*, 115 S. Ct. at 973.

145. *Id.* (citing Pennsylvania v. Board of Directors of City Trusts of Philadelphia, 353 U.S. 230 (1975) (per curiam)).

146. "[W]here as here, the Government creates a corporation by special law, for the furtherance of governmental objectives, and retains for itself permanent authority to appoint a majority of the directors of that corporation, the corporation is part of the Government." *Lebron*, 115 S. Ct. at 974.

147. *See supra* text accompanying note 95; *see also supra* note 133 (describing varying roles of RTC).

148. Indeed, Justice Scalia distinguished Amtrak, an FGC wholly owned and controlled by the federal government, from corporations in which the government does not hold a controlling interest. *Lebron*, 115 S. Ct. at 974. In so doing Justice Scalia distinguished Bank of United States v. Planters' Bank of Georgia, 22 U.S. (9 Wheat.) 904 (1824), in which the Supreme Court held that the Eleventh Amendment did not apply to a state-chartered bank in which the State of Georgia held a noncontrolling interest.

should not be treated as part of the government.[149] The analogy to private contractors is convincing if one looks only at the primarily commercial tasks that are most often entrusted to FGCs. Indeed, any rule requiring FGCs to comply with the constitutional mandates applicable to federal agencies could easily extend to all other private corporations.[150]

On the other hand, FGCs at least partly controlled by the government are arguably the government's agents. The federal government's agents should comply with the Constitution.[151] If FGCs that are partly owned or controlled by the government are private, they may provide a vehicle for the federal government to hide behind the corporate veil and escape responsibility for its actions. If the state action doctrine means anything, it is surely that the government cannot contract out of the Constitution.[152]

2. *Mixed-Ownership FGCs*

For the same reasons that a wholly owned corporation should be treated as a federal actor, both *Lebron* and the state action doctrine suggest that any mixed-ownership FGC in which the federal government owns more than half the shares should be treated as a federal actor for constitutional purposes. In addition, because the number of shares required to control a corporation varies with the circumstances, whether the United States has effective control over a particular

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149. A contractor that receives its revenue from the government does not, on that basis alone, become a state actor. *See, e.g.*, Blum v. Yaretsky, 457 U.S. 991, 1011 (1982).

150. *See* San Francisco Arts & Athletics, Inc. v. United States Olympic Comm., 483 U.S. 522, 543 n.23 (1987).

151. *Lebron*, 115 S. Ct. at 973. Thus, the "Government is free . . . to 'privatize' some functions it would otherwise perform. But such privatization ought not automatically release those who perform Government functions from constitutional obligations." *San Francisco Arts & Athletics, Inc.*, 483 U.S. at 560 (Brennan, J., dissenting); *see also* West v. Atkins, 487 U.S. 42, 56 (1988) ("Contracting out prison medical care does not relieve the State of its constitutional duty to provide adequate medical treatment to those in its custody . . . ."). *But see Blum*, 457 U.S. at 1002-12 (rejecting Medicaid patients' claims of entitlement to notice and hearing prior to transfer to low-treatment category by private state-funded nursing home because nursing home's decisions were not state action).

152. *See Lebron*, 115 S. Ct. at 973. This is not a new concern:

> That a state may rightfully evade the prohibitions of the constitution, by acting through the instrumentality of agents in the evasion, instead of acting in its own direct name, and thus escape from all its constitutional obligations; is a doctrine to which I can never subscribe: and which, for the honour of the country, for the good faith and integrity of the states, for the cause of sound morals, and of political and civil liberty, I hope may never be established.

Briscoe v. Bank of the Commonwealth of Ky., 36 U.S. (11 Pet.) 257, 339-41 (1837) (Story, J., dissenting). In *Briscoe* the bank's charter specified that the State of Kentucky would remain the sole shareholder and that its officers would be elected by the state legislature. The majority held that the bank nonetheless remained a legally separate private person, not subject to the Coinage Clause, U.S. CONST. art. I, § 10, cl. 1, a restriction that applies only to the States. *Briscoe*, 36 U.S. (11 Pet.) at 281-83; *see also* Curran v. Arkansas, 56 U.S. (15 How.) 304, 318 (1853) (fact that state holds 100% of shares not a reason to apply Bills of Credit Clause to bank with private charter); Darrington v. Bank of Ala., 54 U.S. (13 How.) 12, 15 (1851) (same).

mixed-ownership FGC in which it owns less than 50% of the shares is a factual question, one that should be decided on the same principles that apply when the existence of control is disputed in the private law context. If shareholding is very dispersed, no group may have complete control of a mixed-ownership FGC. In such cases, coalitions may form and shift from issue to issue or year to year. It is anybody's guess whether a policy that an FGC pursues with the support of the United States, or with the support of directors appointed by the United States, has a sufficient nexus to the government that can be fairly ascribed to it.

These esoteric contingencies illustrate the difficulties that can result from the unclear status of mixed-ownership FGCs, but they are largely theoretical at present. Although the government initially took an equity stake in a large number of mixed-ownership corporations, the modern trend has been toward requiring the corporations to repurchase the government's (often nonvoting) stock. As a result, although the government retains its statutory directors, it no longer has any shares in the large majority of "mixed-ownership" government corporations. Conversely, sometimes Congress designates a corporation as "mixed-ownership" even when there is no plan to sell any stock to private investors.[153]

3. *Private FGCs with Presidentially Appointed Directors*

The federal charters of several private FGCs in which the United States holds no stock provide for the presidential appointment of a minority of directors. These "public" directors sit alongside the private directors elected by the shareholders.[154] For example, the President appoints five of Fannie Mae's eighteen directors, with the majority elected annually by the common stockholders.[155]

The appointment of a minority of directors gives the appointing authority no more formal control over a corporation than would the ownership of a minority of the stock. Indeed, the power to appoint a minority of directors may carry less influence over the corporation's affairs than the ownership of an equivalent block of stock; although minority blocks sometimes suffice to control a corporation whose other shares are widely distributed, the same is rarely true of voting in a small group like the board of a corporation. In addition, the presence

153. *See, e.g.*, Alan L. Dean, *Getting Together on Public Enterprise*, NAPA J., Mar. 25, 1987, at 4-5 (United States Railroad Association designated as a "mixed-ownership" by Regional Rail Reorganization Act when in fact it was wholly owned by the federal government).

154. The government also has statutory directors in a number of "mixed-ownership" corporations in which it owns no shares. The position of these *un*mixed ownership corporations is little different from the "private" corporations discussed in this section.

155. 12 U.S.C. § 1723(b) (1988 & Supp. V 1993).

of a minority of presidentially appointed directors on the board of an otherwise private corporation does not make it a state actor and, thus, does not necessarily undermine the corporation's fundamentally private legal character.[156]

4. *Nondelegation of Public Powers to Private Groups*

If an FGC is a private body, its establishment can be viewed as a delegation of public power to a private group, much as authorizing an administrative agency to regulate is a delegation of legislative power. Viewed this way, it seems natural to ask whether there is a nondelegation doctrine for private groups akin to the nondelegation doctrine that prevents Congress from delegating standardless rule-making power to the executive branch.[157]

A delegation of federal power to a private corporation differs from delegations to an agency in two important respects: what is being delegated and the natural competence of the delegate. The agency version of the nondelegation doctrine limits delegations of legislative power; but the power of the agency to execute the laws is unquestioned. When a private body is the delegate, whether it has any right to exercise government power—legislative or executive—is an issue.[158] When the federal government delegates power to a small group of

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156. Separation of powers cases could suggest an opposite conclusion. The argument would be that, just as a single congressional director suffices to disqualify a government body from exercising executive powers, *see, e.g.*, Buckley v. Valeo, 424 U.S. 1, 140-41 (1976) (per curiam), so too does the presence of a single agent of the executive branch among the directors prevent a corporation from being private. This argument is very appealing; the considerations of ordered and balanced liberty that animate the Supreme Court's active vigilance against congressional encroachments on the executive branch's prerogatives are at least as strong when the government as a whole may be encroaching on the liberty of the people. However, so long as *McCulloch* and *Osborn* remain valid, the analogy with separation of powers is inapplicable. Both decisions clearly accepted that the Second Bank, a corporation with 20% of its directors appointed by the President, was a private corporation.

157. *See* A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495, 529-30, 538-40 (1935); *see also* J.W. Hampton, Jr. & Co. v. United States, 276 U.S. 394, 409 (1928) (delegation of regulatory authority permissible where Congress has set forth "intelligible principle[s]" guiding application of such authority). The agency form of the nondelegation doctrine is not thought to have much force because the Supreme Court has not used it to strike down a single exercise of regulatory power since the Depression. *See* IRA P. ROBBINS, THE LEGAL DIMENSIONS OF PRIVATE INCARCERATION 9-34 (1988) (collecting cases). *But see* Industrial Union Dep't v. American Petroleum Inst., 448 U.S. 607, 673-75, 685-87 (1980) (Rehnquist, J., concurring) (intimating revival of nondelegation doctrine); David Schoenbrod, *The Delegation Doctrine: Could the Court Give It Substance?*, 83 MICH. L. REV. 1223, 1226 (1985) (suggesting doctrine not dead yet).

158. On the other hand, although an agency is fundamentally a creation of statute, one with no natural powers other than those Congress gives it, a private person—even a legal person—has independent powers. Thus, one might view the granting of a corporate charter as no more than giving a convenient legal status to a series of transactions which are, in theory, already within the private capacities of individuals. Under that view, so long as the power being granted is not something that only government can do (e.g., make laws or pardon crimes), legislative power is the only nondelegation issue. This latter view, however, may be less appropriate for a corporation with a federal charter, because its powers are presumably limited to those enumerated in the statute that gave it life.

individuals, it transfers power to a private group that is presumptively less accountable to the public than are legislators, who must face reelection, or administrators, who must report to the President.[159]

This judicial concern over the delegation of legislative power to private persons reached its high-water mark in *Carter v. Carter Coal Co.* In *Carter Coal*, the Supreme Court struck down a statute authorizing coal producers and mine workers to vote on a regional basis to set hours and wages that would bind dissenters. Justice Sutherland described the statute as "legislative delegation in its most obnoxious form; for it is not even delegation to an official or an official body, presumptively disinterested, but to private persons whose interests may be and often are adverse to the interests of others in the same business."[160] The *Carter Coal* rationale has not, however, been used to invalidate any subsequent federal delegation to a private group.[161] In a world in which private police forces and private prisons are imaginable, if not yet commonplace, if a nondelegation rule applies at all, it probably applies only to legislative powers.

The *Carter Coal* doctrine is known as a nondelegation doctrine, but this name is misleading. Unlike the real nondelegation doctrine, which relies on the separation of powers to prevent Congress from making standardless delegations to administrative agencies, the *Carter Coal* doctrine is in fact a prohibition against self-interested regulation. The *Carter Coal* doctrine seeks to prevent private individuals from judging or regulating their own causes.[162] Thus, it is not surprising that the Supreme Court unanimously found it "beyond dispute" that Congress may give a private corporation the power of eminent domain,[163] because a government-sponsored taking entitles the owner to just compensation—secured in court if necessary.

If the President neither appoints nor removes private FGC directors, there is a strong argument, deriving from separation of powers cases, that FGCs cannot be given public powers. Settled constitutional principles prescribe that the only government agencies that may exercise executive powers are those in the executive branch.[164] An agency that is responsible to Congress or the courts may not execute the laws.

159. *But see* JERRY L. MASHAW, DUE PROCESS IN THE ADMINISTRATIVE STATE (1985) (describing, and criticizing, "conveyor belt" theory of accountability); Richard Stewart, *The Reformation of American Administrative Law*, 88 HARV. L. REV. 1667 (1975) (same).

160. Carter v. Carter Coal Co., 298 U.S. 238, 311 (1936).

161. *See* Harold I. Abramson, *A Fifth Branch of Government: The Private Regulators and Their Constitutionality*, 16 HASTINGS CONST. L.Q. 165, 193 (1989) (arguing that Court abandoned doctrine after *Carter Coal*); Lawrence, *supra* note 12, at 647-49, 672 (same).

162. *See* Lawrence, *supra* note 12, at 659.

163. Luxton v. North River Bridge Co., 153 U.S. 525, 529-30 (1894). The corporation's charter required that it pay "proper compensation . . . ascertained according to the laws of the State" within which the taken property was located. *Id.* at 527 n.1.

164. *See* Peter L. Strauss, *The Place of Agencies in Government: Separation of Powers and the Fourth Branch*, 84 COLUM. L. REV. 573 (1984).

The *Carter Coal* doctrine can be seen as the private analog of this limit on congressional delegation.

In *Morrison v. Olson*,[165] the Supreme Court distinguished the independent special prosecutor, who could be removed by the Attorney General for "good cause," from "a case in which the power to remove an executive official has been completely stripped from the President, thus providing no means for the President to ensure the 'faithful execution' of the laws."[166] Unlike the *Carter Coal* doctrine, which focused on excessive delegation of legislative power to private groups,[167] the modern separation of powers cases often examine the extent to which the President's powers have been impermissibly diminished by congressional action. One way to read these cases, perhaps the most persuasive way, is to view them as concerned with the balance of power among the branches. Under this interpretation, the Supreme Court is primarily concerned with congressional actions that aggrandize its own power at the President's expense. Actions that weaken the President without transferring authority directly to Congress are less likely to be held unconstitutional. This view provides a simple way of reconciling *Commodity Futures Trading Commission v. Schor*,[168] *Mistretta v. United States*,[169] and *Morrison*,[170] with the harsh language in other separation of powers cases.[171]

On the other hand, if one takes the strong language in cases such as *Morrison* at face value, then clearly an FGC headed by private directors may not exercise any public power. Although *Morrison* did not concern a delegation of power to a private group, *Morrison* asserts that there are core presidential powers with which Congress may not "interfere impermissibly," including the power to ensure the "faithful execution" of the laws.[172] Today, this restriction seems almost insubstantial for two reasons. First, the set of core presidential powers remains indeterminate—*Morrison* itself found that the President's powers were permissibly undermined by the independence of the special prosecutor. Second, the distinction between public and private functions is very vague. If either doctrine were made clearer, one side effect might be to reduce the sphere of action for FGCs.

Assuming that the *Carter Coal* doctrine is still valid, nonetheless, it seems very unlikely that any existing FGC would be declared unconstitutional under it. Although a government corporation competes

165. 487 U.S. 654 (1988).
166. *Morrison*, 487 U.S. at 692.
167. *See supra* text accompanying notes 160-64.
168. 478 U.S. 833 (1986).
169. 488 U.S. 361 (1989) (upholding constitutionality of U.S. Sentencing Commission).
170. *See supra* notes 165-66 and accompanying text.
171. *See* A. Michael Froomkin, *The Imperial Presidency's New Vestments*, 88 Nw. U. L. Rev. 1346, 1368-69 (1994).
172. *See* Morrison v. Olson, 487 U.S. 654, 693 (1988).

with private firms, it cannot regulate its competitors; thus, the central evil identified in *Carter Coal* is lacking. Competition alone, even competition by an FGC powerful enough to set the market price, is not a constitutional violation.[173] Nor do the exclusive lending powers enjoyed by certain GSEs rise to the level of control over others struck down in *Carter Coal*, for it is the legislature that decides who may, and who may not, have those powers, not the delegates themselves. Modern FGCs do not legislate and do not ordinarily issue regulations binding anyone but themselves and their employees. Nor do most modern FGCs exercise powers traditionally reserved to the state.

B. Limited Market Discipline

FGCs are most commonly created to operate a self-sustaining bank, insurance, or other commercial activity.[174] Ordinarily, the federal government is involved in the activity either because the goods or services are deemed of national importance but are not adequately provided by the private sector or because the commercial opportunity is a by-product of some other federal activity. In either case, an FGC is usually created with the hope that it will be more efficient than a traditional government department.

Although efficiency is a core justification for the existence of FGCs, in practice, FGCs are subject to a very limited degree of market discipline from bondholders, competitors, and shareholders. The absence of market discipline suggests that FGCs have little incentive to be efficient. As a result, FGCs are probably not as efficient as proponents hoped. Of course, this does not mean that FGCs are inevitably inefficient or that they could not become efficient if confronted with competitors.

1. Efficiency Claims Made for FGCs

The efficiency claims that have been asserted to justify FGCs are sufficiently broad to cover almost any contingency. At one time or another proponents have claimed FGCs are appropriate for both commercial and noncommercial purposes, as the most efficient form of nationalization, and as preparation for eventual privatization.

a. Commercial Purpose/Market Failure

Congress often turns to an FGC when the mission, often viewed as necessary to fill a gap in the private sector, is basically commercial.

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173. *See* Tennessee Elec. Power Co. v. TVA, 306 U.S. 118, 139 (1939).
174. *See* NAPA, *supra* note 45, at 27-28.

The theory is that a corporation is more efficient than a traditional federal bureaucracy.[175] President Harry S. Truman summed up the received wisdom—still current today—when he stated, "Experience indicates that the corporate form of organization is peculiarly adapted to the administration of governmental programs which are (1) predominantly of a commercial character; (2) are at least potentially self-sustaining; and (3) involve a large number of business-type transactions with the public."[176]

The market failure justification was particularly applicable to the FGCs designed to create secondary financial markets during a period in which intermediation in particular consumer credit markets remained highly regional. When Fannie Mae was established in 1938 it was the only truly national purchaser of home mortgages.[177] Its national status not only protected it from regional fluctuations in the housing market, but over time it has also generated economies of scale.[178] More recently, the General Accounting Office has suggested that the secondary capital market for multifamily housing loans has failed to mature due to potential lenders' difficulties in obtaining information about loan performance and other costs associated with these complex loans.[179]

In general, the private sector produces goods and services more efficiently than a traditional government department,[180] although

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175. *See* Lawrence, *supra* note 12, at 655 ("While not all private groups are nonbureaucratic, it is often true that a private group to which a governmental power is being delegated is less bureaucratic than the alternative public group, and for that reason it may be advantageous to make the delegation."). *But see* ANNMARIE H. WALSH, THE PUBLIC'S BUSINESS 29-30 (1978) (quoting U.S. Chamber of Commerce view that FGCs are never worth having under any circumstances because of the "built-in inefficiency in government business operations [that] no amount of reorganization or improvement in accounting technique or in personnel selection policy can ever overcome.").

176. President Harry S. Truman, 1948 Budget Message, *quoted in* NAPA, *supra* note 45, at 10. For a contemporary restatement of Truman's conclusions, *see id.* at 7 (arguing an FGC is appropriate if the government engages in commercial relations with public, users are expected to pay for the costs of particular goods and services, and expenditures fluctuate with consumer demand and cannot be limited by lags caused by the annual appropriations process).

A special case in this category is a commercial activity that is a side effect of a fundamentally noncommercial project. *See, e.g.*, 18 U.S.C. §§ 4121-29 (1988 & Supp. V 1993) (incorporating Federal Prison Industries to sell goods produced by prisoners); United States v. Appalachian Elec. Power Co., 311 U.S. 377, 426 (1940) (selling electric power out of an irrigation project).

177. *See* PRIVATIZATION, *supra* note 126, at 33.

178. CBO STUDY, *supra* note 57, at 123.

179. *See* GENERAL ACCOUNTING OFFICE, HOUSING FINANCE: EXPANDING CAPITAL FOR AFFORDABLE MULTIFAMILY HOUSING 6 (1993).

180. "The evidence that public provision of a service reduces the efficiency of its provision seems overwhelming." DENNIS C. MUELLER, PUBLIC CHOICE II 266 (rev. ed. 1989). Mueller summarizes more than 40 studies comparing public and private provision of services ranging from airline refuse collection to weather forecasting. Only two studies showed that the public sector was as efficient as the private sector. *Id.* at 263-66. James Buchanan has argued that public organizations are less efficient because their goals are not clear. JAMES M. BUCHANAN, THE DEMAND AND SUPPLY OF PUBLIC GOODS (1969). *But see* Hal G. Rainey, *Public Agencies and Private Firms: Incentives, Goals and Individual Roles*, 39 PUB. ADMIN. REV. 440-48 (1979) (both public and private administrators feel equally clear about organization's goals).

there are exceptions to the rule.[181] Unfortunately, whether a publicly owned corporation is more or less efficient at adding value than a private firm is difficult to measure. Return on equity is perhaps the simplest crude measure, but its value is limited. Just because an FGC produces a high return does not mean that it is efficient. A fair comparison with the private sector must account for whether the FGC operates in a competitive market and whether it has comparable access to capital.[182]

On the other hand, even if FGCs have a lower return on equity than comparable private firms, they should not necessarily be written off as failures. The FGC may have been created to provide other social outputs, which are external to the FGC, or inherently hard to measure.[183] In some cases, federal ownership may be a more efficient means than regulation to achieve a social goal that interferes with profit maximization.[184] If, however, the social outputs are internal to the FGC, e.g., higher wages or better working conditions than in comparable private firms, then an ordinary private corporation might be preferable.[185]

The existing empirical evidence provides weak support, at most, for the hypothesis that government corporations are less efficient than private corporations.[186] Strong evidence suggests, however, that at least some profit-oriented FGCs, such as Fannie Mae, have a far higher return on equity than do most large private firms.[187] The in-

181. *See* JOHN D. DONAHUE, THE PRIVATIZATION DECISION 57-69 (1989) (discussing studies suggesting that purely competitive solutions may be less efficient than public provision of certain services).

