Testimony
Of
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Since the last time I had a chance to address this committee in 2006 much has changed in the financial world. Mortgage loans have defaulted by the billions, home prices have dropped, investment banks have gone bust, liquid securities have become illiquid, bond insurers have lost their ratings, bonds have been downgraded, banks have been required to raise billions in new capital to support their balance sheets and Congress has decided to back Fannie Mae.

None of this has helped government address its problems in the key mission of building and maintaining infrastructure.

While the world has spun out of control and billions have been spent or lost no one has seen fit to solve the infrastructure problem

The proponents of P3 are still playing the same tune that they can deliver more value through private ownership than a public solution.

As was proven by North Texas Tollway Authority's bid for SH 121, a public sector infrastructure provider can always deliver more value than a private sector provider since its costs of funds are at least 30% less. This advantage has not waned with the financial chaos in the market place, if anything it has increased.

Recent Activity Proves the Public Advantage

The recent bidding for the proposed 75 year lease of the Pennsylvania Turnpike, the granddaddy of all toll roads, has once again proven the point. Although highly touted as having a potential value of as much as $20 Billion, the actual bidding topped out at a nominal $12.8 Billion. This number is even overstated since the State agreed to absorb the cost of police patrols which are currently paid for by the Turnpike Commission. This lower bid price reflected the higher costs of capital now demanded in the credit markets. The so called Weighted Average Cost of Capital for this price was between 9-9.50%, an increase of nearly 300 basis points over the Weighted Average Cost of Capital underlying the SH121 bid of Cintra in 2006. The primary mover in pushing up this cost of money was the demand of debt providers to limit their loans to only 60% of acquisition cost versus the 80% loans being advanced pre 2007. As a point of interest the Cintra bid for the Pennsylvania Turnpike came in 3rd , while the group led by Goldman Sachs, one of P3's biggest activists, came in second hundreds of millions of dollars behind the winner, Abertis and Citigroup.

A comparable transaction if proffered by the Public Sector would have a cost of funds between 5-6% in today's market and would deliver a value of at least $16 billion.

The case for public versus private finaincnig of infrastructure has now been made in a real world environment twice, yet the advocates of P3 continue to assert the private option is better.

They now even invent new metrics to support their weak case. The presentation of these new measures often sounds compelling but upon review they are often revealed as "voodoo economics". Recently in the battle over the Pennsylvania Turnpike one advocate for privatization used the metric of operating expenses as a percentage of revenues as a measure to prove alleged inefficiency of operations. In reality this is a bogus measure since the lowest-toll-rates-possible goal of a public authority drives a de facto result that their expenses consume almost all of their revenues. In fact the Pennsylvania Turnpike maintains one of the 3 lowest tolls per mile in the country at about 5 cents and therefore its expense will reflect a higher percentage of revenues. This would not be true in the hands of a private operator who must increase tolls to squeeze out a profit margin. The true measure of efficiency is operating cost per mile of toll road and the Pennsylvania Turnpike would score well for efficiency using this metric.

The Real Issue

While many public officials are sidetracked by P3 promoters with too much money and not enough projects, the underlying issue in transportation finance is left unspoken. The infrastructure finance problem is <u>not</u> one of the <u>availability</u> of capital regardless of whether it is public or private, <u>but rather</u> the establishment of an acceptable method of <u>charging motorists</u> for roadway usage.

When we open the door of our automobiles we are utilizing a vehicle that we have invested in heavily through its purchase, normally the second largest investment behind a home for the average family and by far the largest investment for renters. We also purchase high priced auto insurance either because it is required by law or so we can drive with peace of mind. I would estimate the minimum annual investment in car payments and car insurance to exceed $3000, plus auto repairs, and in many cases it may be more than twice that amount.

To protect this investment we all expect smooth roads that will take us to our destination, however, no one want to pay for the roads!!

The average motorist drives 13,000 miles and pays 18.4 cents per gallon into the federal highway trust fund and 20 cents per gallon in Texas gas tax. The average car has fuel efficiency of 20 miles per gallon therefore the average Texas motorist buys 650 gallons of gas per year is paying only $250 per year or about 2 cents per mile driven toward the maintenance, upgrading and expansion of the highway system in Texas. This paltry contribution is in stark comparison to the dollars invested annually in the ownership and operation of a motor vehicle. In Texas the cost of the privilege to legally drive on the roads of the State costs one only $24 per year; the cost of legally putting a passenger vehicle on the roads that will create wear and tear is no more than $60 per year.

At recent prices in excess of $4.00 per gallon for gasoline, the average driver will be paying more than 20 cents per mile just for fuel alone, while paying only 2 cents toward roadway infrastructure.

Does this system make any sense?

Shouldn't the average driver be required to pay his fair share of the cost of the roadway infrastructure? Wouldn't a reasonable number be $500 to $1,000 per year, whether it is paid in license fees, registration fees, gas taxes or tolls?

If a fair and equitable revenue collection system is installed, such as a true cost gas tax or its technologically advanced equivalent, then the capital needed for infrastructure old and new can be readily obtained in the public tax exempt bond market at the most efficient interest rates that will keep these costs to motorists at a minimum.

You should consider a combination of all revenue collection mechanisms in order to assure a vibrant and healthy infrastructure financing program that will end the "crisis". It is not a capital crisis it is a revenue crisis and one that is easily solved. Assessing new roads a toll of 15 cents a mile when the actual cost is 5 cents per mile is not an equitable way to charge motorists. Let motorists pay as they drive through the gas tax but set the gas tax at a true cost of usage amount so that the roadway infrastructure can be delivered.

The Private Sector Role

None of this is to say there is not a role for the private sector in infrastructure. The private sector can often add value through project delivery that reduces the time or in some cases the cost of new roads, but these benefit can be had without giving up public control of the asset. The only case where private ownership might make sense is one that transfers large amounts of risk to the private sector. The Miami Port Tunnel appears to be a good example; the Trans Texas Corridor may be another.

In the end the public versus private choice should be decided with discipline in the analytical process and focus on who can deliver the **most value** to the users of the roadway in terms of cost per mile.