THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

May 24, 2006

The Honorable Thomas E. Petri
Chairman
Subcommittee on Highways, Transit, and Pipelines
Committee on Transportation and Infrastructure
U.S. House of Representatives
Washington, DC 20515

Dear ~~Mr. Chairman:~~ Tom:

I am writing to commend you and Ranking Member DeFazio for holding this important hearing on public private highway partnerships. For more than three years, the U.S. Department of Transportation has made development and expansion of these partnerships one of our highest priorities. I was pleased when Congress included provisions in the surface transportation reauthorization to support innovative financing and encourage public private partnerships (PPPs). I welcome your leadership in continuing to raise awareness among your colleagues about one of the most significant economic trends in the United States.

In order to promote greater private sector participation in our Nation's highway system, the Department has pursued the following strategies: 1) exercise existing legal flexibility to eliminate Federal impediments; 2) conduct extensive outreach to public and private entities interested in the topic; 3) produce materials outlining the potential benefits of partnering with the private sector; and 4) seek legislative changes to further remove barriers to private investment.

Just last week, we announced a National Strategy to Reduce Congestion on America's Transportation Network. This Strategy, discussed more fully below, contains six different initiatives, including a specific effort to encourage States to enact flexible public private partnership legislation similar to what has been adopted in Virginia and Texas.

Much of the media attention to date has focused on the staggering sums offered for long-term leases for two existing U.S. toll roads, one in Chicago and the other in Indiana. By the estimate of some analysts, the upfront lease value of America's existing toll roads exceeds $200 billion and may be much higher. Medium risk, medium return assets such as toll roads are extremely attractive to a wide range of equity investors who, unlike lenders, are willing to bear greater traffic and revenue risk.

In addition, strong projected economic growth, a stable legal regime and low long-term interest rates make the U.S. highway system one the world's most attractive destinations for global capital. We expect an entirely new investor class for these assets to emerge in coming years. Moreover, with every highway project in the planning phases over $500 million expected to be a toll road, this market cannot accurately be considered a niche market. It is real and growing, and we are proud to have played a critical role in creating it.

While there are substantial financial efficiencies and resources that the private sector brings to bear, there are equally strong system performance and accountability improvements that can take place in connection with a privatization.

First, because throughput strongly correlates to revenue, private operators have powerful incentives to reduce congestion and increase the number of vehicles served per hour. It is no coincidence that the Chicago Skyway is now an electronic toll road and that capacity has been significantly expanded through the creation of three reversible lanes. Related to that, customer service levels are likely to be higher on facilities operated by the private sector. As with other businesses, building "brand" loyalty is a primary objective of many private toll road owners around the world.

Second, the private sector will focus investment resources on projects that produce the highest returns. Planning processes are intended to balance various competing interests and produce projects that maximize societal benefits. Too often, however, these processes become heavily politicized, leaving the most beneficial projects without a reliable funding source. Unsolicited private proposals, in particular, can play an important oversight role in this regard.

Third, private providers are more likely to make efficient upfront facility investments that generate higher returns in the future. These investments include longer lasting pavement and faster deployment of new technologies, among others. This risk of public sector undercapitalization can be expected to grow over time as States face increased competition for transportation funds from other State programs.

This is a transformational time in the history of American highways. We are entering the third era of Federal leadership in highway development. The first era began in 1916 with passage of the Federal-Aid Road Act. The Bureau of Public Roads was focused on getting farmers out of the mud and getting their produce to market. The second era began in the 1950s when our Nation faced a crisis of connectivity. President Eisenhower's dissatisfaction with this lack of connectivity led to the largest civil works project in world history – our Interstate highway system.

The challenge of the third era – today's challenge – is congestion and system performance. Each year, Americans lose 3.7 billion hours and 2.3 billion gallons of fuel sitting in traffic jams -- to say nothing of growing unreliability, safety, and environmental costs. Congestion is affecting the quality of American lives by robbing them of time that could be spent with families and friends. A reformed service model that more fully embraces private sector investment and innovation will go a long way toward reversing these alarming trends.

National Congestion Relief Initiative

The *National Strategy to Reduce Congestion on America's Transportation Network* is a six-point plan to reduce congestion in the short term and to build the foundation for successful longer term congestion reduction efforts. The six points include: relieving urban congestion; unleashing private-sector investment resources; promoting operational and technological improvements; establishing a "Corridors for the Future" competition; targeting major freight bottlenecks and expanding freight policy outreach; and accelerating major aviation capacity projects and providing a future funding framework.

The plan focuses heavily on our largest metropolitan areas. The Department plans to enter into *Urban Partnership Agreements* with cities to implement broad congestion pricing or variable toll demonstrations to spread traffic flows throughout the day and to get more out of existing highways. These agreements will help to expedite completion of the most significant highway capacity projects currently underway that hold the greatest potential for reducing congestion and bottlenecks. Additionally, these agreements will provide for more efficient and responsive bus systems that tailor services specifically for rush-hour commuters and for the establishment or expansion of telecommuting and flex scheduling programs.