182. Anthony E. Boardman & Aidan R. Vining, *Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed, and State-Owned Enterprises*, 32 J.L. & ECON. 1, 8-9 (1989). Capital risk is very low in public enterprises. BARRY BOZEMAN, ALL ORGANIZATIONS ARE PUBLIC 52 (1987) (citing Steven N.S. Cheung, *Transactions Costs, Risk Aversion, and the Choice of Contractual Arrangements*, 12 J.L. & ECON. 23 (1969)).

183. In an era in which private corporations are regularly criticized for short-term planning, it is interesting to consider Barry Bozeman's hypothesis that the more public an organization, the longer term its planning horizon. BOZEMAN, *supra* note 182, at 137.

184. *See* Catherine C. Eckel & Aidan R. Vining, *Elements of a Theory of Mixed Enterprise*, 32 SCOTTISH J. POL. ECON. 82, 85 (1985).

185. Boardman & Vining, *supra* note 182, at 9.

186. *Id.* at 1. A further complication is that many FGCs are mixed enterprises with both public and private directors. The empirical evidence suggests that mixed enterprises (defined as those in which the government holds stock) tend to be at least as inefficient as state-owned enterprises. *Id.* at 26. "[I]nvestors anticipate that partially nationalized (unregulated) companies [mixed ownership government corporations] will have significantly lower profitability than" private corporations. *Id.* at 5.

187. Fannie Mae earned approximately $1.6 billion in 1994. 1996 BUDGET APPENDIX, *supra* note 80, at 119. Its after-tax return in 1994 was a healthy 24%. *See Fannie Mae Expansion Could Boost Political Risk*, WASH. POST, Feb. 6, 1995, at F25 [hereinafter *Political Risk*]. In 1990 the average return on equity was only 7.8% for all FDIC-insured commercial banks and 12.0% for the S & P 500 companies. TREASURY GSE STUDY, *supra* note 26, at 1; *see also* U.S. GEN. ACCOUNTING OFFICE, GOVERNMENT-SPONSORED ENTERPRISES: A FRAMEWORK FOR LIMITING THE GOVERNMENT'S EXPOSURE TO CAPITALIZE RISKS 81 (1991) [hereinafter GAO FRAMEWORK] (setting out return on average equity capital of selected GSEs). By 1994, the private

creasing number of FGCs with an implicit federal guarantee, and the growth in the size of their liabilities, raise micro- and macroeconomic concerns. The greatest microeconomic concerns are self-dealing,[188] and management or shareholder enjoyment of a publicly created rent, free of charge.[189] The greatest macroeconomic concern is that the FGCs may fail, leaving the government with no real alternative but to deliver on the implicit guarantee. Delivering is likely to be expensive; refusing to do so is likely to cause severe credit shortages in the relevant markets and to cause a great decline in confidence in the other FGCs in the credit markets.[190]

b. Noncommercial Purpose

Today, most FGCs are involved in commercial, if not necessarily competitive, activities. Even if the entity's task is not commercial, structuring it as a corporation arguably allows it to avoid the inefficiencies believed characteristic of the federal bureaucracy. Thus, for example, President Franklin Delano Roosevelt, proposing the creation of the TVA, spoke of "a corporation clothed with the power of government but possessed of the flexibility and initiative of a private enterprise."[191] Nonprofit FGCs include the Smithsonian,[192] the U.S. Institute for Peace,[193] and the National Park Foundation.[194]

c. Nationalization

Retaining the corporate form simplifies the nationalization of a private corporation because only the ownership is changed. Moreover, when assets (such as a railroad) formerly operated by a private corporation pass into the hands or the effective control of the United States, they are often managed by a new or existing corporation, whether or not the transaction is labeled nationalization. The takeover of "essen-

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sector had somewhat closed the gap, as FDIC-insured commercial banks achieved a return on equity of 14.9%, Carl Horowitz, *Freeing Banks to Compete More*, INVESTOR'S BUS. DAILY, Jan. 23, 1995, at A1, while the S & P 500 companies achieved a return of 16.4%. Bernice Napach, *Conservative Glasebook Earns Top Honors*, INVESTOR'S BUS. DAILY, Nov. 7, 1994, at A1. The comparison is undoubtedly unfair to the private sector as Fannie Mae has privileged access to cheap capital.

188. *See infra* text accompanying note 220.

189. *See infra* text accompanying note 265.

190. *See* CBO STUDY, *supra* note 57, at 16-17.

191. H.R. DOC. NO. 15, 73d Cong., 1st Sess. (1933); *see also* Lilienthal & Marquis, *supra* note 42, at 559 ("It is only reasonable that the Government, in entering the field of business enterprise, should closely adapt its administrative procedures and techniques to those which private business has found to be the most successful.").

192. 20 U.S.C. §§ 41-42 (1988); *see also infra* note 401 and accompanying text (arguing that the Smithsonian is unconstitutionally constituted).

193. 22 U.S.C. § 4603 (1988 & Supp. V 1993).

194. 16 U.S.C. § 19e-n (1988).

tial" assets from corporations threatening to cease providing an uneconomical service prompted the creation of FGCs, including Conrail[195] and Amtrak[196]—perhaps the best-known example.

The federal government currently is not reaping significant profits from its relationship with the FGCs as a group, although it does collect federal taxes from most of those in which it owns no equity. Nonetheless, federal ownership of valuable assets, managed for profit, could be used either to lower taxes or to produce other benefits for the citizenry. Arguably, some degree of public ownership, particularly if combined with private management with suitable incentives, might be a more efficient means of funding some government activities than taxation.

The federal government has never started or taken over a commercial venture solely or primarily to produce revenue.[197] The profit motive alone is probably an insufficient constitutional justification for a government-owned and government-run commercial enterprise[198] because the applicable federal powers are only incidental to other Article I powers.[199] The Commerce Clause, however, might justify the creation of a corporation to provide additional competition in a market that Congress reasonably found and declared to be insufficiently competitive. Or, a profit-making high-technology corporation might be justified on national security grounds, on the theory that a domestic corporation must retain control over the development and exploitation of a sensitive technology.

In modern practice, however, the federal government has tended only to take over unprofitable activities, particularly railroads, from owners who, for bankruptcy or other reasons, did not intend to maintain them and who could not find another buyer. If the activities become profitable, they are usually sold off.[200] Because the government ends up owning only unprofitable activities that it cannot sell, this policy has been dubbed "lemon socialism."[201]

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195. *See supra* note 126 (describing statutory and economic background to federal takeover of Conrail).

196. *See supra* notes 116-18 (describing statutory regime governing Amtrak). "Although its enacting legislation specified that Amtrak is not a federal agency, the U.S. government does in fact own the railroad." PRIVATIZATION, *supra* note 126, at 168.

197. In 1955, President Eisenhower approved a policy that "the Federal government will not start or carry on any commercial activity to provide a service or product for its own use if such product or service can be procured from private enterprise through ordinary business channels." PRIVATIZATION, *supra* note 126, at 1.

198. The profit motive appears to be a large part of the motivation behind the proposed Technology Transfer and Commercialization Financing Corporation, *see supra* note 7.

199. *See supra* text accompanying note 27.

200. *See, e.g., supra* note 126 (Conrail sold as soon as it became profitable).

201. *See* Dean Brackley, *The South Bronx: Past Destruction and the Rebuilding Process*, 22 HARV. C.R.-C.L. L. REV. 1, 40 (1987) (Professor Sylvia Law's comments on the presentation).

d. Preparation for Eventual Privatization

The corporate form is a natural method of organizing enterprises that are considered candidates for eventual privatization. An enterprise that has corporate status can more easily become profit oriented, if only because employee pay can be linked to performance. In addition, it is easier to keep business-style accounts which reflect costs such as office rent, capital depreciation, pensions, and even goodwill, that would be difficult to assess in a single agency. Such accounts give potential buyers a clearer idea of the value of the enterprise than is available to assess an agency. The transfer of a traditional agency would have to be organized as a sale of physical assets and certain contracts. But a going concern consists of more than its physical assets and its rights and obligations. For example, because the government does not have mechanisms for transferring employees who have civil service status, i.e., who work for an agency, employees may seek transfers if their departments are sold. Excluding an FGC's employees from the civil service system allows transfer of the corporation's asset-specific human capital as well.[202]

In theory, "virtually any [government] function is, at least potentially, amenable to 'privatization.' "[203] Indeed, during the Reagan administration, the Office of Personnel Management proposed spinning off a large number of government entities as independent, for-profit companies with the current government employees as shareholders.[204] Congress and the agencies currently are considering several privatization proposals.[205]

2. *Negligible Bond Market Discipline*

The bond market is a potential source of discipline for FGCs that are regular borrowers because these FGCs have a long-term interest in keeping the cost of credit as low as possible. However, because

202. The Rural Telephone Bank, a wholly owned FGC that Congress originally classified as an agency, 7 U.S.C. §§ 941-50b (1988 & Supp. V 1993) (establishing Rural Telephone Bank as body corporate), is being privatized in this manner. The Rural Telephone Bank has 13 directors, 7 of whom are appointed by the President, *id.* § 945(b)(1), with the other 6 elected by holders of Class B and C stock, *id.* § 945(b)(2)-(3). The federal authority to purchase Class A stock lapsed at the end of 1991, and the Bank has an obligation to repurchase all the government's stock by 1995. *Id.* § 946(a), (c). When 51% of the government's Class A stock has been retired, 5 of the government's directors will resign, the wholly owned FGC will cease to be an agency of the United States, and it will become a mixed-ownership FGC. *Id.* § 950(a).

203. BOZEMAN, *supra* note 182, at 4. *But see* Eckel & Vining, *supra* note 184, at 84 (stating that optimal level of public ownership is unclear).

204. PRIVATIZATION, *supra* note 126, at 3. The Office of Personnel Management argued that by offering existing employees an ownership stake it could "build support within a group normally opposed to proposals to reduce the federal role." *Id.* No one took the bait.

205. *See, e.g.*, USEC Privatization Act, H.R. 1216, 104th Cong., 1st Sess. (1995) (requiring privatizations of United States Enrichment Corporation).

bond holders have little incentive to carefully monitor GSEs whose debt benefits from a federal guarantee, the bond market poorly constrains FGC activities. There is no doubt that the market's perception that GSE debt is implicitly guaranteed by the United States government, despite disclaimers to the contrary, means that GSE debt trades at low rates of interest regardless of the actual soundness of their balance sheets. FICO, for example, continued to sell its obligations at near-Treasury rates despite a negative net worth.[206]

Indeed, proponents of increased safety and soundness regulation for GSEs have argued that the existence of the implicit guarantee may have a perverse effect: as a GSE approaches insolvency, management's access to credit will remain unimpaired; in turn, this access to relatively cheap credit, arguably, provides an incentive for management to engage in excessive risk taking in increasingly desperate attempts to recoup their losses. In addition, whether an FGC is eligible to become a debtor under the Bankruptcy Code is unclear.[207]

3. *Weak Competitive Market Discipline*

Few FGCs operate in competitive markets; indeed, many were created because the market was not able or willing to take on the task entrusted to them. The Federal Prison Industries[208] literally has a captive source of labor[209] and sells primarily to the government. The Tennessee Valley Authority sells power on a competitive market but enjoys at least the same anticompetitive advantages as any utility with a monopoly access to a source of hydropower.

A few FGCs do operate in competitive markets. Amtrak competes with other forms of transport. Connie Lee competes directly with private insurers.[210] Several of the GSEs have private competitors or sell financial products that are close substitutes for securities sold by the Treasury, other GSEs, or private institutions. In addition, the public purposes and financial strategies of Fannie Mae and Freddie Mac have converged, effectively making them competitors,[211] or duopolists.

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206. STANTON, *supra* note 57, at 4.

207. *See* STANTON, *supra* note 26, at 206.

208. 18 U.S.C. §§ 4121-29 (1988 & Supp. V 1993). Federal Prison Industries is also known as UNICOR.

209. *But see* Lariscey v. United States, 949 F.2d 1137 (Fed. Cir. 1991) (holding that Federal Prison Industry's use of prisoner's invention was a taking in contravention of Fifth Amendment), *vacated*, 962 F.2d 1047 (Fed. Cir. 1992) (granting rehearing en banc). *Cf.* Lariscey v. United States, 981 F.2d 1244 (Fed. Cir. 1992) (en banc) (contrary ruling by Claims Court affirmed by equally divided court), *cert. denied*, 113 S. Ct. 2997 (1993).

210. GAO FRAMEWORK, *supra* note 187, at 17.

211. *See* CBO STUDY, *supra* note 57, at 122-28.

Private competitors of the few FGCs that operate in competitive markets sometimes accuse the FGCs of having unfair advantages.[212] FGCs are ordinarily immune from state tax;[213] and sometimes they have unique abilities to operate on national scale. And, of course, the large financial GSEs are able to borrow at lower rates than available to competing private financial institutions. It even has been suggested that Fannie Mae's entry into the mortgage-backed security market contributed to the savings and loans crisis because investors preferred its mortgage-backed securities to certificates of deposit (CD) issued by S&Ls. An S&L's CD is ultimately backed by its assets, primarily its portfolio of mortgages, making the certificate of deposit, arguably, a close substitute for a Fannie Mae mortgage-backed security. In addition, the mortgage-backed security enjoyed an implicit government guarantee at no charge, while an S&L was required to purchase its guarantee, further lowering the rate of return it was able to offer. Finally, S&Ls had much stiffer capital requirements than Fannie Mae, increasing their relative costs.[214] In defense of the GSEs, however, it should be noted that their charters usually restrict them to a narrow line of business, depriving them of the ability to diversify.

The aftermath of the recent scandal concerning price fixing in the government bond market provides a striking example of a GSE's market power.[215] Freddie Mac's contracts with its original dealers are terminable at will. When it learned that more than a third of its original dealers had provided misleading information designed to secure excessive allocations of Freddie Mac securities, Freddie Mac informed the responsible dealers that it believed their activities constituted breach of contract. Subsequently, the dealers had a choice between paying a fine equal to twenty percent of their commissions earned in 1990 and 1991, or having their contracts terminated. Many dealers chose to pay fines totalling over $1 million.[216]

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212. For a striking example, albeit on a small scale, see Joseph Radigan, *Fannie Mae Creates a Stir*, U.S. BANKER, Dec. 1993, at 54 (quoting allegations that Fannie Mae's decision to give away its "Desktop Trader" loan origination software in order to link in brokers with its systems undermined commercial vendors of similar software).

213. Fannie Mae has proved particularly adept at preserving its exemption from local taxes in the District of Columbia despite being the city's largest and most profitable company. *See Political Risk*, *supra* note 187; *see also* Lilienthal & Marquis, *supra* note 42, at 596 n.134 (collecting cases). The FHL Banks, FICO, REFCORP, Farmer Mac, and the Farm Credit Banks are also immune from federal income taxes. Thomas H. Stanton, *Federal Supervision of Safety and Soundness of Government-Sponsored Enterprises*, 5 ADMIN. L.J. 395, 402 (1991).

214. *See* George Melloan, *Was Fannie Mae a Factor in the Thrifts Crisis?*, WALL ST. J., Apr. 4, 1989, at A23; *see also* CBO STUDY, *supra* note 57, at 139 (describing crowding out of S&Ls from holding fixed rate mortgages).

215. A terse description of the affair can be found in 1992 JOINT REPORT, *supra* note 58, at 1-6.

216. *See* Steven Boehm & Mark Stabile, *A Low-Key Market Makeover*, LEGAL TIMES, Feb. 24, 1992, at 22 ("approximately" 18 dealers paid fines totalling over $1 million); Statement of Victoria Whitenton, Director, Money Markets, Federal Home Loan Mortgage Corporation,

C. *Internal Governance*

The generally unsettled nature of the law relating to FGCs is reflected in the remarkably small number of clear rules regulating their internal governance and their relations with their shareholders.

1. *Limited Shareholder Discipline*

Any privately owned or mixed-ownership for-profit FGC that issues shares faces two theoretical types of discipline from shareholders. First, shareholders, including the government if it owns shares, may vote their shares to replace the management, or they may sell their shares to a predator seeking to take over the company. Second, if the FGC contemplates returning to the market for additional capital it will want to act in a manner that tends to increase its share price.

How much control shareholders actually have over the ordinary corporations in which they hold shares has been the subject of a great deal of legal and economic analysis, particularly in the literature deriving from the property rights theory of the firm.[217] Corporate managements are greatly concerned with corporate control, or at least with the acquisition and retention of it. A normative desire that managers remain accountable to owners, i.e. shareholders, often combines with the positive assertions that this is what shareholders desire and that this is in their interest. Shareholders are presumed to be most interested in the maximization of the value of their investment, albeit with varying time-preferences for money. Protecting one's corporate control, it is argued, supplies salutary market discipline to owners and managers alike by forcing directors to maximize value of shares or face hostile takeover (and loss of employment for managers) by predators better able to put assets to remunerative use.[218]

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prepared for Subcomm. on Oversight, House Comm. on Ways and Means (Sept. 26, 1991) (copy on file with author) (describing contractual relationships). For a general description of the market in GSE securities, see 1992 JOINT REPORT, *supra* note 58, at D-1 to D-6.

217. *See generally* Armen A. Alchian & Harold Demsetz, *The Property Rights Paradigm*, 33 J. ECON. HIST. 16 (1973); Harold Demsetz, *Toward a Theory of Property Rights*, 57 AM. ECON. REV. 347 (1967). *But see* ADOLPH A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932).

218. Although the classic view of agencies accountable to the President and Congress and the property rights theory of the firm apply different premises to different problems, the legal rules they both analyze and influence address a similar problem: in both cases a diffuse group of principals (the voting public, the shareholders) seek legal means to control a bureaucratic agent (agencies, corporations). The parallel is not exact because "the people" must act through agents, the President and Congress, whereas stockholders can in theory act directly by voting their shares; the parallel may be stronger in fact, however, because stockholders too often act through institutional agents. Further, politicians may have their own legitimate personal and institutional interests and prerogatives, whereas, arguably, the board of directors of a corporation does not.

Having addressed similar problems, the two lines of analysis also have come up with a similar solution: a principal's control over an agent depends upon the power to hire and fire the agent. Writers on both administrative and corporate law agree that the essence of control over an organi-

The federal government is not an ordinary shareholder.[219] Its interests are more likely to be political than profit maximizing. Majority control by the federal government provides takeover insurance that can only be dented by privatization. Any federal corporation in which the federal government has a majority stake thus gains unusual insulation from the chief source of discipline on which the property rights theory of the firm relies.

Some FGCs are wholly or partly owned by persons whom the FGCs were designed to benefit. Vesting ownership in the targeted beneficiaries has the advantage of greatly increasing the chances that any profits generated by the FGCs' activities will go to those groups. Unfortunately, vesting ownership in the target group also can create significant conflicts of interest and moral hazard, and certainly gives the owners a special interest in retaining control. The insolvency of the Farm Credit System, the only FGC to become insolvent since World War II, has been attributed to lax loan standards due to cooperative ownership by its borrowers.[220]

The peculiar structure of the boards of privately owned FGCs also may serve to insulate them from shareholder discipline. For example, for many years Sallie Mae's twenty-one-member board of directors was divided into three groups, with seven directors appointed by the President, seven elected by educational institutions holding voting stock, and seven by financial institutions holding voting stock.[221] In this scheme, no private individual or individual institution could

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zation is the power to appoint and remove its top officials, be they cabinet officers or the board of directors.

Of course, from a political viewpoint there is more to control than the power to fire. A strong and popular cabinet official can act with relative impunity if the President does not dare fire her. Conversely "independent" officials may feel duty-bound to follow administration policy, or may be selected for their views in conformity with it; the desire for future preferment also may reduce independence. Writers on administrative and corporate law also agree that the absence of clear control can create legal and policy difficulties. Thus, the extent and legitimacy of the freedom enjoyed by independent agencies and "managerial" firms have been continuing sources of debate.

219. *See* Lilienthal & Marquis, *supra* note 42, at 570.

220. *See* UNITED STATES GOV'T, FY 1991 BUDGET 240 [hereinafter 1991 U.S. BUDGET].

221. 20 U.S.C. § 1087-2(c)(2) (1988). Amendments, however, ameliorated this situation. Although the quota system governing who can be on the board has not changed, every share now gets an equal vote on all 14 private directors. *Id.* § 1087-2(c)(1)(A), 2(f)(4) (creating a single class of voting common stock).

It did not take long for the change in voting structure to have an effect: In June 1995, Sallie Mae became the first GSE to undergo a proxy fight. A dissident slate of eight directors, including a former CEO, won seats on the board in a bitterly contested election sparked by dipping share prices, and disagreements about Sallie Mae's response to proposed privatization legislation, H.R. 1720, 40th Cong., 1st Sess. (1995). *See* Albert B. Crenshaw, *Sallie Mae Dropping Proxy Fight; Company to Seat All 8 Dissidents*, WASH. POST, June 27, 1995, at D2 (noting that Sallie was abandoning court challenge to election of dissident directors); Maggie Urry, *Sallie Mae Rebels Win Board Row*, FIN. TIMES, July 7, 1995, at 29.

As this article went to press, the Clinton administration announced that it planned to introduce its own privatization legislation, differing from H.R. 1720, that would affect both Sallie Mae and Connie Lee. Sallie Mae's management described the administration's bill as "unacceptable" because it would require Sallie Mae to disband if its shareholders voted against privatization. *See* control Sallie Mae; a takeover would have required coordinated action among, say, seven financial institutions and four universities. Sallie Mae's longstanding (but now greatly lessened) insulation from market discipline may explain why, until recently, Sallie Mae's management pursued surprisingly risk-averse policies.[222] The need to take risks in order to increase earnings is greatly reduced if a firm faces no danger of a hostile takeover.

2. *Unclear Directors' Duties*

The privately elected directors of a private or mixed-ownership FGC are presumably subject to the same duties as the directors of an ordinary corporation. Precisely what law governs these duties is, however, unclear. There is no federal corporate code, essentially no relevant federal common law outside the context of the Securities Acts, and most FGCs are exempt from registration requirements.[223] If a court were asked to find an applicable law, presumably it would have to fashion federal common law.[224]

Very little law governs the duties of presidentially appointed directors in a mixed-ownership or private federal corporation. At the turn of the century, the Supreme Court considered the status of Union Pacific, a private railroad which had a minority of directors appointed by the President. The Court held that, although the directors appointed by the President were required to make reports to the Secretary of the Interior in addition to their ordinary duties, "[t]hey had the same powers as the other directors and no more" because "Congress did not vest in the government directors any peculiar powers."[225] The Court emphasized that the presence of the directors appointed by the President did not alter either the internal governance of the corporation or its relations with others.[226]

Administration Will Introduce Bill to Privatize Sallie Mae, Connie Lee, Banking Rep. (BNA), No. 26, at 1231 (June 26, 1995), *available in* LEXIS, Banking Library, Bnabnk File.

222. *See, e.g.*, CBO STUDY, *supra* note 57, at 260 (expressing puzzlement that unregulated Sallie Mae has followed low-risk policies that would have been required by a "well-informed and motivated regulator").

223. The Bush administration proposed legislation that would have removed this exemption. *See* 1992 JOINT REPORT, *supra* note 58, at 33-34.

224. The rule that federal courts construing federal statutes touching corporate law should borrow state corporate law rules when possible, recently restated in Kamen v. Kemper Financial Services, 500 U.S. 90 (1991), would not necessarily apply because that rule rests on the fact that state law defines the powers and duties of a state-chartered corporation. *See* Burks v. Lasker, 441 U.S. 471, 478 (1979).

225. Union Pac. Ry. v. Chicago, R.I. & Pac. Ry., 163 U.S. 564, 599 (1896).

226. *Id.* at 600 ("We regard the position as wholly untenable that this provision for government directors took the corporation out of the general rule that except in cases where the charter imposes a limitation the stockholders are the proper parties to take final action in the management of the corporate affairs.").

The *Union Pacific* case could be read to suggest that so-called public directors do not have special duties to the public at large. This simply cannot be right. Requiring presidentially appointed directors would be pointless, especially in FGCs in which the government owns no shares, unless the government's directors represented the national interest in some way. What remains unclear is to what extent these public directors have special responsibilities and to what extent their duties are the same as ordinary directors whose fiduciary duties include the traditional duties of diligence and loyalty to the corporation and its shareholders. More troubling, no body of law exists to guide the directors themselves in reconciling the two sets of duties should they conflict.

The issue has been further confused by Justice Scalia's recent opinion in *Lebron*. He distinguishes between so-called nongovernmental, albeit government-controlled, corporations such as Conrail, in which the "responsibilities of the federal directors are not different from those of the other directors—to operate [the corporation] at a profit for the benefit of its shareholders,"[227] from governmental, government-controlled, corporations such as Amtrak, in which the public directors have other duties besides profit, as set forth in the corporation's charter.[228] Justice Scalia's distinction is unfortunate not only because it relies on a case that wrongly determined whether Conrail was part of the government,[229] but also because it mistakenly implies that private directors might not share in the duty to give effect to the public purpose specified in an FGC's charter.

Although the duties owed by executive and nonexecutive directors sometimes differ, the fiduciary duties to which they are subject are basically the same. A government director, whose role resembles that of a nonexecutive director in an ordinary corporation, may feel—and should feel—a duty to represent the public interest.[230] It is not obvious, however, how government directors are supposed to act on this feeling. Further, even if government directors are expected to use their votes and influence to promote the public interest, their influence may not be equal to the task when they are in the minority.[231]

227. Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961, 974 (1995) (quoting *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 152 (1974)).

228. *Id.* (citing 45 U.S.C. § 501a).

229. *See supra* notes 225-26 and accompanying text.

230. Dianne Hobbs, *Personal Liability of Directors of Federal Government Corporations*, 30 CASE W. RES. L. REV. 733, 740-41 (1980). A few authors have suggested that public directors should be required in all large private corporations. *See, e.g.*, Elliott J. Weiss, *Social Regulation of Business Activity: Reforming the Corporate Governance System to Resolve an Institutional Impasse*, 28 UCLA L. REV. 343 (1981); *see also* Roberta Romano, *Metapolitics and Corporate Law Reform*, 36 STAN. L. REV. 923 (1984) (surveying a wide variety of reform proposals).

231. Herman Schwartz, *Governmentally Appointed Directors in a Private Corporation: The Communications Satellite Act of 1962*, 79 HARV. L. REV. 350, 353-54, 358-59 (1965); *see also* Ronald J. Gilson & Reinier Kraakman, *Reinventing the Outside Director: An Agenda for*

(Suppose, for example, that the corporation is considering trade-offs between profit maximization and nonpecuniary social interests such as environmental quality or compliance with current government policy.) On the other hand, if the presidentially appointed directors primarily function as the eyes, ears, and mouthpieces of the President and the federal bureaucracy, then numbers are less important, although there may be a conflict with duties of confidentiality owed to the corporation. The conflicts are likely to be particularly acute if the director is privy to corporate secrets concerning litigious or contractual relationships with the government. Some evidence suggests that the private directors of more than one FGC, not blind to the potentially dual loyalties of the directors appointed by the President, have cut them out of key decisions.[232]

In addition to the duties resulting from their public status, the government directors of a corporation may share the personal liability that emanates from acceptance of an ordinary directorship. Directors are often insured against their personal liability for negligence. Government officials do not always enjoy similar protection; some types of liability for official wrongs may be uninsurable as against public policy.[233]

Directors appointed by the President may sometimes find themselves in anomalous positions. For example, the Secretary of Housing and Urban Development (HUD) served for about a year as an ex officio member of Freddie Mac's board of directors. HUD was also Freddie Mac's regulator. As a result, HUD issued no regulations affecting Freddie Mac, fearing that regulations would be inappropriate while the Secretary served in this dual capacity.[234]

Institutional Investors, 43 STAN. L. REV. 863 (1991) (discussing shortcomings of monitoring currently performed by (private) outside directors). Note also that the other shareholders' right to complain about the public directors' disloyalty is likely to be limited: shareholders, after all, were on notice as to the presence of the directors appointed by the President when they bought their shares. Further, if the directors appointed by the President are seen as officers of the United States, they may enjoy governmental immunity. *See* Harlow v. Fitzgerald, 457 U.S. 800 (1982); Butz v. Economu, 438 U.S. 478, 507-08 (1978) (describing qualified immunity granted to executive officials).

232. *See* Schwartz, *supra* note 231, at 354-63 (describing mistreatment of government directors by private directors, e.g., not inviting government representatives to directors meetings and committee meetings, failing to consult them on mergers, dividends, and debt); *see also* Union Pac. Ry. v. Chicago, R.I. & Pac. Ry., 163 U.S. 564, 598 (1896) (railroad delegated all authority to executive committee, thereby freezing out public directors).

233. PETER SCHUCK, SUING GOVERNMENT 85 (1983); *see also* Hobbs, *supra* note 230, at 742 (discussing liability of federal officials).

234. *See Treasury, CBO and GAO Reports on FNMA, FHLMC and the Federal Home Loan Bank System: Hearings Before the Subcomm. on Housing and Community Development of the House Comm. on Banking, Finance and Urban Affairs*, 102d Cong., 1st Sess. 72 (1991) [hereinafter *HUD Hearings*] (statement of Alfred Dellibovi, Deputy Secretary, HUD).

3. *Voting the Government's Stock*

Voting the government's shares in a corporation is either an act of appointment (when electing directors), or an act that can affect the rights, duties, and responsibilities of a person outside the legislative branch (when voting on any other type of shareholder's resolution). In the case of the latter, it is either an executive act or one that Congress can only exercise in conformity with the bicameralism and presentment requirement of the Constitution.[235]

No statute or case determines how the government's shares should be voted on shareholder's resolutions.[236] *Immigration & Naturalization Services v. Chadha* suggests that Congress could pass legislation, duly presented to the President, that would mandate that the directors appointed by the President submit a particular resolution or that the nation's shares be voted for or against a particular shareholder initiative.[237] In the absence of legislation, the President, or his delegate, is presumably the nation's proxy-holder. The alternative is to share the nation's proxies among the publicly appointed directors.

4. *Private Shareholders' Rights*

Shareholders in an FGC have few obvious rights.[238] If a corporation is private enough to avoid being subjected to constitutional prohibitions,[239] but still a creature of federal law, then the only apparent source for shareholders rights, beyond the few provisions contained in the corporation's charter, is federal common law. Federal charters ordinarily set out the voting rights that attach to a share of stock. Such provisions probably suffice to create a private right of action if the right to vote such a share is somehow impaired. Other traditional corporate claims, such as waste and acting ultra vires, either do not exist or, if they do exist, must arise from the federal common law of corporations or from federal common law regulating the

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235. U.S. CONST. art. I, § 7. *See generally* Metropolitan Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc., 501 U.S. 252 (1991) (holding that participation of members of Congress in committee with power to veto decisions regarding local airports violated separation of powers); Immigration & Naturalization Serv. v. Chadha, 462 U.S. 919, 946-51 (1983).

236. In 1834, however, the Attorney General opined that the U.S.'s dividends from the Bank of the United States were federal property and could not be withheld or set off by the Bank. *See* 2 Op. Att'y Gen. 663 (1834).

237. *Chadha*, 462 U.S. at 955 & n.19.

238. *See* Lynch v. United States, 292 U.S. 571, 579 (1934). *But see* Fahey v. O'Melveny & Myers, 200 F.2d 420 (9th Cir. 1952) (holding that Due Process Clause does not apply to relations between FHLBank and its shareholders), *cert. denied sub nom.* Mallonee, Bucklin & Fergus v. Fahey, 345 U.S. 952 (1953). For an analysis concluding that shareholders in Fannie Mae have practically no rights at all, see Comment, *FNMA and the Rights of Private Investors: Her Heart Still Belongs to Daddy*, 59 GEO. L.J. 369, 376-85 (1970).

239. *See supra* notes 86-92 and accompanying text.

(implicit) contract formed when an investor purchases a share. If the courts have the authority to make such federal common law, they have yet to do so. Thus, any discussion of shareholders' rights in FGCs is fundamentally speculative. Apparently, no shareholder action, derivative or otherwise, has succeeded against any federally chartered corporation in this century.[240] Until this year, no federal corporation has been the subject of a takeover or even a proxy fight. One reason for the lack of reported cases may be that private shareholders in a private or mixed-ownership corporation chartered by Congress face a daunting task in making a claim against the corporation or its directors unless Congress has subjected the corporation to the laws of the District of Columbia. Or, it may be that shareholders in the for-profit FGCs that issue stock lack the motive to bring a claim because they make sufficiently high returns on their investment.

D. Sovereign Immunity and the Merrill *Doctrine*

The greater an FGC's entitlement to sovereign immunity, the more it enjoys an advantage over private competitors. If an FGC is private, then it has no right to sovereign immunity unless Congress, by statute, chooses to grant that immunity. If an FGC is public, whether it has sovereign immunity is a question of statutory construction involving both the FGC's charter and the various limited statutory waivers of the United States's immunity. Courts have found two types of immunity that apply to FGCs: sovereign immunity from tort claims and protection from estoppel claims based on employee conduct. The interplay between these two areas has not only given many FGCs an advantage over private competitors, but it has given some FGCs greater immunity from suit than is available to ordinary federal agencies.

1. Sovereign Immunity

As a general rule, when a federal incorporated (or even unincorporated) entity is "launched into the commercial world"[241] the government is assumed to have "accepted the ordinary incidents of suits in such business,"[242] unless there are statutory grounds for a different

240. The odds of success are remote. *See* First Am. Fed. Sav. & Loan Ass'n v. Student Loan Mktg. Ass'n, No. 84-1014 (E.D.N.C. Apr. 16, 1985) (order granting motion to dismiss) (S&L that held shares in Sallie Mae failed to state claim when it filed shareholder suit seeking to block Sallie Mae's acquisition of state S&L as *ultra vires* under Sallie Mae charter).

241. Franchise Tax Bd. v. United States Postal Serv., 467 U.S. 512, 520 (1984).

242. Standard Oil Co. v. United States, 267 U.S. 76, 79 (1925); *see also* cases cited *supra* note 38.

conclusion. Torts are one area where courts have found grounds for an exception.

The Federal Tort Claims Act (FTCA)[243] provides a limited waiver of the sovereign immunity of the United States for certain torts of federal agency employees. The FTCA defines federal agencies as including "the executive departments, . . . independent establishments of the United States, and corporations [other than contractors] primarily acting as instrumentalities or agencies of the United States . . . ."[244] If the FTCA applies, it ordinarily provides the exclusive monetary remedy for the tort—even if the federal agency employing the tortfeasor has a sue-and-be-sued clause in its charter.[245]

Courts seeking to determine whether the FTCA applies usually examine five factors: (1) the federal government's ownership interest in the entity; (2) the federal government's control over the entity's activities; (3) the entity's structure; (4) government involvement in the entity's finances; and (5) the entity's function or mission.[246] Thus, the Seventh Circuit recently held that the FTCA did not apply to Freddie Mac because it was not one of the "corporations primarily acting as instrumentalities or agencies of the United States"[247] contemplated by that act.[248] The Seventh Circuit did not explain why Freddie Mac, which is a mixed-ownership GSE in which the govern-

243. Federal Tort Claims Act, 28 U.S.C. §§ 1346, 2671-80 (1988 & Supp. V 1993).

244. *Id.* § 2671.

245. *Id.* § 2679(a): "The authority of any federal agency to sue and be sued in its own name shall not be construed to authorize suits against such federal agency on claims which are cognizable under [28 U.S.C. § 1346(b)]." In the FTCA Congress "wished to 'place torts of "suable" agencies of the United States upon precisely the same footing as torts of "nonsuable" agencies.'" Loeffler v. Frank, 486 U.S. 549, 562 (1988) (quoting H.R. REP. NO. 1287, 79th Cong., 1st Sess. 6 (1945)).

246. *See* Mendrala v. Crown Mortgage Co., 955 F.2d 1132 (7th Cir. 1992) (collecting cases); *see also* United States v. Orleans, 425 U.S. 807 (1976) (Community Action Agency, created pursuant to Economic Opportunity Act, not federal agency for FTCA); Logue v. United States, 412 U.S. 521 (1973) (private contractor exception to FTCA); FDIC v. Citizens Bank Trust Co., 592 F.2d 364 (7th Cir.), *cert. denied*, 444 U.S. 829 (1979) (holding FDIC is federal agency within FTCA); Safeway Portland Employees' Federal Credit Union v. FDIC, 506 F.2d 1213, 1215 (9th Cir. 1974) (same); Freeling v. FDIC, 221 F. Supp. 955 (W.D. Okla. 1962), *aff'd per curiam*, 326 F.2d 971 (10th Cir. 1963) (same). *But see* Lewis v. United States, 680 F.2d 1239 (9th Cir. 1982) (Federal Reserve Bank not federal agency under FTCA because federal government does not control it); Pearl v. United States, 230 F.2d 243 (10th Cir. 1956) (Civil Air Patrol not controlled by United States).

247. 28 U.S.C. § 2671 (1988 & Supp. V 1993).

248. Mendrala v. Crown Mortgage Co., 955 F.2d 1132 (7th Cir. 1992). The Seventh Circuit noted that the government (1) has no ownership interest in Freddie Mac, (2) does not control it, (3) appoints only a minority of its directors, and (4) makes no appropriations to it. *Id.* at 1138. These factors outweighed the fact that Freddie Mac "furthers an important federal mission, and does act as a federal agency or instrumentality in this sense," *id.* at 1139. The court found that this factor was "not dispositive when weighed against the other four factors." *Id.*

ment holds no stock, was entitled to sovereign immunity at all,[249] and this seems to be the minority rule.[250]

2. *The* Merrill *Doctrine*

The *Merrill* doctrine holds that estoppel generally cannot be applied, at least offensively, against the government.[251] Although originally based on principles of sovereign immunity, the doctrine also has been justified as deriving from separation of powers and public policy.[252]

The *Merrill* case concerned the Crop Insurance Corporation, a wholly owned FGC that the Supreme Court equated with "the Government."[253] The doctrine is routinely applied to actions against federal agencies.[254] The Seventh and D.C. Circuits have held that, because Freddie Mac has a public mission, it too should be entitled to *Merrill* doctrine protection.[255] Because of this protection, in the Seventh Circuit and D.C. Circuit at least, FGCs like Freddie Mac enjoy the best of both worlds. Like federal agencies, they have sovereign immunity and *Merrill* doctrine protection. Yet, unlike federal agen-

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249. The Seventh Circuit alluded to this problem in a footnote, *Mendrala*, 955 F.2d at 1134 n.3.

Had Freddie Mac been a foreign corporation it would not have been entitled to foreign sovereign immunity. *See* 28 U.S.C. § 1603(b) (1988) (limiting foreign sovereign immunity to corporations that are organs of a foreign state or are at least 50% owned by foreign government); *id.* § 1605(a)(2) (1988 & Supp. V 1993) (commercial activity exception to immunity).

250. The D.C. Circuit appears to be the only circuit with a similar rule. Construing the FTCA, the D.C. Circuit found the District of Columbia Redevelopment Land Agency immune to suit "in spite of its name and its limited area of operation," because "[r]edevelopment of the Nation's capital is 'the policy of the United States'" and the "Agency receives direct appropriations from the Congress," and "acquires land 'for the use of the United States.'" Goddard v. District of Columbia Redevelopment Land Agency, 287 F.2d 343, 345 (D.C. Cir.), *cert. denied*, 366 U.S. 910 (1961).

A more common result is that found in, for example, the Ninth Circuit. In Lewis v. United States, 680 F.2d 1239 (9th Cir. 1982), the Court found that Federal Reserve Banks are not immune from suit under the FTCA because (1) the government does not have control over their day-to-day operations, (2) the banks are not listed as wholly owned or mixed-ownership government corporations in 31 U.S.C. § 846 or 31 U.S.C. § 856, (3) they are privately owned and receive no congressional monies, and (4) the banks are empowered to sue and be sued in 12 U.S.C. § 341. *Id.* at 1240-42.

251. Federal Crop Ins. Corp. v. Merrill, 332 U.S. 380 (1947). Recent reaffirmations include Office of Personnel Management v. Richmon, 496 U.S. 414 (1990), and Heckler v. Community Health Services, Inc., 467 U.S. 51, 63 (1984).

252. *See Richmon*, 496 U.S. 414; Portmann v. United States, 674 F.2d 1155, 1158-60 (7th Cir. 1982).

253. *Merrill*, 332 U.S. at 384-85. The plaintiff sought compensation for an employee's misinformation regarding the insurability of a crop.

254. *Cf.* A.E. Alie & Sons, Inc. v. United States Postal Serv., 897 F.2d 591 (1st Cir. 1990) (criticizing *Azar*); Rider v. United States Postal Serv., 862 F.2d 239 (9th Cir. 1988) (same). *But see* Azar v. United States Postal Serv., 777 F.2d 1265 (7th Cir. 1985) (*Merrill* doctrine held not applicable to (unincorporated) U.S. Postal Service on facts similar to *Merrill*).

255. Mendrala v. Crown Mortgage Co., 955 F.2d 1132 (7th Cir. 1992); McCauley v. Thygerson, 732 F.2d 978, 982 (D.C. Cir. 1984).

cies they are not subject to the waiver of sovereign immunity in the FTCA.

All FGCs that enjoy sovereign immunity receive greater protection from suit than is available to a private competitor. This advantage persists when the FTCA applies because the government waives less than the full extent of private liability. As a counterweight, however, those same FGCs may be subject to constitutional restrictions as federal actors. FGCs that enjoy sovereign immunity, *Merrill* protection, and are not subject to the FTCA, have greater immunity from suit than is available to either private competitors or agencies—and may not be federal actors subject to the Constitution.

Logically, sovereign immunity should go hand in hand with status as a state or federal actor. The same policies that determine whether constitutional restrictions apply to an entity should be used to determine whether an entity is entitled to the special protections reserved for the nation's agents. Although Congress could, by legislation, confer sovereign immunity on a private body, it makes as little sense for courts to create a class of entities that have sovereign immunity but are not federal actors as it would to create a class of agencies that are federal actors but are ineligible for any immunity. The anomalous position of FGCs like Freddie Mac, combined with the wording of the FTCA, has produced, in a minority of circuits, a peculiar result which does not deserve wider acceptance and may, in fact, warrant reversal. Unfortunately, this minority includes the D.C. Circuit, which is where the majority of such cases are likely to be heard.[256]

E. Lessened Accountability to Congress

The Constitution provides that ordinary agencies are formally accountable to Congress in at least three ways. First, what Congress creates, Congress can destroy; that is, Congress can simply abolish an agency.[257] Similarly, Congress can restructure an agency or require it to act in some manner. Second, Congress has the power of the purse.[258] Third, all civil officers of the federal government are im-

256. There is, however, no reason to deny to wholly government owned and controlled corporations the full benefit of whatever estoppel rule applies to the government. Thus, Helm v. Resolution Trust Corp., 18 F.3d 446 (7th Cir. 1994) (no estoppel against FDIC), and Kershaw v. Resolution Trust Corp., 987 F.2d 1206 (5th Cir. 1993) (per curiam) (no estoppel against RTC), were correctly decided.

257. *See* Glidden Co. v. Zdanok, 370 U.S. 530, 534 (1962) (Harlan, J.) (Congress may repeal tenure or salary of public officers); Crenshaw v. United States, 134 U.S. 99, 107-08 (1890) (Congress cannot be required to fund office not specified in Constitution). For the odd suggestion that Congress cannot constitutionally abolish some administrative offices, see Richard A. Cirillo, Comment, *Abolition of Federal Offices as an Infringement on the President's Power to Remove Federal Executive Officers: A Reassessment of Constitutional Doctrines*, 42 FORDHAM L. REV. 562, 590-93 (1974).

258. U.S. CONST. art. I, § 9, cl. 7.

peachable,[259] which presumably includes the publicly appointed directors of an FGC. Congress's continuing oversight of agency behavior is a fourth, informal and erratic, source of accountability. If FGCs are public bodies, then they are subject to all of these congressional powers, although the power of the purse may have less influence over an FGC with an independent source of income.[260]

Perhaps by design, private and mixed-ownership FGCs are significantly less accountable to Congress than agencies. Because they have alternate sources of funding—debt, equity, or revenue from transactions—Congress's power of the purse is lessened.[261] In addition, because private directors of an FGC do not hold civil office under the Constitution, they are not impeachable. Nevertheless, Congress's leverage over FGCs contains both carrots—removing restrictions on an FGC's activities and providing direct funding—and sticks—adding new restrictions, subjecting the FGC to regulation, and abolishing the FGC entirely.

1. Keeping It Out of Politics

Sometimes FGCs are created in an attempt to insulate an activity from the political process. Entrusting federal responsibilities, or even just federal money, to corporations subject to varying degrees of presidential and congressional control raises difficult questions of constitutional and administrative law, such as when the corporation's action should be characterized as federal action, and whether the corporation must observe First Amendment, due process, and other restrictions in its dealings with the public.[262]

Another fundamental question is whether any justification ever exists for keeping an activity that owes its inspiration and at least part of its funding to the government "out of politics." For many years there has been a consensus that certain areas of public life, notably the money supply, should be insulated from direct political control and entrusted to autonomous bodies such as the Federal Reserve Board. Privately owned FGCs are far more independent than the Federal Reserve Board. The attempt to keep an FGC "out of politics"

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259. *Id.* art. I, § 2, cl. 5, § 3, cl. 6.

260. If a corporation is public then presumably its funds belong to the United States and could be reprogrammed by Congress; ultimately the corporation could even be liquidated.

261. Indeed, the debates at the framing of the Constitution reflected the fear that the federal sale and disposal power might become, in Story's words, "a source of such immense revenue to the national government, as to make it independent of and formidable to the people." 3 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1320, at 196 (Fred B. Rothman & Co. ed., 1991).

262. *See supra* text accompanying note 92.

does not always succeed,[263] which is perhaps fortunate as "out of politics" also means beyond the reach of democratic accountability.

2. *Serving the Clients*

FGCs are used to subsidize certain sectors of the economy. Once the political decision has been made to give a particular group or activity a federal subsidy, an FGC has political advantages as the vehicle for delivery of the benefits. Because some FGC accounts are usually not included in the main part of the federal budget, the subsidy may not be as visible, tending to reduce the opposition from competing interest groups. Because an FGC can operate outside the ordinary bureaucracy, and often enjoys more freedom from congressional and executive control than an agency, Congress also insulates the subsidy program from future Presidents and, to a great degree, future Congresses as well.

A federal charter that creates a self-sustaining corporation provides the enacting Congress with an almost unique means of insulating a program that benefits a favored group from future Congresses.[264] Using an FGC to deliver a subsidy has the additional advantage of not requiring a direct federal expenditure, although it almost inevitably involves indirect costs to the Treasury and competing private interests.

Ordinarily a statute establishing a new program can, at most, set up an institution that will administer it and authorize funding for it. A separate funding bill is then required to appropriate the money. Funding bills typically appropriate money only for the coming year. Thus, the agency remains on a short leash, and the program's beneficiaries are dependent on future Congresses to approve the annual appropriations. By contrast, a self-sustaining program has two advan-

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263. The Legal Services Corporation (LSC), an FGC, is a case in point. *Cf.* Warren E. George, *Development of the Legal Services Corporation*, 61 CORNELL L. REV. 681 (1976) (discussing controversies over LSC policies); *Bush Names Directors of Legal Services Corp.*, N.Y. TIMES, Jan. 12, 1992, at A12 (reporting that, for third time in three years, President Bush made 10 recess re-appointments to LSC because Congress refused to confirm incumbents).

264. Of course, the House and the Senate are not the only parts of government that have an interest in cutting out future Congresses. *See supra* note 16. This interest may, if anything, be stronger in the executive branch:

> Special constituencies and their patron committees in the Congress have joined forces to gain independence from controls by the Executive. The Executive itself has sometimes (as when Fannie Mae was given private status) taken the initiative in such efforts to placate these constituencies or to reduce the apparent size of federal expenditures and deficits. Each new enterprise or loan guarantee has been treated as a special case and new corporations were created in an *ad hoc* manner disregarding prior experience and the rules of responsible government in which public funds must be properly accounted for by private officials.

NAPA, *supra* note 45, at 17. For a discussion of the ways in which legislators bind their successors, and an analysis of their reasons for doing so, see Stewart E. Sterk, *The Continuity of Legislatures: Of Contracts and the Contracts Clause*, 88 COLUM. L. REV. 647, 698-721 (1988).

tages. First, its appropriations do not have to compete with other programs for funds. Second, Congress can entrench a program so that future Congresses must take strong affirmative action to kill it. Because the legislative process makes it far easier to block legislation than to secure its passage, an entrenched program requires only a blocking minority in one House rather than enacting majorities and presidential assent. The result is the rent-seeker's paradise: a one-time victory is locked in virtually forever. Subsidy programs may benefit from an additional degree of political camouflage if the general public comes to perceive the FGC as a private body. A suitably camouflaged, privately owned FGC has an enhanced capacity to capture rents without attracting political opposition because the public is not as aware that the rents are going to the private shareholders.[265]

The ultimate entrenchment device creates a property right that the government must buy back in order to cancel the program. *Dartmouth College v. Woodward* established that a state's grant of a corporate charter can be a contract vesting rights in the corporation.[266] The effects of a federal charter are not any different except that, unlike the State of New Hampshire in the *Dartmouth College* case, the federal government may impair the obligation of contracts,[267] including corporate charters. In theory then, congressional amendments to a private or mixed-ownership FGC's charter that lessen the value of a charter could be characterized as a taking of private shareholders' property compensable under the Fifth Amendment. That is, if a vested right is diminished, shareholders may have a right to claim compensation.[268] To avoid such claims, Congress has reserved the power to amend or repeal at will in many federal corporate charters.[269]

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265. A large theoretical literature exists concerning rent-seeking through government action or a government franchise. *See, e.g.*, TOWARDS A THEORY OF THE RENT-SEEKING SOCIETY (James M. Buchanan et al. eds., 1980) [hereinafter BUCHANAN]; MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION (1965); THE POLITICAL ECONOMY OF RENT-SEEKING (Charles K. Rowley et al. eds., 1988) [hereinafter ROWLEY]; Richard A. Posner, *The Social Costs of Monopoly and Regulation*, 83 J. POL. ECON. 807 (1975); George Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3 (1971).

266. *See* Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 641-50 (1819). *But see* Coombes v. Getz, 285 U.S. 434, 442 (1932); Lake Shore & Mich. S. Ry. v. Smith, 173 U.S. 684, 690 (1899), *overruled on other grounds*, Pennsylvania R.R. v. Towers, 245 U.S. 6, 17 (1917).

267. U.S. CONST. art. I, § 10 applies only to the states. National R.R. Passenger Corp. v. Atchison, T. & S.F. Ry., 470 U.S. 451, 473 n.25 (1985); Pension Benefit Guar. Corp. v. R.A. Gray & Co., 467 U.S. 717, 723-33 (1984).

268. *See* 1 Op. Off. Legal Counsel 126 (1977); *see also* Hobbs, *supra* note 230, at 757 n.116 (describing congressional restructuring of TVA). For a careful discussion of possible constitutional limits to the federal government's power to renege on contracts, including Due Process Clause limits, see Michael H. Schill, *Privatizing Federal Low Income Housing Assistance: The Case of Public Housing*, 75 CORNELL L. REV. 878, 936-44 (1990).

269. *E.g.*, "The Bank shall have perpetual existence unless and until its charter is revoked or modified by Act of Congress. The right to revise, amend, or modify the charter of the Bank is

An FGC in which the government owns no stock also has a potential source of leverage over Congress that agencies lack. Agencies, and corporations in which the federal government owns stock, are not allowed to expend their funds to lobby Congress or make campaign contributions. Private FGCs, even those in which the federal government appoints directors, are not so constrained.[270] Thus, creating a private corporation with a source of funding not only creates a program that can be protected from future Congresses, it also creates one with special means of advancing its own interests. For example, when the Reagan administration indicated that it was considering making Fannie Mae fully independent,[271] Fannie Mae established a political action committee to oppose the Reagan administration initiatives.[272] It also took out more than $100,000 worth of newspaper advertisements to "raise housing as an issue in this election year." Fannie Mae's chairman reportedly told congressmen that if they severed Fannie Mae's links to the government, he would make sure that they had to "run for reelection on a platform that you just made it more expensive to buy a home."[273] Contributions to federal candidates must be disclosed and are relatively easy to monitor. A more insidious problem is the ability of some FGCs to make contributions to private advocacy groups which then lobby Congress on the FGCs' behalf.[274]

Fannie Mae, the oldest GSE, is a privately owned FGC that concentrates on the secondary mortgage market. The President appoints just over a quarter of its directors.[275] Fannie Mae earned about $1.6 billion in 1994, giving it an after-tax return on equity of 24%, which

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specifically and exclusively reserved to the Congress." 12 U.S.C. § 3011 (1988) (charter of National Consumer Cooperative Bank).

270. 18 U.S.C. § 1913 (1988). This prohibition on lobbying with appropriated moneys applies to any "officer or employee of the United States or of any department or agency thereof," *id.*; agency is defined to include "any corporation in which the United States has a proprietary interest, unless the context shows that such term was intended to be used in a more limited sense." *Id.* § 6.

271. *See* U.S. DEP'T OF HOUS. & URBAN DEV., 1987 REPORT TO THE CONGRESS ON THE FEDERAL NATIONAL MORTGAGE ASSOCIATION, ch. 3-4 (1989), *cited in* CBO STUDY, *supra* note 57, at 16 n.9. The President's Commission on Privatization also recommended that Fannie Mae should be fully privatized and that during a transition period it should pay fees for federal attributes, increase equity-to-asset ratios, and satisfy SEC registration requirements. PRIVATIZATION, *supra* note 126, at 38.

272. STANTON, *supra* note 26, at 5, 120.

273. Fran Hawthorne, *Fannie Mae Flexes Its Muscles*, INST'L INVESTOR, Nov. 1988, at 131.

274. *See* H.R. REP. NO. 206, 102d Cong., 1st Sess. 114-15 (1991) (dissenting views of Rep. Jim Leach: "The committee's judgment on the housing provisions of the bill unfortunately was clouded by the endorsement of the approach favored by Fannie and Freddie by a variety of activist consumer groups which without notification to Congress became recipients of substantial contributions from the two GSEs."). Both direct lobbying by FGCs and lobbying via intermediaries may fit the profile of rent-seeking behavior.

275. 12 U.S.C. § 1723(b) (1988 & Supp. V 1993). Fannie Mae currently has a board of 18 directors, five of whom are appointed by the President for one-year terms and the remainder of whom are elected annually by the common stockholders. *Id.*

compares well to the average return on equity of 14.9% for all FDIC-insured commercial banks and 16.4% for the Standard & Poor's (S&P) 500 companies.[276] Fannie Mae's profitability rests heavily on its ability to borrow more cheaply than any private competitor.[277] Estimates vary, but the consensus is that Fannie Mae saves somewhere between 30-75 basis points in borrowing costs compared to an AA-rated private borrower.[278] About half of this pricing advantage is thought to come from the implicit federal guarantee.[279] Fannie Mae's sheer size is a factor as well: Size creates economies of scale. Moreover, size, when coupled with an ever-increasing number of mortgage-backed securities (MBSs) and other outstanding obligations, enhances the secondary market for those obligations. In turn, a strong secondary market provides an incentive for acquiring more obligations.[280]

The implicit government guarantee can be viewed as a subsidy to Fannie Mae. The only direct costs to the Treasury, however, are the contingent liability if Fannie Mae defaults and the government decides to fulfill the market's expectation of an implicit guarantee. In addition, Treasury borrowing costs may increase due to the perception

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276. *See supra* note 187 (describing FNMA profits in 1990 and 1994).

277. *See, e.g.*, GAO CREDIT STUDY, *supra* note 25, at 28 (noting importance of market's perception of implicit guarantee in determining advantageous pricing of GSE debt).

278. *See* CBO STUDY, *supra* note 57, at 10 n.6 (citing studies seeking to measure value of GSE's borrowing advantages). One would expect a comparison between FGC debt and AAA, not AA, bonds because of the implicit federal government guarantee they enjoy. However, available studies use AA bonds as their benchmark because the AA rating is the rating most commonly held by mortgage backed securities. *Id.* at 126. One basis point equals 0.01%. JOHN DOWNES & JORDAN GOODMAN, DICTIONARY OF FINANCE AND INVESTMENT TERMS 31 (2d ed. 1985).

279. S&P defines an AA rating, its second highest, as "having a very strong capacity to pay interest and repay principal and differs from the highest rated issues only in small degree." TREASURY GSE STUDY, *supra* note 26, at A-2. A recent report states that Fannie Mae mortgage-backed securities are priced about 30-40 basis points below AA-rated private mortgage-backed securities. STANTON, *supra* note 26, at 76-77, although Hawthorne, *supra* note 273, at 125, suggests the savings may be as much as 50 basis points (½%). The Treasury estimates that Fannie Mae saves somewhere between 35-75 basis points. 1990 U.S. BUDGET, *supra* note 26, at II-229.

280. CBO STUDY, *supra* note 57, at 13. Recently, the Treasury Department asked S&P to rate Fannie Mae's financial safety and soundness on the assumption that it was cut off from any further federal cash. S&P gave Fannie Mae an "A-" rating. TREASURY GSE REPORT, *supra* note 26, at A-36. An "A" rating is defined as having "a strong capacity to pay interest and repay principal although it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than debt in higher rated categories." A plus or minus suffix signifies "relative standing with the . . . rating category." *Id.* at A-2, A-3. S&P rated four other GSEs as follows: The Farm Credit System was rated at "BB." S&P defines BB as having "less near-term vulnerability to default than other speculative issues. However, it faces major ongoing uncertainties or exposure to adverse business, financial or economic conditions which could lead to inadequate capacity to meet timely interest and principal payments." *Id.* at A-2, A-5. The Federal Home Loan Bank System was rated at AAA, which S&P defines as "[c]apacity to pay interest and repay principal is extremely strong." *Id.* at A-1, A-18. Freddie Mac was rated at A+. *Id.* at A-25. Sallie Mae was rated at AAA. *Id.* at A-46. This suggests that Fannie Mae's actual borrowing advantage over comparable private sector borrowers may be even greater than 30-75 basis points. *See also supra* note 26.

that GSE debt is a relatively good substitute (substitution cost).[281] No study has measured the effect of GSE debt on the market for Treasury bonds, but estimates based on more general empirical work suggest an increase of no more than 2.5 basis points in the Treasury's short-term cost of borrowing for every $100 billion of GSE debt issued, and negligible long-term effects.[282]

Measuring how much of the federal "subsidy" to Fannie Mae is passed on to mortgage borrowers, who are presumably the intended beneficiaries of the subsidy, is a difficult exercise, but studies suggest that the existence of Fannie Mae and Freddie Mac in the secondary market ultimately lowers mortgage rates by up to 50 basis points.[283] Further evidence that Fannie Mae passes on at least a significant fraction of its lower costs to primary lenders comes from studies demonstrating that Fannie Mae's entry into new product markets in the securities field has lowered interest rates in those markets.[284]

The difference between the estimate of Fannie Mae's borrowing advantage (30-75 basis points) and the estimate of the benefit to consumers (25-50 basis points) suggests that while borrowers are getting the lion's share of the savings, either Fannie Mae and/or primary mortgage lenders are benefiting from a rent of up to 50 basis points (one-half percent) on mortgage loans. This rent originates, at least in part, from the investment community's perception that Fannie Mae debt has an implicit federal guarantee. Given that Fannie Mae is expected to issue more than $121 billion in mortgage backed securities in 1996,[285] even a quarter of a percent spread adds up to $300 million. In fact, the Treasury has estimated that the various federal advantages granted to Fannie Mae and Freddie Mac together are worth some $2 to $4 billion per year.[286]

Borrowing at near-Treasury rates, and in some cases enjoying important efficiencies of scale made possible by their monopoly or near-monopoly position in particular credit markets, GSEs can, if they choose, pass on their savings to the groups to which they lend. Privately controlled GSEs, however, have no obligation to do so. A pri-

281. Other costs also may fall on Fannie Mae's competitors in the securities and secondary mortgage markets, some of which may indirectly affect the Treasury. The lost opportunity to sell the federal guarantee to the GSE represents a further indirect cost to the Treasury.

282. *See* CBO STUDY, *supra* note 57, at 18-19. Although the Treasury does not deny the theoretical possibility of a substitution cost, the Treasury does not agree that sufficient evidence exists to show that it is significant. TREASURY GSE STUDY, *supra* note 26, at 47-52. The estimate of 2.5 basis points represents the estimated cost to the Treasury above the increase it would have suffered had it issued the same amount of debt itself. CBO STUDY, *supra* note 57, at 19.

283. 1990 U.S. BUDGET, *supra* note 26, at II-229.

284. *See* CBO STUDY, *supra* note 57, at 137-39 (summarizing empirical work to date).

285. *See* 1996 BUDGET APPENDIX, *supra* note 80, at 1119.

286. *See* H.R. REP. No. 206, 102d Cong., 1st Sess. 114 (1991) (dissenting views of Rep. Jim Leach).

vately owned GSE can keep much of the profit from its intermediation for its shareholders and investors.

The evidence that one GSE, Sallie Mae, did not pass on any of its gains to its ostensible clients—student borrowers[287]—was so damning that the Clinton administration decided to cut out the middleman and have the government begin to make student loans directly.[288] In the case of Fannie Mae, which is the largest GSE, a significant fraction of the interest rate differential goes to its private shareholders, who receive annual dividends and who benefit from retained earnings as their stock appreciates. These gains are an amalgam of a rent and a return on the shareholders' investment, but it is difficult to say which element predominates. The efficient markets hypothesis suggests that shareholders should bid up the price of Fannie Mae stock to a level at which it provides no better risk/return combination than other shares.[289] Similarly, although bond holders receive a higher return than Treasury bill holders, they bear the risk, however minimal, that the GSE will fold and the government will not mount a rescue. The small premium over T-Bills presumably reflects the market's estimate of the value of this risk. Thus, although Fannie Mae benefits from a rent, if the financial markets are efficient then neither current lenders nor investors in Fannie Mae's equity in the secondary market necessarily benefit from it.

Whether purchasers of the original issue of a GSE's equity secure a rent by purchasing shares may depend on the conditions under which the equity is issued and, in some cases, whether investors have the foresight or good fortune to hold their shares long enough. If the shares are issued on the open market, investors should bid up the shares to a point at which there is no rent to be had. If shares are issued to a limited class of persons, however, the reduced market may create a potential rent.[290]

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287. *See* STANTON, *supra* note 57, at v, 11; *see also infra* note 298 (explaining how Sallie Mae avoids bearing any risk). Recent reforms to Sallie Mae's loan authority may change this.

288. *See* 1995 BUDGET ANALYSIS, *supra* note 26, at 142-43 (summarizing new program); Dean Foust, *Sallie Mae: Still a Big Woman On Campus?*, BUS. WK., Nov. 15, 1993, at 160.

289. *See generally* RICHARD A. BREALEY, AN INTRODUCTION TO RISK AND RETURN FROM COMMON STOCKS (2d ed. 1983).

290. Freddie Mac provides an example of a related phenomenon. Freddie Mac used to be owned by the Federal Home Loan Bank System and its members, and was governed by members of the FHLB Board. In 1989, the FIRREA reforms made Freddie Mac an independent, privately owned entity managed by an 18 person board (5 appointed by the President and 13 elected by common shareholders) but subject to regulation by HUD. *See* 12 U.S.C. § 1452 (1988 & Supp. V 1993). Freddie Mac now has a statutory mission that is virtually identical to Fannie Mae's, and the two are effectively competitors in the secondary mortgage market. In 1984, Freddie Mac issued preferred nonvoting stock that could be held only by S&Ls. In 1988, the Freddie Mac board relaxed the ownership restriction, raising the value of the stock held by S&Ls from $50/share to more than $100/share almost overnight. *See* Nathanial C. Nash, *Freddie Mac Clears Stock Sale*, N.Y. TIMES, July 14, 1988, at D1. This windfall, however, was not a classic rent

Several public choice theorists have suggested that rents derived from government benefits will be dissipated totally by socially wasteful expenditures to capture them.[291] Once a GSE has secured the right to a rent it does not need to go back to Congress; its relative insulation from congressional control and its lack of effective competitors render it relatively immune from the competition that could dissipate its rent.[292] Investors, however, face the misfortune of having to compete with each other and, at least in the secondary market, may well be unable to enjoy any of the rent.

Some of the rent may go to the GSE's employees, although this fact alone may not differentiate it from an ordinary managerial firm.[293] Fannie Mae recently paid its retiring chairman a $20 million lump-sum pension payment, in addition to his $7 million annual salary—a payment it justified by saying that he had turned the company around from losing $1 million per day to earning $1 billion a year.[294] Fannie Mae's special stock plan for presidentially appointed directors, designed to "reinforce the mutuality of interest between such directors and the company's stockholders," may give those directors an incentive to prefer the stockholders' interests over the public's.[295]

In the case of Sallie Mae, which Congress established to make a secondary market for student loans at a time when private lenders did not want to invest in them,[296] few of the benefits of the government

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because it did not result from an unproductive activity; if anything, the change made the secondary market for Freddie Mac shares *more* efficient by allowing everyone to participate.

291. *See, e.g.*, Gordon Tullock, *Efficient Rent Seeking, in* BUCHANAN, *supra* note 265, at 97; Gordon Tullock, *Back to the Bog*, 46 PUB. CHOICE 259 (1985). Strict neoclassical economists challenge the view that an expenditure aimed at capturing a rent can be characterized as wasteful given that it is an argument in someone's utility function. *See, e.g.*, Michael A. Brooks & Ben J. Heijdra, *In Search of Rent-Seeking, in* ROWLEY, *supra* note 265, at 27.

292. If there were such an expenditure to secure a GSE charter, it would have to be a one-time expenditure comparable to the present discounted value of Fannie Mae's charter. There is no evidence of any such expenditure.

293. *See* BERLE & MEANS, *supra* note 217. Civil service pay and promotion laws and regulations do not apply to Fannie Mae. 12 U.S.C. § 1723a(d)(2) (1988 & Supp. V 1993).

294. Cindy Skrycki, *Fannie Mae Chief Gets $27 Million Handshake*, INT'L HERALD TRIB., Apr. 4, 1991, at 9 (regarding chairman Maxwell's retirement). Subsequently, Mr. Maxwell declined an additional $5.5 million payment for the company's performance after his retirement that became due to him under a long-term incentive clause in his employment contract. Mr. Maxwell stated that he feared payment of the additional millions could persuade Congress to restrict the pay of Fannie Mae executives. Albert B. Crenshaw, *$5.5 Million Declined by Ex-Official: Fannie Mae's Maxwell Feared New Pay Fight*, WASH. POST, Jan. 22, 1992, at F1. Fannie Mae stated it would "commit" the funds to low-income housing. *Id.* In context, "commit" appears to mean "loan at our usual rate."

295. STANTON, *supra* note 57, at 26 (quoting FANNIE MAE, PROXY STATEMENT DATED MARCH 27, 1987, app. C at 1); Ronald Moe & Thomas Stanton, *Government-Sponsored Enterprises as Federal Instrumentalities: Reconciling Private Management with Public Accountability*, 49 PUB. ADMIN. REV. 329 n.33 (1989).

296. Investors were leery of student loans because student loans are risky and expensive to service. CBO STUDY, *supra* note 57, at 242-43. Sallie Mae has cut service costs and enjoys important economies of scale, *id.* at 248, 262, but these savings have not been passed on to student borrowers.

guarantee reached the students who were the purported beneficiaries.[297] In addition to benefiting from an implicit federal guarantee, Sallie Mae deals primarily in loans that are insured by the government, which means it faces little if any credit risk. Indeed, the government pays a substantial, explicit subsidy to the lenders from which Sallie Mae purchases loans.[298]

FGCs make a politically attractive vehicle for delivering subsidies because the absence of an actual appropriation makes them appear costless. If the long-term substitution cost to the Treasury is indeed negligible as some studies suggest,[299] and the subsidies do indeed reach their intended beneficiaries, FGCs impose no direct costs on the public.

Regardless of the extent of their direct costs, however, FGCs clearly create two types of opportunity cost and a contingent risk for Congress and the taxpayer. First, because an FGC must ordinarily borrow at a rate slightly higher than the Treasury, the public that the FGC is designed to serve pays a premium for funds compared to what it would pay if the debt were guaranteed by the full faith and credit of the United States. Second, to the extent that private investors provide the equity for a GSE and receive dividends as a return, the taxpayer (or the would-be beneficiary of the program) loses sums that might have been available had the government provided the equity capital.[300] The contingent risk arises from the fact that the government might rescue a GSE that fails.

3. *The Contingent Risk: The Next S&L Crisis?*

The separate personality of an FGC not owned and controlled by the federal government almost certainly means that the federal government has no formal, legal obligation to make good the debts of an

297. STANTON, *supra* note 57, at 1 (Sallie Mae "keep[s] most of the benefits for shareholders rather than passing them on to lower the interest rate on loans it funds.").

298. CBO STUDY, *supra* note 57, at 31, 244. Because Sallie Mae deals almost exclusively in student loans that have been guaranteed by the government, it bears almost no risk. *See* 1991 U.S. BUDGET, *supra* note 220, at 242. Any remaining risk is immediately swapped away. STUDENT LOAN MKTG. CORP., SALLIE MAE ANN. REP. 1990, at 17. At the end of 1986, Sallie Mae had purchased $8 billion in guaranteed student loans and provided advances to help fund another $6.5 billion. Sallie Mae also has branched out into many unrelated businesses, e.g., financing home equity loans. STANTON, *supra* note 57, at 4. It also has subsidiaries, such as Minnesota Guarantor Servicing, Inc. *See* CBO STUDY, *supra* note 57, at 251. Sallie Mae even bought a savings and loan, STANTON, *supra* note 57, at 13 & n.48; *see also* FRANCES J. LEAZES, JR., ACCOUNTABILITY AND THE BUSINESS STATE 81-82 (1987) (discussing Sallie Mae's evolution), prompting Congress to enact limits on Sallie Mae's diversification, prohibiting ownership of a bank, S&L, savings bank, or credit union. CBO STUDY, *supra* note 57, at 259.

299. *See supra* note 282.

300. The opportunity cost is set off by the use value of the funds that government did not have to make available initially. In a perfect world the present value of these two sums would be identical at the time the GSE is created.

insolvent FGC. Nevertheless one GSE has encountered difficulties since World War II, and the government has responded by authorizing up to $4 billion to rescue it.[301] Given the size of most GSEs, the political pressure to rescue a failed GSE again almost certainly would be overwhelming. The practical consequence of this political reality is to weaken Congress's power of the purse by holding the nation potentially liable for unauthorized debts—debts that may have been incurred to increase private profits rather than to further a public purpose set by Congress.

GSEs carry less capital than comparable private financial institutions.[302] Either GSEs are not subject to capital requirements,[303] or the current rules are antiquated; they fail to provide for GSE expansion into new types of business, such as guarantees. As a result, GSEs tend to hold lower capital levels than do regulated financial entities. The lower capital ratios allow the GSEs to benefit from increased leverage on the funds they control, which may either increase their ability to fulfill their public purposes, contribute to the GSEs' profits, or both.[304]

The financial risk from all but a few GSEs appears, however, to be negligible, and even the GSEs most at risk are not in great danger.[305] The S&L crisis was caused in large part by the perverse incentives produced by federal deposit insurance. The managements of troubled S&Ls knew that the government insured a large majority of their depositors' money at a cost that did not account for the riskiness of an individual S&L's behavior. A failing S&L thus had an incentive to take desperate, risky measures, and its depositors did not have an incentive to prevent it. When property prices fell and took the S&L's assets with them, these S&Ls, given their incentives, reacted rationally, plunging deeper into debt and ultimately incurring losses that exceeded the sums available to the FSLIC.

In theory, the essentially limitless access to cheap borrowing could create an incentive for a GSE's management to borrow reck-

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301. CBO STUDY, *supra* note 57, at 69 (discussing rescue of Farm Credit System); *see also supra* note 220 (discussing reasons for FCS insolvency).

302. Private financial institutions that issue securities or guarantees similar to those issued by GSEs are subject to safety and soundness regulations; the most common type of safety and soundness regulation is a capital requirement. In theory, requiring a financial enterprise to hold a certain level of capital discourages excessive risk taking by ensuring that the owners have something to lose. If nothing else, capital requirements postpone insolvency. *See* 1991 U.S. BUDGET, *supra* note 220, at 251. Increasing the amount of capital that an enterprise must retain reduces its gearing, or debt-to-equity ratio, thereby reducing its ability to make financial commitments such as loans or guarantees and (assuming its business is profitable) reducing its profits.

303. Capital requirements are rules requiring an institution to hold a particular percentage of its assets in liquid or low-risk reserves. For many years Sallie Mae and Farmer Mac had no minimum capital levels, GAO FRAMEWORK, *supra* note 187, at 9, but this has now changed. *See* 20 U.S.C. § 1087-2(r) (Supp. V 1993) (imposing modest capital requirements on Sallie Mae).

304. Alternately, the lower capital requirement may increase the rents available to be paid out. *See supra* text following note 264; *see also supra* note 265.

305. *See supra* note 26.

lessly once it reaches a point where it has little or no capital left to lose.[306] Currently, however, only one of the GSEs is arguably low on capital, and this moral hazard seems a remote specter.[307] Unlike the S&Ls, which were numerous and dispersed, and therefore difficult to monitor, only a handful of GSEs exist, making them relatively easy to monitor. Indeed, the Treasury argues that GSEs pose a greater threat than did S&Ls precisely because there are so few of them—the five largest GSEs alone have obligations that exceed the total deposits of the more than 2000 insured S&Ls. Mismanagement by a small group of private persons could, the Treasury argues, expose the government to (moral) obligations as large as the S&L bailout.[308] Implicit in the Treasury concern is a legitimate fear that because there is no supervisory power over most GSEs' safety and soundness, under the current regime a GSE could become insolvent, or at least sufficiently capital-poor to be subject to moral hazards, long before Congress could organize a response.

4. *Inadequacy of the Government Corporation Control Act*

Congress's previous attempt to control FGCs was, at most, a limited success. At the end of World War II, the United States had sixty-three wholly owned and thirty-eight partly owned FGCs as well as nineteen noncorporate credit agencies and hundreds of military-run enterprises.[309] In response to this proliferation of FGCs, inconsistent accounting standards, and a general lack of federal control and accountability,[310] Congress enacted the Government Corporation Control Act (GCCA).[311] The GCCA required the liquidation of FGCs chartered in the District of Columbia and not reincorporated by, or pursuant to, an act of Congress within the next two and a half years.[312] It subjected all existing FGCs to a new regime of audit and budgetary control.

From its inception, the GCCA distinguished between wholly owned government corporations and mixed-ownership corporations. Wholly owned corporations were subject to much tighter control. They submitted an annual "business-type budget" to the President to

306. *See supra* text accompanying note 206.

307. Of the GSEs intended to be self-sustaining, only the Farm Credit System is arguably in any danger. *See supra* notes 26, 280.

308. TREASURY GSE STUDY, *supra* note 26, at 2.

309. WALSH, *supra* note 175, at 29.

310. *See, e.g.*, Oliver P. Field, *Government Corporations: A Proposal*, 48 HARV. L. REV. 782 (1935) (describing problems caused by wide variation among then-existing corporations).

311. Pub. L. No. 79-248, 59 Stat. 597 (1945) (codified as amended at 31 U.S.C. §§ 1105, 9101-09 (1988 & Supp. V 1993)) [hereinafter GCCA].

312. GCCA, *supra* note 311, § 304(b), 59 Stat. at 602.

modify as he saw fit and then transfer to Congress,[313] and were subject to periodic audits.[314] The GCCA gave the Treasury the power to set the terms and price of any debt issued by most FGCs.[315] (In practice, however, the Treasury does not exercise this power except to insure that GSE debt is not issued on dates that would conflict with Treasury issues.) Mixed-ownership government corporations were free to make their own budgets, although the GCCA contemplated presidential recommendations that mixed-ownership corporations return government capital to the Treasury.[316]

The orderly approach of the GCCA reflected the administrative theory of the day, which held that the corporate form should be restricted to predominantly commercial government programs.[317] Chaos quickly returned, however, as Congress exempted the majority of FGCs created after 1945 from all or part of the GCCA.[318] And although the GCCA also prohibits the creation or acquisition of new FGCs by the executive branch without specific legal authorization,[319] at times this rule has been ignored.[320]

Although the GCCA brought temporary order to the oversight of the FGCs within its purview, it did little to resolve the basic issue of where FGCs fit into the legal order. Labelling some FGCs as "pri-

313. 31 U.S.C. § 9103(a) (1988 & Supp. V 1993). The first year's audit covered 58 FGCs with combined assets of $30 billion. E. LESLIE NORMANTON, ACCOUNTABILITY AND AUDIT, STATE-OWNED ENTERPRISE IN THE WESTERN ECONOMIES 157 (Raymond Vernon & Yair Ahoroni eds., 1981).

314. GCCA, *supra* note 311, § 105, 59 Stat. at 599. Amendments adopted in 1982 to the GCCA require the Comptroller General to perform triennial audits of all corporations it covers and report to Congress, the Treasury, and the President. 31 U.S.C. §§ 9105(a)-06(a) (1988 & Supp. V 1993).

315. 31 U.S.C. § 9108(a) (1988 & Supp. V 1993). Mixed-ownership government corporations are exempt "when the corporation has no capital of the Government," *id.* § 9108(d)(1), as are certain other listed corporations. *Id.* § 9108(d)(2).

316. GCCA, *supra* note 311, § 203, 59 Stat. at 600.

317. *See supra* note 176 and accompanying text.

318. *See, e.g.*, MOE, *supra* note 34, at 41-42 (discussing various corporations exempt from GCCA); Harold Seidman, *Public Enterprise in the United States, in* 1 ANNALS OF PUBLIC AND CO-OPERATIVE ECONOMY (1983) (17 out of 30 of the corporations created by Congress in a 15-year period were exempt from the GCCA).

319. GCCA, *supra* note 311, § 304(a), 59 Stat. at 602, *amended by* Pub. L. No. 97-258, 96 Stat. 1042 (codified as amended at 31 U.S.C. § 9102 (1983)).

320. The most flagrant case is probably the creation of the Federal Asset Disposition Administration (FADA), which was established as a Colorado corporation by an agency that apparently lacked congressional authority to do so. *See* 1988 Op. Com. Gen. B-226708.3 (1988), *available in* 1988 LEXIS 1587, Genfed Library, Comgen File (concluding that Federal Home Loan Bank Board "acted improperly" by establishing FADA; and that FADA employees are not federal employees because they fail to satisfy criteria in 5 U.S.C. § 2105(a) despite being "engaged in the performance of federal functions"); 134 CONG. REC. E1185-86 (1988) (remarks of Hon. Paul E. Kanjorski) (alleging FADA was established to evade pay caps, personnel ceilings, and "budgetary and legal constraints"); *see also* LAWRENCE J. WHITE, THE S&L DEBACLE 144 n.28 (1991) (describing FADA as having potential to achieve best of both worlds by "carry[ing] out governmental functions, but be able to attract the specialized skills in asset management and disposal that required private sector salaries" but having "early leadership . . . insensitive to the political nuances of Washington"); Harold Seidman, *The Quasi World of the Federal Government*, BROOKINGS REV., Summer 1988, at 23, 26 (summarizing controversy over FADA).

vate" and others as "mixed-ownership" may provide a congressional finding of fact or declaration of policy as to how certain FGCs are to be treated in the courts, but the categories themselves bear little relation to the FGC's relations with the government. There is no reason why, for example, a "mixed-ownership" FGC in which the government owns no shares should be treated differently than a private FGC with some directors appointed by the President.

The result has been confusion: sometimes FGCs are held to be public,[321] and sometimes they are held to be private or partially private.[322] Indicia of publicness include whether the FGC's staff is in the civil service, and whether the FGC is directly controlled by an agency[323] or by government directors.[324] Indicia of privateness may focus on the FGC's activity. For example, FGCs engaged in market transactions, such as foreclosing on a mortgage, usually succeed in repulsing due process and other constitutional claims as well as claims that they have a duty to behave like an agency.[325]

F. Lessened Accountability to the President and Regulators

If an FGC is public, then its relationship with the President and with the executive branch is, at a formal level (i.e., discounting political constraints), essentially hierarchical. The President does not control private firms; instead, the agencies that the President controls have wide regulatory powers. FGCs, however, are often less closely regulated than their private counterparts. The result in some cases is

321. Lebron v. National R.R. Passenger Corp., 115 S. Ct. 961 (1995) (Amtrak federal actor for First Amendment); Gaubert v. United States, 499 U.S. 315, 319 (1991) (FDIC subject to FTCA); Rainwater v. United States, 356 U.S. 590, 592 (1958) (fraudulent crop loan application made to the Commodity Credit Corporation is a claim against the government within the False Claims Act); McCauley v. Thygerson, 732 F.2d 978, 982 (D.C. Cir. 1984) (Freddie Mac considered "a federal entity" for employment relations and hence subject to narrower promissory estoppel); Rust v. Johnson, 597 F.2d 174, 178 (9th Cir.) (state foreclosure on property subject to Fannie Mae mortgage was impermissible exercise of state power over "property of the United States"), *cert. denied*, 444 U.S. 964 (1979); Association of Data Processing Serv. Orgs. v. Federal Home Loan Bank Bd., 568 F.2d 478, 483 (6th Cir. 1977) (FHLB subject to APA); Rocap v. Indiek, 539 F.2d 174, 177 (D.C. Cir. 1976) (Fannie Mae subject to FOIA amendment affecting "Government controlled corporation[s]"); Ackerley v. United States, 741 F. Supp. 1519, 1520-21 (D. Wyo. 1990) (FDIC is subject to FTCA).

322. Ralis v. RFE/RL, Inc., 770 F.2d 1121, 1124-25 (D.C. Cir. 1985) (Radio Free Europe is not a "government controlled corporation"); Warren v. Government Nat'l Mortgage Ass'n, 611 F.2d 1229, 1232-34 (8th Cir.) (Ginnie Mae foreclosures are not government action), *cert. denied*, 449 U.S. 847 (1980); Roberts v. Cameron-Brown Co., 556 F.2d 356, 358-60 (5th Cir. 1977) (Fannie Mae acts are private action); Reconstruction Fin. Corp. v. Langham, 208 F.2d 556, 559 (6th Cir. 1953) (district court had jurisdiction over employment claim because RFC employee is not federal government employee).

323. *See, e.g.*, *Rainwater*, 356 U.S. at 591 (noting that Commodity Credit Corp. is subject to supervision and direction by the Secretary of Agriculture and that all Commodity Credit employees are deemed Department of Agriculture employees).

324. *Lebron*, 115 S. Ct. 961.

325. *See supra* note 322.

that the President, and the executive branch as a whole, lack both the direct authority and the regulatory authority to ensure that FGCs accomplish their statutory objectives.

1. *Attenuated Accountability of Publicly Appointed Directors*

The President has formal control over most federal agencies.[326] In modern practice, the constitutional concept of a unitary executive headed by the President is sufficiently flexible to permit the existence of independent agencies headed by officials whom the President appoints to fixed terms during which he ordinarily cannot remove them without cause. Even with this significant exception to the President's otherwise plenary power over the top officials in the executive branch, the hallmarks of the President's executive primacy include his power to appoint all, and remove nearly all, principal officers in the executive branch. In *Bowsher v. Synar*, as in earlier cases, the Supreme Court emphasized the close connection between the power to remove an official and the power to control her.[327] The President's appointment and removal power is the formal foundation of agency accountability to the President, just as Congress's ability to change an agency's powers by statute, and its power of the purse, are the formal foundations of accountability to Congress. The FGCs that are wholly owned by the United States *and* have a majority of directors appointed by the President are just as accountable to the President as are traditional agencies—however much or little that may be. FGCs over which the President lacks this control are probably not agencies for constitutional purposes; they are more analogous to private firms.

If a federal officer is appointed improperly, or if the statute creating the office contains an improper removal provision, then her office must be categorized as outside the executive branch. In *Buckley v. Valeo*, the Supreme Court ruled that the Appointments Clause[328] does not allow the legislative branch to usurp for itself the President's appointing authority.[329] *Buckley* also made clear that the Court was prepared to declare void all actions by an agency headed by an invalidly

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326. Some agencies, for example the Federal Trade Commission, are "independent." This independence is often attacked as being bad policy, or even unconstitutional, on the grounds that a democratic form of government requires that the public executive power should be exercised by persons ultimately accountable to an elected official, usually the President, and thus in some way, however attenuated, accountable to the people. "[O]ne of the weightiest objections to a plurality in the executive . . . is that it tends to conceal faults and destroy responsibility." THE FEDERALIST No. 70, at 427 (Alexander Hamilton) (Clinton Rossiter ed., 1960). *See generally* Strauss, *supra* note 164.

327. *See* Bowsher v. Synar, 478 U.S. 714, 728-32 (1986); Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 58-60 (1982) (plurality opinion); Weiner v. United States, 357 U.S. 349, 356 (1958).

328. U.S. CONST. art. II, § 2, cl. 2.

329. Buckley v. Valeo, 424 U.S. 1, 127-28 (1976) (per curiam).

appointed official,[330] a point reiterated in *Bowsher*.[331] Article II of the Constitution provides the only alternatives to presidential appointment by authorizing Congress to vest the appointment of "inferior Officers . . . in the President alone, in the Courts of Law, or in the Heads of Departments."[332] The Supreme Court also upheld the judicial appointment of a special prosecutor, whom the Court described as an "inferior officer."[333]

If a corporation is a public body like an agency, its top officials must be officers of the United States, or at least inferior officers of the United States appointed in the manner set out in Article II. Ordinarily, the statute creating an FGC sets out the method of appointment of all the directors. The appointment of directors by the President often makes the post subject to the advice and consent of the Senate. Clearly, however, whether the corporation is seen as public or private, and regardless of the percentage of the government's shareholding, the government's directors hold public office as defined in *United States v. Hartwell*: "An office is a public station, or employment, conferred by the appointment of government. The term embraces the ideas of tenure, duration, emolument, and duties."[334] As public officials, public directors must be appointed in conformity with the Appointments Clause, that is, either by the President (with the advice and consent of the Senate, if required) or by another official in the executive branch.[335]

The *Hartwell* definition of "public office" is distinctly preferable to that suggested in *Osborn*, where Chief Justice Marshall airily stated, "It will not be contended, that the directors, or other officers of the bank, are officers of the government."[336] The *Hartwell* definition

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330. *See id.* at 142.

331. 478 U.S. at 726-27; *see also* Metropolitan Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc., 501 U.S. 252 (1991) (holding that participation of members of Congress in committee with power to veto decisions regarding local airports violated separation of powers).

332. U.S. CONST. art. II, § 2, cl. 2.

333. Morrison v. Olson, 487 U.S. 654 (1988) (holding that the independent special prosecutor is an "inferior official" because she can be removed, albeit only for cause, by the Attorney General and thus is in some sense a subordinate official rather than one directly responsible to the President); United States v. Perkins, 116 U.S. 483, 485 (1886) (holding that Congress may insulate inferior officers from dismissal by President); *see also Buckley*, 424 U.S. at 132 (explaining distinction between officer and inferior officer); United States v. Germaine, 99 U.S. 508, 509-10 (1879) (same).

334. United States v. Hartwell, 73 U.S. (6 Wall.) 385, 393 (1867) (concerning a clerk to the Assistant Treasurer); *see also Buckley*, 424 U.S. at 126 (describing the phrase "Officer of the United States," in context of Appointment Clause, as an "appointee exercising significant authority pursuant to the laws of the United States"). *But see* Pierce v. United States, 314 U.S. 306, 310 (1941) (holding that officers and employees of TVA were not within meaning of the term used in criminal statute enacted before TVA was incorporated).

335. U.S. CONST. art. II., § 2, cl. 2.

336. Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738, 866-67 (1824) (Marshall, C.J.) (dictum). Interestingly, at the time *Osborn* was decided, qualified immunity had not yet been invented and public officials were at least as subject to common-law liability as private

contends exactly that. The *Hartwell* view should be applied to public directors of FGCs. Otherwise, if public FGC directors are not public officials, appointment in conformity with the Appointments Clause is meaningless. Theoretically, Congress could authorize the Speaker of the House, or a congressional Joint Committee, to appoint directors of an FGC.[337] The consequences would devastate presidential power.

This possibility, however, is remote because the Supreme Court subsequently ignored Marshall's dictum regarding the directors of the Bank of the United States. Instead, in *Springer v. Philippine Islands*, the Court essentially applied the *Hartwell* definition of a public office to a wholly owned government corporation.[338] The Court held that voting stock to appoint directors in a government corporation, whether viewed as a sovereign or a proprietary action, is an executive act that only an executive official may perform.[339] This principle is equally applicable to all federally appointed directors, even if the government owns no shares in the entity.

Presidential appointment of all of a corporation's directors by and with the consent of the Senate clearly complies with the Appointments Clause's requirements for officers of the United States. By contrast, the selection of even a fraction of the directors by private stockholders (or worse, members of Congress[340]) may so violate the separation of powers as to make the corporation illegally constituted. The Appointments Clause contemplates presidential appointment, judicial appointment, and appointment by officers in the executive branch. Whether one views directors as principal officers or inferior officers, no reading of the Appointments Clause, however broad, could conceivably encompass the appointment or election of an "officer of the United States" by private citizens. To escape unconstitutionality, therefore, any corporation with one or more directors appointed in a manner that does not conform to the Appointments Clause must be something very different from an agency—it must be a private body. Indeed, in 1962 Attorney General Robert F. Kennedy opined that

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citizens. *See* David E. Engdahl, *Immunity and Accountability for Positive Governmental Wrongs*, 44 U. COLO. L. REV. 1 (1972). Chief Justice Marshall noted, but did not decide, the appellants' argument that the Incompatibility Clause, which prohibits a member of Congress from serving in the executive branch, did not apply to the directors of the Bank. U.S. CONST. art. I, § 6, para. 2.

337. Another possibility is an FGC whose directors are drawn from Congress itself. *See infra* note 401. If the directorship of an FGC is not a public office, presumably, although not inevitably, it is not a "civil office" for the purpose of the Incompatibility Clause, U.S. CONST. art. I, § 6, para. 2.

338. 277 U.S. 189 (1928) (Sutherland, J.); *see also* Metropolitan Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc., 501 U.S. 252, 274 (1991) (Stevens, J.) (dictum) (citing *Springer* with approval). The *Springer* Court, although addressing the Philippine Organic Act and not the U.S. Constitution, based its reasoning on federal separation of powers grounds. *See* 277 U.S. at 200-01.

339. *Springer*, 277 U.S. at 203-05.

340. *See, e.g.*, *Metropolitan Wash. Airports Auth.*, 501 U.S. at 274.

presidentially appointed directors of COMSAT, a fully private FGC, did not meet the *Hartwell* test and thus were not officers of the United States and were not impeachable.[341] Subsequent Supreme Court decisions make this view very problematic. If the corporation is a private body, the Senate's participation in the appointment of even one of its directors probably violates the strictures of *Chadha*, which require that all congressional action affecting private rights requires action by both houses of Congress and presentment to the President.[342]

The President's removal power derives from both the Appointments Clause[343] and the constitutional injunction that the President "shall take care that the laws [are] faithfully executed."[344] This power has limits: Congress may insulate certain high officers from removal without "cause," although precisely which posts and for what cause are not clear. *Humphrey's Executor v. United States* was the first of several cases that sought to draw a line between officers who had "purely executive" functions and whom Congress could not therefore insulate from presidential removal and another, ill-defined class of officers with different functions.[345] Subsequent courts struggled with nomenclature such as "quasi-executive" and "quasi-legislative" to describe these other functions, but these terms were neither clear nor free from criticism.[346] In *Morrison v. Olson*,[347] however, Chief Justice Rehnquist abandoned the effort to draw a bright line when he wrote that "the determination of whether the Constitution allows Congress to impose a 'good cause'-type restriction on the President's power to remove an official cannot be made to turn on whether or not that official is classified as 'purely executive.' "[348] Rather than relying on "rigid categories,"[349] the Chief Justice defined the "real question" as "whether the removal restrictions are of such a nature that they impede the President's ability to perform his constitutional duty, and the functions of the officials in question must be analyzed in that light."[350]

Most statutes providing for presidential appointment of directors to FGCs are silent about removal. Courts should follow the cases re-

341. Communications Satellite Corp., 42 Op. Att'y Gen. 165 (1962).

342. *See* Immigration & Naturalization Serv. v. Chadha, 462 U.S. 919, 951-59 (1983).

343. Shurtleff v. United States, 189 U.S. 311, 318 (1903) (explaining that the "right of removal [is] inherent in the power of appointment"); *Ex Parte* Hennen, 38 U.S. (13 Pet.) 230, 259 (1839).

344. U.S. CONST. art. II, § 3; *see also* Morrison v. Olson, 487 U.S. 654, 689-90 (1988).

345. Humphrey's Ex'r v. United States, 295 U.S. 602, 631-32 (1935).

346. *See, e.g.*, Froomkin, *supra* note 171, at 1348-49.

347. *See supra* notes 165-66 and accompanying text.

348. *Morrison*, 487 U.S. at 689.

349. *Id.*

350. *Id.* at 691.

lating to independent agencies and find at least a "good cause" removal power in the absence of a congressional statement to the contrary.[351] If the FGC is private, courts should not assume that the entity's corporate status entitles the nation's directors to any more independence from the "shareholder," i.e., the government, that selected them. If the FGC is public, the directors constitutionally cannot have any more independence than other federal officers. Indeed, in the only modern case to review the removal of an FGC director, the Sixth Circuit treated the wholly owned nonstock TVA as an ordinary agency and its directors as no different from executive officers who serve at the pleasure of the President.[352] The Sixth Circuit determined that the TVA "exercises predominantly an executive or administrative function . . . it is predominantly an administrative arm of the executive department" and that the TVA director's argument that the TVA resembled an independent agency failed.[353]

2. *Private Directors Not Accountable to President*

Privately appointed directors (and publicly appointed directors if one follows *McCulloch* instead of *Hartwell*) are not public officials. Even if they owe their office to the statute chartering or funding the corporation, their appointment remains a private affair, dictated by

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351. In Weiner v. United States, 357 U.S. 349, 355-56 (1958), the Supreme Court unanimously refused to imply that the President had the power to remove a member of the War Claims Commission without cause when the statute was silent about removal. The Court has never had to decide whether to imply "good cause" removal. The decision in *Weiner* rested heavily on the "quasi-judicial" adjudicatory role of the Commission. *See id.* at 355. Even if the classification of functions in Myers v. United States, 272 U.S. 52 (1926), Humphrey's Executor v. United States, 295 U.S. 602 (1935), and *Weiner* has survived Morrison v. Olson, 487 U.S. 654 (1988), most, if not all, FGCs perform functions that would have to be classified as executive if indeed they are governmental at all.

352. Morgan v. Tennessee Valley Auth., 115 F.2d 990, 992-93 (6th Cir. 1940), *cert. denied*, 312 U.S. 701 (1941). President Roosevelt attempted to replace TVA director Morgan before the incumbent's nine-year term expired. Morgan argued that because the TVA statute gave only one ground for removal—engaging in political appointment or promotion of an employee—the President lacked the authority to fire him. Seeking to come under the rule set out in *Humphrey's Executor*, which held that the FTC's status as a "quasi-legislative" body entitled its commissioners to protection from dismissal without cause, Morgan argued that TVA more closely resembled the FTC than a normal agency.

353. The Sixth Circuit also stated that the TVA lacked the "quasi-legislative" functions that had insulated the FTC from the otherwise sweeping presidential power to dismiss officials in *Humphrey's Executor*. *Morgan*, 115 F.2d at 993-94. Morgan apparently failed to argue that TVA's corporate form and independent legal personality offered him more protection than afforded to what are now known as independent agencies. Combined with TVA's relatively unusual nonstock corporate structure, Morgan's failure to raise this argument limits the importance of what would otherwise be the major modern case determining the relationship between FGCs and the President.

More recently, President Nixon removed a director of Fannie Mae appointed by President Johnson; newspaper reports suggested that the removal was motivated by the director's attempt to continue sending Fannie Mae's local foreclosure business to firms with connections to the Democratic party rather than switching to Republican ones. *See* Comment, *supra* note 238, at 386 n.98, 390 n.115.

private shareholders. The separation of powers concerns, particularly fear of legislative aggrandizement, that animate recent decisions limiting Congress's involvement in the appointment process (such as *Chadha*), simply do not apply. Absent specific statutory authorization,[354] the President cannot remove directors whom he does not appoint, if only because the removal power derives primarily from the appointment power.

3. *Weak Programmatic Control of Private and Mixed-Ownership FGCs*

FGCs not controlled by the government are, theoretically, subject to the same federal regulatory powers as ordinary private firms. In practice, however, their public purpose, their links to the government, the existence of the implicit guarantee, and their general uniqueness have all combined to exclude many FGCs from the same degree of federal regulation as comparable private firms. States are unable to fill the regulatory vacuum because, absent legislation to the contrary, a federal charter gives a corporation the same immunity from state regulation as enjoyed by the federal government itself. Most FGCs thus exist in a regulatory environment characterized by a relative absence of oversight and programmatic control at any level of government. Similarly, FGCs, even those heavily involved in the financial markets, face little overt regulation. For example, whether the Administrative Procedure Act,[355] the Freedom of Information Act,[356] or the Debt Collection Act[357] applies is rarely clear.[358] One thing that is clear, however, is that the FGCs involved in the financial markets are not required to comply with the SEC registration requirements or safety and soundness rules (minimum levels of capital) required of their purely private competitors.

FGCs ordinarily are created to achieve a public purpose, but in many cases the federal government does not monitor their activities in an organized fashion. The extent of federal agency oversight over FGCs varies enormously. At one extreme lies the wholly owned FGCs that are little more than departments of an agency; at the other lies FGCs that are subject to little if any oversight. Congressional over-

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354. The FNMA Charter Act gives the President the authority to remove privately elected directors. *See* 12 U.S.C. § 1723(b) (1988 & Supp. V 1993).

355. Pub. L. No. 79-404, 60 Stat. 237 (1946) (codified as amended in scattered sections of 5 U.S.C.).

356. 5 U.S.C. § 552 (1988 & Supp. V 1993).

357. 31 U.S.C. § 3717 (1988 & Supp. V 1993) (requiring agencies to assess interest and penalties on debts owed the United States unless otherwise governed by statute, regulation or contract).

358. *See* GAO PROFILES, *supra* note 16, at 236-51 (table showing FGC's views of which of 25 acts applicable to agencies apply to them).

sight and GAO audits are the only monitoring devices that apply to all FGCs. These are week reeds at best. Congressional oversight is notoriously uneven; GAO audits are more predictable, but are limited to information provided by the FGC. And, the audits focus on balance sheets rather than the degree to which FGCs are fulfilling their public purposes.

Fannie Mae, for example, has statutory responsibilities to provide funds for loans for affordable housing. The legislation giving Fannie Mae that duty also gives HUD oversight responsibility; but HUD's actual powers over Fannie Mae are unclear.[359] HUD has argued that it can issue regulations that would require Fannie Mae to make particular types of loans.[360] Fannie Mae, however, disagrees,[361] and HUD has never overcome Fannie Mae's resistance.[362] Sallie Mae is the most extreme example, as no federal agency even claims the power to regulate Sallie Mae.[363]

Without some form of routine programmatic control, neither the federal government nor the public are adequately positioned to determine whether FGCs are meeting their goals, be they the efficient provision of goods and services, provision of nonmarket goods, or the exploitation of a government-granted monopoly. The piecemeal authority that characterizes the programmatic regulation of FGCs also may make it difficult for the government to do anything if it determines that an FGC is failing to serve the purposes for which it was designed.

G. *Deficit Politics*

FGCs excel as a device that Congress and the President can use to disguise the size of federal expenditures, and in particular, evade debt ceilings such as the Gramm-Rudman-Hollings budget requirements,[364] or a hypothetical balanced budget amendment. Charging expenditures and borrowing to private and mixed-ownership government

359. *See* 12 U.S.C. § 1452(b) (1988 & Supp. V 1993). Previously, the Secretary of HUD could require that a "reasonable portion" of Fannie Mae's mortgage purchases be "related to the national goal of providing adequate housing for low and moderate income families, but with reasonable economic return to the corporation," *id.* § 1723a(h) (1988); however, in 1992 that language was repealed. *Id.* § 1723a(h) (Supp. V 1993).

360. STANTON, *supra* note 26, at 59.

361. *Id.* at 60.

362. *HUD Hearings*, *supra* note 234, at 211-12 (statement by Alfred DelliBovi, Deputy Secretary, HUD, that existing HUD powers are inadequate).

363. CBO STUDY, *supra* note 57, at 35.

364. Balanced Budget and Emergency Deficit Control Reaffirmation Act of 1987, Pub. L. No. 100-119, tit. I, 101 Stat. 754, *amended by* Budget Enforcement Act of 1990, Pub. L. No. 101-508, tit. XIII, 104 Stat. 1388-1573 (current version at 2 U.S.C. §§ 901-09 (1988 & Supp. V 1993)).

corporations can be hidden "off budget."[365] Using this device, FGC spending and borrowing easily avoids triggering the deficit reduction process, and also protects it from external triggers, thus making FGCs the vehicle of choice for borrowing without the constraints of budget targets.[366]

Three of the eleven GSEs—the Financial Assistance Corporation (FICO),[367] the Farm Credit System Financial Assistance Corporation (FAC),[368] and the Resolution Funding Corporation (REFCORP)[369]—are unlikely to turn a profit, are not truly designed to be self-sustaining, and are, in fact, little more than an accounting trick, one that has justly been called the budget gimmick of the 1990s.[370] Although the details of each differ, Congress has created these entities to borrow now, at near-Treasury rates, guaranteeing the debt with future income streams and, in the case of REFCORP, with the Treasury guaranteeing the interest payments.[371]

The use of an FGC to fund or manage an activity that would be funded or managed by an ordinary federal agency but for budget

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365. *See supra* note 81 (defining "off budget").

366. For a description of the deficit reduction process, see COLLENDER, *supra* note 81, at 17-29. Passage of the Budget Enforcement Act of 1990, Pub. L. No. 101-508, tit. XIII, 104 Stat. 1388-1573, changed the focus of the deficit reduction process from borrowing to spending, although some borrowing caps remain in place. COLLENDER, *supra* note 81, at 19-38.

367. FICO's purpose is to fund the recapitalization of insolvent savings and loans without having the cost counted on-budget. *See* CBO STUDY, *supra* note 57, at 2. "FICO represents an extreme use of a government sponsored enterprise to provide an off-budget federal subsidy whose costs to taxpayers will be deferred for many years." STANTON, *supra* note 57, at 4. FICO was established August 28, 1987, by the FHLBank Board (an independent agency whose FICO-related functions were later assumed by a new independent agency, the Federal Housing Finance Board) pursuant to the Federal Savings and Loan Insurance Corporation Recapitalization Act of 1987, Pub. L. No. 100-86, 101 Stat. 585 (codified as amended at 12 U.S.C. § 1441 (1988 & Supp. V 1993)) (FHFB shall charter FICO "[n]otwithstanding any other provision of law"). FICO issues debt and nonvoting capital stock. Proceeds were formerly used to purchase FSLIC securities and are now placed in the FSLIC Resolution Fund, *id.* § 1441(c) (Supp. V 1993), in order to help close insolvent S&Ls. FICO is under the general direction of the FHFB. GAO STAFF STUDY, *supra* note 60, at 32.

FICO is less private and less independent than most GSEs. Although the GAO views FICO as a mixed-ownership government corporation, *see* GAO PROFILES, *supra* note 16, at 120, it is in fact a nonstock federally owned corporation, *see* 12 U.S.C. § 1441 (1988 & Supp. V 1993). FICO is run by a three-person board consisting of the Director of the Office of Finance of the Federal Housing Finance Board and two persons appointed by the Federal Housing Finance Board from among the presidents of the 12 FHLBanks (themselves mixed-ownership GSEs, *see supra* note 61). *Id.* § 1441(b) (1988 & Supp. V 1993).

368. FAC was created by the Agricultural Credit Act of 1987 in order to bail out the farm credit system (FCS). *See* CBO STUDY, *supra* note 57, at 2, 78-79. It is managed by the board of directors of the Federal Farm Credit Banks Funding Corporation, which is a private Farm Credit System institution. Unlike most other GSEs, its debts are backed by the full faith and credit of the United States. GAO STAFF STUDY, *supra* note 60, at 44. FAC is, technically, private. It appears, however, to be closely controlled by an agency, the Farm Credit System Financial Assistance Board. *See* CBO STUDY, *supra* note 57, at 79-80.

369. REFCORP was created in 1989 to assist in the refinancing of the savings and loan system. *See* CBO STUDY, *supra* note 57, at 208-09.

370. *See* William G. Gale, *The Budget Gimmick of the 1990s*, WALL ST. J., May 3, 1989, at A19 (referring to REFCORP, FAC & FICO).

371. 12 U.S.C. § 1441b (Supp. V 1993).

targets and/or political concerns about the size of the official budget deficit imposes both financial and moral costs.

1. Financial Costs

Because FGC debt is not backed by the full faith and credit of the United States, the FGC borrows at a rate higher than that available to the Treasury, although lower than the rate available to comparable private borrowers. As a result, the activity costs more to fund than it would have had the Treasury borrowed the money itself.[372] In the case of the $15 billion borrowed by FICO, for example, the differential has ranged between 50 and 110 basis points,[373] suggesting that had FICO (a relatively small GSE) been funded directly by the Treasury, the borrowing costs for its activities might have been reduced by as much as $165 million per year. Applying a similar differential to REFCORP, the cost to the taxpayers would be over $0.5 billion per year for every $50 billion borrowed. Despite complete government ownership, management consisting of high government officers serving ex officio as directors, and an explicit federal guarantee on its interest payments, REFCORP pays a premium to borrowers over comparable T-bill rates.[374] If the Treasury guarantees an FGC's debts, whether explicitly in the case of REFCORP and FAC,[375] or implicitly in the case of FICO, it might just as well borrow the money itself through the Treasury at the lowest rate. The accounting trick increases the program's costs in exchange for nothing more than (false) bragging rights about meeting budget targets.

In the case of REFCORP, the accounting problem is compounded by the way that the sham GSE uses the funds that it borrows. REFCORP's borrowings are transferred to the RTC, a "mixed-ownership" FGC that is actually wholly owned by the federal government, is on-budget, and is charged with recapitalizing insolvent savings and loans.[376] REFCORP receives a claim against future reve-

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372. The only valuable thing the taxpayer receives in exchange for this expenditure is the right to wait until the FGC fails before deciding whether to bail it out. This seems a very small benefit given the nature of the costs and the widespread belief that defaults are politically unacceptable.

373. *See* WHITE, *supra* note 320, at 145 n.32.

374. *See id.* at 184; William Keeling, *Hold-up in Nigerian Bank Debt Agreement*, FIN. TIMES, June 13, 1991, at 4 (noting Nigeria sought to substitute higher-yielding REFCORP debt for Treasuries as collateral in restructuring agreement). T-bills are more widely accepted and known than RTC bonds, but given the size of the REFCORP issue, it is hard to believe that the difference is great enough to justify the existence of a spread.

375. The complexities of FAC's funding and borrowing are outlined in GAO STAFF STUDY, *supra* note 60, at 45-46.

376. Notwithstanding the fact that "no Government funds may be invested in" the RTC, it is treated, for purposes of the GCCA, as a mixed-ownership government corporation that has capital from the government. 12 U.S.C. § 1441a(b)(2) (Supp. V 1993); *see also* 31 U.S.C. § 9101(2)(L) (Supp. V 1993) (defining RTC as mixed-ownership). For a summary of the RTC's

nues. The government treats the payment by REFCORP to the RTC as revenue, even though the money has been borrowed (at higher than Treasury rates) and the RTC is obligated to pay all of it back plus interest.[377] Thus, the two federal corporations together are used to understate the true federal debt twice—once when borrowing is ignored and again when it is treated as revenue.

Congressional opposition to the use of FGCs as an accounting sham to evade the budget targets provoked controversy over whether REFCORP debt should be on- or off-budget for Gramm-Rudman-Hollings purposes. The Bush administration wanted all $50 billion of the funds for the savings and loan "bailout"[378] to be off-budget finance in order to keep down the official budget deficit. A significant faction in Congress wanted it on-budget but would have exempted it from the Gramm-Rudman-Hollings ceiling. In a Solomonic but illogical compromise, Congress labeled $20 billion of REFCORP's debt on-budget borrowing and the additional $30 billion as off-budget.[379]

2. *Moral Costs*

The practice of hiding costs off-budget, in the hope that either voters will not notice or Congress can postpone actual appropriations until the bonds issued by the FGC become due, is dishonest and cyni-

activities, see Wayne M. Josel, *The Resolution Trust Corporation: Waste Management and the S&L Crisis*, 59 FORDHAM L. REV. S339 (1991) and David W. Adams, *Is the Power of the RTC Unlimited?: Federal Preemption of State Banking Law*, 18 FLA. ST. U. L. REV. 995 (1991).

377. *See* Lescher & Mace, *supra* note 24, at 533 (REFCORP payment to RTC treated as federal collection). The government arguably is not responsible for the RTC's debt to REFCORP or for REFCORP's debts to its lenders. Under FIRREA, however, the government is directly liable for interest payments on REFCORP debt that are not met by its income from the RTC's activities.

378. Lawrence White argues convincingly that the term *bailout* is highly misleading because almost all of the funds expended to rescue insolvent S&Ls are funds that the FSLIC was obligated to pay depositors in the event of the S&Ls' insolvency. *See* WHITE, *supra* note 320, at 160-64. The linchpin of this argument, however, is that the United States was responsible for the FSLIC's debts. No one seems to have seriously considered that the United States would have let the FSLIC fail, although the FSLIC was, before its demise in 1989, "a body corporate." 12 U.S.C. § 1725(c) (1988) (repealed 1989). This may reflect a legal judgment that because the FSLIC was also "an instrumentality of the United States," *id.*, the government remained liable for its debts despite FSLIC's separate legal personality. More likely, however, it represents an understandable political judgment that the insured depositors had legitimate expectations which the government had a moral obligation to honor, and an equally understandable economic judgment that failure to do so might trigger a liquidity crisis.

379. *See* Financial Institutions Reform, Recovery and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (codified as amended at 12 U.S.C. § 1441b (Supp. V 1993)); *see also* COLLENDER, *supra* note 81, at 12-13. The FGCs created to provide funds to troubled financial sectors, such as the S&Ls, have also imposed organizational costs on the government. They either started from scratch, leading to charges of confusion and mismanagement at least initially, *see, e.g.*, U.S. GEN. ACCOUNTING OFFICE, RESOLUTION TRUST CORPORATION: UNNECESSARY LOAN SERVICING COSTS DUE TO INADEQUATE CONTRACT OVERSIGHT (1991), or were cobbled together out of existing agencies and/or FGCs and suffer from complicated lines of authority.

cal.[380] It both poisons the political process and reflects a poison already present within it. By hiding the true cost of public decisions nothing valuable is gained, and indeed, we probably lose a lot. If spending and deficit reduction targets are valuable then they should not be undermined by subterfuge; if the targets are unrealistic, it does not follow that FGCs promote the best use of the extra funding. In either case, the GSEs are used to accomplish by subterfuge something that politicians dare not do directly.

The only argument in favor of using FGCs to hide the true cost of federal programs is that necessary programs that otherwise would not survive the deficit reduction process are made financially possible. Even if this dubious argument is valid, the financial costs of this subterfuge are high.

III. Reform

FGCs as a class are less accountable than any other type of domestic civilian federal government entity. Constitutional, statutory, and regulatory controls are unclear, weak, or nonexistent. Both presidential and congressional control are stunted, except in the case of wholly owned FGCs. Courts are uncertain whether to treat FGCs as public or private. FGCs also cause both macro- and microfinancial problems. The three largest macro effects, each of which affects the federal budget, are:

(1) the contingent risk imposed by the implicit guarantee;

(2) the additional cost (borne either by the Treasury or by the beneficiaries) of borrowing for a public purpose at a premium over Treasury rates; and

(3) the misuse of certain GSEs to hide the budget deficit.

The most critical microeconomic problems are:

(1) the lack of incentives for FGCs to be efficient;

(2) the danger that shareholders, management and/or debt-holders are collecting rents at the public's expense; and

(3) the effects that FGCs have on existing and would-be private competitors.

The trillions of dollars borrowed, lent, and insured by the GSEs are a source of special concern because the sums involved are so large. First, although GSEs benefit from an implicit guarantee, they nonetheless borrow at slightly over Treasury rates, imposing an extra, and arguably unnecessary, cost on their activities. Second, investors' understandable reliance upon the implicit guarantee suggests that the Treasury would face intense pressure to rescue a GSE were one to

380. *See* Guido Calabresi, Ideas, Beliefs, Attitudes and the Law (1985) (discussing costs of dishonesty in public life).

become insolvent. Taxpayers face the contingent risk that, in the event of a major management blunder, the government may be called upon to make good on debts it played no part in incurring and from which taxpayers may have derived little if any benefit. The implicit guarantee also arguably creates a moral hazard for GSE management once capital levels fall. Third, private shareholders or management may be appropriating profits that could go to the beneficiaries of the FGC, or that—had the corporation been designed more carefully—could go to the taxpayer. Fourth, GSEs have advantages denied to private competitors (although they also face some special restrictions).

A. *Limited Aims of Recent Reforms*

From time to time Congress worries about FGCs, but it consistently focuses only on the first of the six problems identified above. Rather than confront the accountability problems common to all FGCs, in 1992 Congress focused on the contingent risk that some GSEs pose to the Treasury and imposed capital requirements as a device to head off insolvency.[381] This reform has reduced the already small risk of a problem that, had it occurred, would have been very expensive to cure. Much remains to be done.

The major recent reform is the Federal Housing Enterprises Financial Safety and Soundness Act of 1992,[382] which unified and slightly tightened the capital adequacy requirements for Fannie Mae, Freddie Mac, and the Federal Home Loan Banks.[383] The new regulator, the Office of Federal Housing Enterprise Oversight, is located in the Department of Housing and Urban Development. It monitors capital levels according to risk criteria spelled out by Congress.[384] The criteria are not particularly onerous, and Freddie Mac and Fannie

381. To be fair, Congress also took a small nibble at the fifth problem identified above when it added to Fannie Mae and Freddie Mac's statutory duties to support lower income housing, 12 U.S.C. §§ 4561-89 (Supp. V 1993), and allowed the Office of Federal Housing Enterprise Oversight to prohibit excessive compensation for directors and staff of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. *Id.* § 4518.

382. Pub. L. No. 102-550, § 1301, 106 Stat. 3672, 3941 (codified at 12 U.S.C. § 4501 (Supp. V 1993)).

383. *See* 12 U.S.C. § 4503 (Supp. V 1993). Congress also has imposed a capital adequacy requirement on Sallie Mae, although it was highly prosperous. *See* 20 U.S.C. § 1087-2(r)(4) (Supp. V 1993).

A rejected proposal, S. 1621, 102d Cong., 1st Sess. (1991), would have created a super-regulator for Fannie Mae, Freddie Mac, Sallie Mae, the FHL Banks, Farmer Mac, the Farm Credit Banks, the Banks for Cooperatives, and the Farm Credit System Insurance Corporation. The GAO endorsed creating a super-regulator for a similar list of GSEs. GAO justified its exclusion of Connie Lee based on its being subject to state insurance regulation and to private market discipline. *See* GAO FRAMEWORK, *supra* note 187, at 17.

384. *See* 12 U.S.C. § 4611-14 (Supp. V 1993).

Mae easily have passed review every quarter to date,[385] although the regulator found the Federal Home Loan Bank System "basically" safe and sound.[386] If one of these GSEs had failed its capital adequacy tests, it would have been required to submit a capital restoration plan; if found "significantly" undercapitalized, a conservator might be appointed to take over the management of the enterprise.[387]

Capital adequacy rules have some virtues because they can function as a type of early warning device. Because Congress is not known for its rapid reaction time, having a mechanism in place that rings an alarm well before a GSE is in danger of needing an expensive bailout is useful. Capital adequacy rules also are attractive because the rules are easily patterned after existing bank regulation.[388] Specifying dire consequences if a GSE falls below a minimum capital ratio intentionally creates an incentive for management to avoid taking too much risk.[389] A capital floor also protects against a GSE that may feel tempted to engage in increasingly risky behavior as insolvency looms, because the capital floor is reached while the GSE still has something to lose.

Capital floors also have costs. The higher the floor, the less a GSE is able to leverage its funds, which raises its costs. Establishing the capital floor level is thus the critical issue. If it is too low, then by the time the alarm is triggered it will be too late for Congress or regulators to react. If it is too high, it imposes a needless cost on the GSE, thereby reducing the benefits that can flow to its public purpose without achieving any corresponding gain.[390] Although GSEs currently operate with low capital ratios, nothing indicates that these ratios are inadequate;[391] the fear is that a GSE might, through management failure, lose a great deal of money either suddenly or quietly, and Congress would not react until it was too late. Because GSEs are very profitable—despite being in the home and agricultural mortgage business during a recession—and use their profitability to build up

385. *See, e.g.*, *Mortgage Developments*, Banking Rep. (BNA) No. 25, at 1190 (June 19, 1995), *available in* LEXIS, Banking Library, Bnabnk File (summarizing office of Federal Housing Enterprise Oversight second Annual Report to Congress); *OFHEO Says Freddie Mac, Fannie Mae Met First-quarter Capital Standards*, Banking Rep. (BNA) No. 62, at 1070 (June 20, 1994).

386. Nicolas P. Retsinas, *HUD's Report on FHLB System*, NAT'L MORTGAGE NEWS, June 20, 1994, at 4.

387. 12 U.S.C. § 4616 (Supp. V 1993). For a lucid discussion of the conservator's powers and duties see Carrie S. Lavargna, *Government-Sponsored Enterprises Are "Too Big to Fail": Balancing Public and Private Interests*, 44 HASTINGS L.J. 992, 1016 (1993).

388. *See, e.g.*, Stanton, *supra* note 213.

389. *See* GAO FRAMEWORK, *supra* note 187, at 9.

390. The GSEs have argued that Congress, not an agency, should set any capital adequacy standards applied to them and that standards should be based on stress tests which seek to model the GSEs' ability to weather a financial crisis rather than on traditional ratios.

391. Most parties to the debate over capital adequacy rules appear to agree that the GSEs are currently healthy and likely to remain so for the foreseeable future. *See supra* note 26.

their capital levels, one might ask why capital adequacy is Congress's top reform priority. The answer, of course, is that having just "bailed out" the S&Ls, Congress was understandably anxious to avoid further bailouts of any kind. And because the S&L model provided the impetus for the change in the regulation of GSEs, the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 borrows liberally from the regulatory scheme used to reorganize insolvent banks.[392]

B. Proposals Rejected by Congress

As part of the omnibus legislation designed to reform the financial industry, Congress instructed the Treasury and other agencies to consider the risks posed by the GSEs and to make proposals for controlling those risks. The resulting proposals included a variety of ingenious "early warning mechanisms," other than capital requirements, all designed to signal Congress that a particular GSE is in financial trouble. Congress rejected this proposal. Other suggestions rejected by Congress included complete privatization, so that markets no longer perceive an implicit guarantee, and replacing the GSEs with ordinary agencies.

1. Warning Mechanisms

Private markets (ideally) price the bonds and shares of ordinary corporations on the basis of all the available information. The market price thus reflects the market's collective conclusion as to the firm's prospects. These prices are arguably the best available barometer of a corporation's prospects. This pricing method, however, does not apply to GSEs because the markets rely on an implicit federal guarantee and therefore pay little, if any, attention to a GSE's actual financial condition.

Early warning mechanisms rely on market-oriented techniques to monitor the GSE's financial prospects. An early warning mechanism either gives Congress the long lead time needed to craft a legislative response, or it carries an automatic, administrative response such as firing the management and bringing in a conservator.

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392. *See* Lavargna, *supra* note 387, at 1016. As the Act does not go into great detail about what a hypothetical conservator should do (perhaps relying on the *in terrorem* effect of the possibility), Lavargna offers to fill the gap by proposing a "best interests of the enterprise" standard. *Id.* at 1035. This suggestion, however, fails to give sufficient weight to Congress's mandate that the conservator act to rebuild the enterprise's capital as a first priority. To the extent that this prime obligation gives the conservator any leeway, surely the best standard in light of the GSE's public purposes would be the "best interests of the public," and particularly the groups whom the enterprise is designed to serve rather than the interests of the enterprise.

a. Ratings

One proposal is to pay rating agencies, such as Standard & Poor's (who are presumably experts at assessing financial risk) to issue regular credit ratings of the GSEs based on the assumption that no federal rescue is available.[393] Unfortunately, evidence suggests that credit ratings of debt issued by private firms are a lagging indicator of the financial health of those corporations.[394]

b. Risky Subordinated Debt

A more ingenious solution, also considered by the Congressional Budget Office (CBO), would require GSEs to issue risky subordinated debt. The function of these securities is akin to a canary in a coal mine: if the debt is subordinated, and hedged with strict loan covenants that make it clear that investors will not be repaid if the GSE's income or other measures of financial soundness fall below a fixed point, then holders of this debt will have an incentive to pay close attention to the GSE's financial health. If the price of the risky debt on the secondary market falls, Congress will have a reliable indication that investors are concerned about the GSE's balance sheet.[395] Although this appears to be the simplest solution to administer, each GSE would have to issue a substantial amount of subordinated debt to make the secondary market large enough, and liquid enough, to make the scheme work.[396] An additional complication is that even the most sensitive canary only provides effective protection in a coal mine if someone who is capable of prompt and effective action is there to hear it. Whether Congress is such a body is open to question. Combining risky subordinated debt with automatic and draconian consequences if the debt falls below a certain value (perhaps computed relative to a market index) creates a powerful and self-executing incentive for GSEs to avoid excessive risk. Overly draconian consequences, or standards that are too high, might create excessively cautious behavior, diluting the effectiveness of the GSE.

393. CBO STUDY, *supra* note 57, at 50-55.

394. *Id.* at 54 (citing Mark I. Weinstein, *The Effect of a Rating Change Announcement on Bond Price*, 5 J. FIN. ECON. 329 (1977)).

395. *See id.* at 55-56. An alternate scheme would require the GSEs to issue puttable subordinated debt with loan covenants specifying it would be worthless if the GSE's capital fell below a certain standard. *Id.* at 56-57. Investors could redeem their investment at any time and would have an incentive to exercise their put options if they thought the GSE was in trouble. *Id.* at 57.

396. CBO also warned that the IRS might treat the interest payments on the debt as equivalent to dividends on preferred stock, increasing the return investors would require to be induced to hold the securities. *Id.* at 56.

2. *Privatization*

Privatization means more than selling off the government's shares. The federal government already requires GSEs to retire or purchase the government's shares, but this has failed to persuade the markets—or even the government itself—that there is no implicit guarantee. Full privatization would require a credible commitment to allow GSEs to fail. GSEs therefore would lose the feature that currently makes their securities most attractive to investors. In exchange, however, the GSEs could be granted new charters, allowing them to diversify beyond the very narrow businesses to which they are currently restricted.

Nevertheless, new charters might fail to communicate a credible commitment to allowing a large GSE to fail. Congress has previously shown a willingness to help out major private corporations, such as Lockheed and Chrysler, and it is doubtful whether it would let the dominant player in a sensitive credit market collapse. What Congressman is going to put a quarter of the nation's home mortgages at risk? The creation and continued existence of a GSE is itself a testament to the political importance of the constituency that it serves. Formal privatization alone is unlikely to change this basic political reality unless some action is taken to break up the GSE as well as privatize it.

3. *Converting FGCs to Agencies*

If convincing privatization is impossible, the next-best solution may be to give up and turn GSEs into ordinary agencies, like most wholly owned FGCs are already. Conversion to ordinary agencies would have pedestrian, but valuable, advantages. Most important, agency status GSEs would borrow at the Treasury rate, thus eliminating the current premium paid to investors to induce them to hold GSE debt instead of Treasury securities. All other things being equal, the GSE could carry out its current activities at lower cost. GSE activities also would have "on-budget" status, eliminating the opportunity for deficit politics. In addition, conversion to agency status would provide a clear, if not necessarily ideal, answer to whether GSEs are public or private. Agency status presumably would subject GSEs to the APA, FOIA, and other federal statutes and rules designed to provide fair and accountable government.

The disadvantages of this proposal may outweigh its benefits. Turning GSEs into agencies amounts to a confession of failure—an admission that the hoped-for efficiencies of the private sector cannot be imported into a public setting. Indeed, to the extent that GSEs already take advantage of their freedom from one-year budget cycles, personnel ceilings, and salary caps, and have realized management efficiencies, conversion to ordinary agency status risks losing these advantages. Finally, the repurchase or confiscation of privately held shares would impose a significant one-time cost: about $3 billion in the case of Fannie Mae alone.[397] To the extent that some GSE holders have vested rights in the continuation of the charter, they might conceivably have a takings claim above the current market value of their shares.[398]

C. *Some Moderate Proposals*

The regulatory proposals Congress has considered in recent years have been narrowly focused on heading off the hypothetical insolvency of the GSEs and thus have ignored most of the important issues that relate to both GSEs and FGCs in general. There is some reason to doubt the urgency of the problem Congress is trying to solve. Although a GSE default is conceivable, it would require serious management failure. Congress's focus on capital adequacy results from its failure to anticipate the S&L crisis—a textbook case of once bitten twice shy. In fact, other than the three sham entities created to provide off-budget finance,[399] the GSEs appear to be healthy.[400]

Rather than being in danger of failing, strong evidence suggests that GSEs are too successful. The GSE's enormous profits in the midst of a nationwide property and agriculture recession suggests that they are being too cautious and may therefore be concentrating on profits at the expense of their public purposes. Alternately, those same profits may be a sign that the GSEs' special advantages are allowing their private shareholders to reap a nearly riskless profit, in which case the public incurs an opportunity cost and private competitors face being crowded out.

The grab bag of proposals that follow does not purport to be a perfect solution to each or all of the problems discussed in this article, but it may provide a starting point for a more comprehensive solution

397. *See id.* at 169 (value of stockholders' equity).

398. An arguable claim might be mounted on the theory that the investor believed that the shares would appreciate at a rate greater than that offered by alternate investments. The investor would either have to argue that she thought markets were not efficient, or that her preferences were somehow peculiarly served by investment in a GSE and that no perfect substitute existed.

399. *See supra* note 370 and accompanying text (discussion of REFCORP, FAC, FICO).

400. *See* CBO STUDY, *supra* note 57, at 62-64; GAO GSE STUDY, *supra* note 76, at 6-9. The least sound GSE is the Farm Credit System. *See supra* note 280. Stress tests performed by the (nonsham) GSEs themselves suggest that they could survive an economic shock as severe as the Great Depression. *See* CBO STUDY, *supra* note 57, at 162-64, 168-73 (summarizing results). Although these tests are now accepted as valid in principle by the CBO, the GAO, and the Treasury, the assumptions on which they are based have been questioned. *See* Martin Mayer, *Another Favor for Fannie Mae and Freddie Mac*, WALL ST. J. EUR., Oct. 23, 1991, at 10 (alleging that stress tests assume that GSEs would stop lending in a depression); *see also* CBO STUDY, *supra* note 57, at 162-63 (least severe stress tests assume lending during economic crisis will level off to steady-state rather than continuing to grow).

to both the legal and financial problems posed by the proliferation of FGCs.

1. *Accountability*

The biggest single problem with FGCs today is not their finances but the lack of accountability when they use their powers.

a. Internal Governance

Clearer rules are needed regarding the appointment and duties of both public and private directors. To avoid doubt, Congress should declare that any person appointed with the Senate's advice and consent is an officer of the United States. These officials should take an oath of office, should be subject to impeachment, and should serve at the pleasure of the President unless the statute creating the office explicitly limits the President's removal power.[401] The statutes creating individual FGCs should set out the duties of public directors. The GCCA also should contain a general statement outlining the extent to which public directors are expected to represent national interests and their duties toward Congress and the President. To increase the odds that FGCs are influenced by the political process rather than the other way around, FGCs should be forbidden from making political contributions or giving money to political action committees.

At present no general rules define who should vote the government's shares in mixed-ownership FGCs. A clear rule should be devised to ensure that the ambiguity does not silence the government's voice. The existence of such a rule may be more important than its content.[402]

In addition, no clear rules currently define private shareholders' rights. Here, however, the need for reform may be less pressing, as private investors seem perfectly willing to purchase shares in FGCs under the current regime. In addition, presumably the courts are capable of making federal common law to fill in whatever gaps exist due

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401. In addition, none of the FGCs' officers should be legislators. The body is undoubtedly unconstitutional if they are. *See* Metropolitan Washington Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc., 501 U.S. 252, 267 (1991). The Smithsonian, which has a Board of Regents composed of Chief Justice of the United States and the Vice President (who serve ex officio) plus three Senators appointed by the President of the Senate, three members of Congress appointed by the Speaker of the House, and nine persons appointed by joint resolution of Congress, is thus illegally constituted, although whether anyone has standing to say so is open to doubt. *Cf.* Springer v. Philippine Islands, 277 U.S. 189, 211 (1928) ("Parallel to the case before us, Congress long ago established the Smithsonian Institution, to question which would be to lay hands on the Ark of the Covenant . . . .") (Holmes & Brandeis, JJ., dissenting).

402. Because the mixed-ownership FGCs in existence today are either wholly owned by the government or privately owned with a minority of statutory public directors, the absence of such a rule has no immediate consequences.

to the absence of a federal equivalent to most state corporate law. The legislative effort involved in agreeing to a complete federal corporate code may be more trouble than it is worth.

b. Accounting for Federal Powers and Benefits

The more that an FGC has federal powers or benefits not available to an ordinary corporation, the greater the need for the corporation to account for its use of those powers or resources. The GAO and the corporations themselves should estimate the cash and present values of the federal benefits made available to the corporation. The GAO, or some other agency, also should estimate the opportunity costs to the government of providing those benefits rather than selling them on the open market. In addition, each FGC should report to Congress on the performance of its public mission. Although annual reports do little by themselves, they provide a convenient excuse for Congress to hold hearings to monitor the FGC's performance; in turn, the threat of hearings gives FGCs reason to believe they have to account for their actions.[403]

c. Enforcing Public Goals

Private control of FGCs and competitive pressures are likely to produce efficiency gains. As the experience of the GSEs demonstrates, the price of private control is a loss of interest in providing benefits, especially pecuniary benefits, to persons other than shareholders and creditors. Thus, if FGCs are to provide such benefits, either regulations or incentive/penalty structures must force them to do so. Whatever the extent of government's ownership—even zero—any FGC that enjoys public powers or benefits (and especially those enjoying an implicit guarantee) should pay for them, either in cash payments to the Treasury or in kind, by providing benefits to the target group the FGC is designed to serve. FGCs that pay in kind should be forced to provide benefits, such as lower mortgage interest rates, to a (hopefully deserving) client group *other than the owners*. Regulation alone is probably not the best solution: most FGCs exist because Congress determined that a program required a federal instrument with more flexibility than the average agency.

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403. If FGCs are not going to be forced to operate in an environment that forces them to deliver benefits to target groups, then the FGCs should be required to pay for the advantages they receive—if the taxpayer provides a benefit, then the taxpayer should get a share in the profits.

i. Regulation

Regulation is a blunt and familiar tool. HUD has been asserting or seeking regulatory authority over Fannie Mae for many years but has failed to impose rules requiring Fannie Mae to devote more of its resources to lower and middle income family housing. The same is true in varying degrees for all other profitable GSEs except for Sallie Mae, which currently has no regulator.[404] Although not necessarily wise, it would not be difficult to write rules requiring profitable FGCs to devote a portion of their resources to specific activities even though they did not necessarily maximize profit. Ordinary administrative sanctions, i.e., fines and other penalties, would back up these rules.

ii. Incentives

A less tried, but probably more fruitful, avenue is to create incentive/penalty structures designed to mold FGC conduct. For example, Congress could limit Fannie Mae's loans to wealthier households by requiring proportional lending based on loans to lower- and middle-income families. Because larger loans tend to be more profitable, once the two are tied together, profits will motivate Fannie Mae to increase the less profitable line of activity. Unlike some regulatory solutions, such a ratio does not require Fannie Mae to make unprofitable loans unless it is certain that these losses are outweighed by the gains on the other more profitable business. Alternatively, targets could be set and then enforced by restricting management pay increases, or levying a surtax on dividends, if the targets are not met.

One danger that must be avoided is self-dealing. Congress should not create FGCs controlled by the groups they are intended to benefit. The classic bad example is the Farm Credit System, which is cooperatively owned by its borrowers. In the past the Farm Credit System allowed lax loan standards to farmers, which resulted in the insolvency of the FCS system in the mid-1980s.[405]

2. *Financial Issues*

The most effective cure for all the FGC-associated financial problems is to increase FGCs' exposure to market discipline. Achieving this end without sacrificing the purposes for which FGCs are created is surprisingly difficult.

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404. Minimal capital adequacy regulation was introduced by the Student Reform Act of 1993, codified at 20 U.S.C. § 1087-2(r) (Supp. V 1993).

405. *See* 1991 U.S. BUDGET, *supra* note 220, at 240.

a. Creating Market Discipline

Market discipline has several forms including the existence of (or possible entry into the market by) other entities providing similar goods or services, procurement from competitive suppliers, lack of favored access to labor and capital, absence of rents or monopoly profits, and the threat of takeover if management underperforms. FGCs that operate in potentially competitive markets benefit from factors that radically reduce the degree of potential competition. For example, the implicit guarantee gives access to credit at rates below those available to private competitors and allows a much higher degree of leverage than markets would likely permit a private firm.[406] And, dominance of a particular market may create an economy of scale.

Each of these benefits is double-edged. Every benefit that allows the FGC to deliver a product at lower cost simultaneously allows it to benefit the group it is designed to serve and to undercut any private competitor. (A third possibility is that the price advantage can become a rent that is shared between management, shareholders, and perhaps debt-holders.) At least at the microeconomic level, it is probably impossible to remove or restructure the FGCs' benefits in a manner that levels the playing field with private firms without removing the very qualities that allow FGCs to provide subsidized goods and services. Take away an FGC's implicit guarantee and you take away its access to cheap credit and its ability to leverage itself far beyond what would be permitted for an ordinary firm. The removal of the implicit guarantee levels the playing field, but does so at the expense of the "subsidy" that the FGC is designed to deliver.[407]

The only way to impose stiff competitive pressures on FGCs short of replacing them with private firms is to create several FGCs with identical powers and missions and have them compete with each other. Fannie Mae and Freddie Mac are already competitors (or oligopolists), and neither appears to have been damaged by it. Creating a larger number of equally situated competitors might erode economies of scale, but it would also erode both the rents and the market share held by existing GSEs. In time, competition also should reduce the size of large GSEs to a point where they are no longer too big to fail. A more radical option would be to break up the largest GSEs, analogous to the break-up of the Bell system. Giving the existing

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406. Currently GSEs enjoy special exemptions from certain federal securities laws. The Bush administration proposed removing these exemptions. 1992 JOINT REPORT, *supra* note 58, at 34.

407. It may well be that the nation as a whole would be better off if there were no subsidy at all; that, however, is an argument for the abolition of all FGCs. This article is concerned with the more modest question of how the policy choice reflected in the creation of FGCs can best be administered.

shareholders shares in each of the new firms created by the break-up would remove possible takings problems.

Competition provides the greatest discipline when firms are at risk of failure, although the profit motive should provide considerable incentive for efficiency even in the absence of this danger. Currently, FGCs with an implicit guarantee face little if any risk of failure. Increasing competition and shrinking market share might increase the risk that the Treasury would have to make good an FGC's losses; the potential expense is a powerful objection to a policy designed to increase the risk of FGC failure. Thus, if the implicit guarantee is retained for FGC's financial advantages, those FGCs whose competitors are created for them must be required to adopt an "early warning" debt scheme to signal the approach of a financial problem.[408]

b. Division of the Spoils

Recently, private and mixed-ownership FGCs have proved highly profitable for their owners,[409] their debt-holders, and their directors and employees. Neither the shareholders nor the debt-holders have profited unfairly; with the exception of shareholders of GSEs like Freddie Mac whose stock was not available on the open market,[410] shareholders, in say Fannie Mae, have just been shrewd. Similarly, purchasers of Fannie Mae bonds can demand a small premium over Treasury bills because the federal guarantee is, after all, only implicit. Nevertheless, to the extent that an FGC is created for a public purpose and that the engine of an FGC's profitability, e.g., increased leverage on borrowed funds, is fueled by its government connection, the Treasury (or the intended beneficiaries) should be entitled to a share of the profits.

Dividends on the government's shares are one means of allowing taxpayers to share in the profits, but this approach has a number of problems. It does not apply to corporations in which the government owns no shares.[411] It also works poorly if FGCs choose to retain earnings rather than pay dividends. Ordinary investors can buy and sell their shares at will; but, as the ultimate insider, the government is not in a good position to play the market, if only because government trades risk sending undesirable signals to other investors. If the government sells, for example, the market may decide that the govern-

408. *See supra* part III.B.1.

409. One exception is Sallie Mae, whose stock has languished since the federal government changed the terms by which Sallie Mae administers guaranteed student loans.

410. *See supra* note 290.

411. Often the government owns no shares because it has sold them. The FGCs and their current owners can hardly be blamed for this quite likely mistaken policy decision unless it could be shown that they made campaign contributions to sponsors of privatization.

ment believes that the market has peaked. This might cause other investors to follow suit and might even cause a small panic. Because the government cannot realize its gains easily, the government might be better off holding shares only in start-up FGCs and requiring the FGCs to repurchase these shares according to a fixed schedule. If the government continues to provide benefits other than start-up capital but is unable to ensure that the benefits pass to the target group, then the fiction that the FGC exists for a public purpose is not worth pursuing. In such cases the FGC either should be fully privatized or the government should charge for the benefit according to its best estimate of the market price.

3. *Legal Status*

The GCCA[412] vision of FGCs as being either private, mixed-ownership, or (one presumes) an agency is simplistic. It has been undermined in two ways. First, from time to time Congress creates FGCs with a formal status at odds with their reality. Calling entities such as REFCORP and RTC "mixed-ownership" when, in fact, no private ownership or control exists, distorts the GCCA categories beyond recognition. Second, the sheer diversity of existing FGCs makes it unhelpful to force them into such unilluminating categories. The GCCA's concentration on audit and budget is too modest. The time has come to update the GCCA and to give it some teeth.

With respect to auditing and classifying, the GCCA's focus should move away from congressional labels, e.g., public, mixed-ownership, private. Instead, the GCCA should adopt a far more contextual approach, taking into account several factors, including the locus of control, the FGC's profit-making status, and the extent to which the FGC benefits from special advantages unavailable to its private competitors. The classification of FGCs as either public or private is particularly important because it determines the type and availability of redress to persons who believe that they have been wronged by an FGC.

a. Actual Control

The degree of actual federal control should determine how FGCs are classified, not the label Congress has given them. Indeed, when creating FGCs Congress should acknowledge that any FGC controlled by the government is an agency for constitutional purposes. In principle, any FGC owned or controlled by the government should be sub-

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412. *See supra* notes 308, 311 and accompanying text.

ject to most of the rules applicable to other agencies; in particular, FGCs should be subject to the Freedom of Information Act. If a compelling reason exists to exempt a government owned or controlled FGC from portions of, say, the Administrative Procedure Act or the FTCA, the exemption should have a "sunset" provision limiting its duration, at the end of which the entity would either become an ordinary agency or become private, or at least mixed-ownership.

The term *mixed-ownership* should be restricted to corporations in which the government holds a noncontrolling minority interest. Despite this government interest, these corporations should ordinarily be treated as private for constitutional and commercial purposes because they are not bodies whose actions display "a sufficiently close nexus" to the government to "be fairly treated as [the actions] of the government itself."

b. Profit or Nonprofit

The GCCA fails to distinguish between nonprofit and for-profit FGCs. The type of rules appropriate for the internal governance, accounting, and external supervision of an FGC should be based on whether it primarily provides nonpecuniary and external benefits, or whether it produces significant profits for shareholders. A nonprofit FGC may not wish to be self-sustaining, but a for-profit FGC aims, ideally, to return capital plus a profit. In the case of for-profit private and mixed-ownership FGCs, Congress should clearly specify the circumstances under which the bankruptcy code applies, thus possibly lessening the effects of the implicit guarantee. Although all FGCs benefit from monitoring to ensure that they fulfill their public purposes, the potential for conflicts of interest are probably greater for for-profit FGCs if only because directors' and shareholders' renumeration criteria are imperfectly aligned with the corporation's public mission. The GCCA should reflect this reality, rather than imposing the least-strict reporting requirements on private FGCs.

c. Sovereign Immunity and Private Interests

The legal status of FGCs is not simply an arcane issue of separation of powers but has important day-to-day consequences for private citizens. Persons who contract with FGCs are entitled to two sorts of protection which are currently absent. First, they are entitled to know whether the entity with which they are dealing is a public body or a private corporation because this characterization affects their rights and remedies, and thus their legitimate expectations. If Congress and the courts apply the tests set out above, then such persons would have greater guidance than is currently available.[413]

An FGC with sufficient independence to avoid being a federal actor does not deserve sovereign immunity and should not benefit from the *Merrill* doctrine. Courts should apply the same test for sovereign immunity as they do for federal actors. Only FGCs that are federal actors should have sovereign immunity. If courts are not willing to adopt this identity then Congress will need to amend the definition section of the FTCA[414] to make it clear that the sovereign immunity of all FGCs that might be considered public is waived to the same extent as that of federal agencies.

IV. Summary and Conclusion

Federal government corporations are not evil per se; nor are they a panacea for inefficiency in government. Because they do not fit in with superficial, but commonly held, views of what government departments are like, the risks they pose too often are ignored. The obscurity in which federal government corporations operate allows them to have the best of both worlds and to avoid both the accountability mechanisms designed to reign in government and the laws and rules that regulate private firms. Congress has failed to come to grips with these issues.

Before Congress and the administration create more federal government corporations—whether to regulate boxing, modernize air traffic control, jump-start small business, or anything else[415]—they would be wise to reconsider (dare one say reinvent?) the fundamental rules governing this potentially useful, but also potentially dangerous, administrative device. Perhaps some day a future administration, desperate to achieve further improvements in government operations, will embark on a program of radical privatization. If so, that administration is likely to transfer some functions to federal corporations, either as a political compromise, or as a way station to full privatization.

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413. Admittedly, there is a risk of complexity when an FGC changes over time. The risk is at its maximum in the (hypothetical) case of a mixed-ownership FGC with dispersed share ownership. In such a case, the FGC might be private for some matters and public for others. Were Congress to create such a beast, it would be wise to provide a default rule—preferably "public" status.

414. 28 U.S.C. § 2671 (1988 & Supp. V 1993).

415. The Bonneville Power Administration is a recent aspirant to accountability-free status. It began a campaign to become a federal corporation, estimating that it could save several million dollars in staff costs alone. Its proposal is a little more brazen than usual as its draft legislation would exempt it from all civil service laws, including whistle-blower protection and conflict-of-interest laws, and insulate it from everything from jury trials to the Freedom of Information Act. *See* Marla Williams, *Bonneville Power Wants to Be on Its Own—Agency Says It Would Save Money, but Critics Wary of Its Autonomy*, SEATTLE TIMES, Feb. 8, 1994, at B3.

The ground rules for such corporations need to be sorted out well before that day comes.

Already, FGCs raise serious concerns about the placement of public power in private hands. Relatively modest reforms, however, can handle the problems. The United States has a long tradition of entrusting decisions of national importance to the market—to private persons and to private corporations—decisions that in other nations, such as France or Japan, are guided by the state.[416] The problem has less to do with the choice of a corporate form than the way in which that choice is implemented.

Most of the primary legal and financial problems with FGCs today could be solved by taking these basic steps:

(1) The legal status of many FGCs needs clarification along the lines described in this article. Identifying a corporation as either public or private instead of letting many get away with being a bit of each will force compliance with either the APA or private (and, usually, tax) law relating to firms. Either way, FGC accountability will increase. Other issues also need to be defined, particularly the position of the public director in the private firm.

(2) The public is entitled to reap its fair share of the profits when FGCs benefit from public powers, public funds, or an implicit debt guarantee. If an FGC makes profits it should pay taxes and, if the government owns shares, it should pay out dividends on those shares. If the government does not own shares, the FGC generally should pay for its privileges.[417]

(3) For-profit FGCs must have similarly situated competitors, be reincorporated as nonprofit, or, if possible, terminated and restarted as government-owned corporations so that any monopoly profits pass to the Treasury. Government chartered copycat, publicly owned, competitors would provide the best solution in some cases.

Reinventing Government involves at least as much fine-tuning of rules as reinvention.[418] Given the government's importance to the nation's economic and social well-being, a little tune-up goes a long way. This article proposes preventive maintenance reforms designed to shape the environment in which federal government corporations operate. These suggestions harmonize with *Reinventing Government*'s emphasis on increasing government accountability, although they do not achieve it in precisely the same way. Alas, the odds of adopting

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416. *See* ANDREW SCHONFIELD, MODERN CAPITALISM: THE CHANGING BALANCE OF PUBLIC AND PRIVATE POWER 298-301 (1965).

417. For an example of how this might work in practice, see 20 U.S.C. § 1087-2(n)(7) (1988 & Supp. V 1993) (charging Sallie Mae an "offset fee" of 0.3% per year for loans that it makes, insures or guarantees subsequent to August 10, 1993).

418. *See, e.g.*, Jeffrey S. Lubbers, *Better Regulations: The National Performance Review's Regulatory Reform Recommendations*, 43 DUKE L.J. 1165 (1994).

these reforms before they are needed is slim, because regulatory reform most often happens only in reaction to a perceived crisis. Changing that dynamic, to anticipate the problems outlined above instead of reacting to them after it is too late, would signal a truly reinvented government.