One of the most critical aspects of the *National Strategy* is reducing or removing barriers to private sector investment in the construction and operation of transportation infrastructure. Today's hearing focuses on this essential DOT initiative. The Department will encourage more States to pursue private sector investment opportunities. State budgets are stretched thin, while gasoline taxes are becoming increasingly untenable as long-term sources of funding. At the same time, major financial institutions and their clients are expressing increasing willingness to invest billions of dollars in roads. Furthermore, PPPs can include incentives for system management and congestion relief, can make owners more accountable to users, and can lower the long-term costs of infrastructure maintenance and reconstruction.

Recent Public Private Partnerships

PPPs are becoming an integral part of the way highways are to be constructed and operated, and they will be even more crucial in the future. Recently, there have been a number of instances in which States have partnered with the private sector. These projects follow a model used widely in other countries in which the government awards a concession to a private sector firm to build or improve a highway, bridge, transit, or railway line. In return, the private sector firm pays the government for the concession and is responsible for maintaining and operating the facility for an extended period of time with tolls collected on the facility.

In May 2003, DOT executed a Transportation Infrastructure Financing and Innovation Act (TIFIA) loan for $140 million for the SR 125 South Toll Road project in San Diego, CA, since renamed the South Bay Expressway. This project is being advanced under a concession agreement between the California Department of Transportation (Caltrans) and the San Diego Expressway Limited Partnership (SDELP), which is owned by the Macquarie Infrastructure Group, an international fund investing more than $150 million to develop and operate the toll road. The South Bay Expressway, which had been on the drawing board for more than two decades, is a key link in the regional transportation system that is needed to accommodate economic growth and cross-border traffic in the southern part of San Diego County. Given its strategic location, the project will facilitate increasing traffic and trade across the U.S.-Mexico border at the Otay Mesa crossing by providing an alternative to the congested environment of Interstates 5 and 805.

This $642 million project is being funded from a combination of senior bank debt, a TIFIA loan, sponsor equity, and donated right-of-way. Without the TIFIA loan, it is doubtful that this project would be moving at all, let alone with a completion date expected in the first quarter of 2007. This is the first TIFIA project advanced with substantial private equity and bank loans, demonstrating how innovative Federal financing tools can attract private investment to critical transportation projects. TIFIA provides an alternative to grants as a way of doing business, allowing private partners to share with the government the risk and rewards of infrastructure investment, thereby providing transportation, creating jobs, and contributing to economic growth. Potential concessionaires seeking to advance PPPs in States such as Texas, Oregon, and Virginia are likely to utilize TIFIA credit assistance for their project financings.

In January 2005, the City of Chicago announced that it had entered into an agreement to lease the 7.8-mile Chicago Skyway Toll Bridge Systems to the Cintra-Macquarie consortium for 99 years. Cintra-Macquarie paid Chicago $1.83 billion for the right to operate the facility and keep the toll revenues.

The Trans Texas Corridor (TTC-35) is probably one of the better known PPPs. In March 2005, the Texas Department of Transportation and Cintra-Zachary, an international consortium of engineering, construction, and financial firms, signed an agreement to develop the TTC-35. Cintra-Zachary will invest $6 billion to build a toll road between Dallas and San Antonio by 2010, and agreed to pay the State $1.2 billion for the concession. In return, Cintra proposes to negotiate a 50-year contract to maintain and operate the new highway as a toll road.

In March of this year, Indiana agreed to lease the Indiana Toll Road, a 157-mile roadway that runs from Ohio to Chicago across the northern part of Indiana, to the Cintra-Macquarie consortium. Under the agreement, Indiana will lease the toll road for 75 years in exchange for a lump sum payment of $3.8 billion, which the State will invest in infrastructure improvements.

DOT PPP Efforts

Recognizing the substantial policy and financial benefits of PPPs, DOT has undertaken a number of initiatives to increase the role of the private sector in highway projects in the last three years, including conducting outreach with State governments and the private sector. We have created a PPP office to serve as a central point of contact for those who want to explore new and creative ways to design, develop, and deliver highways and bridges. FHWA also has created a Tolling and Pricing Team to educate public authorities about the many tolling options and programs available and to assist them with pursuing those options and programs.

In December 2004, the Department issued a *Report to Congress on Public-Private Partnerships*. The report is a rich source of information on the value that these partnerships can add to our transportation system. This includes quantifiable cost and time savings, as well as anecdotal evidence suggesting that quality and innovation increase by involving the private sector earlier in a project. The report's many case studies serve as an important resource. In preparing the report, FHWA consulted with States, local governments, trade associations, law firms, and the contracting community. They were asked to help identify impediments to forming not just more PPPs, but more kinds of PPPs, for large, capital-intensive highway and transit projects.

FHWA also published a *Manual for Using Public-Private Partnerships on Highway Projects*, which is available at http://www.fhwa.dot.gov/ppp/manual_0905.pdf. The Manual is intended to provide a one-stop resource for States interested in pursuing PPPs and needing information about how Federal requirements apply to PPPs. Although a summary document, it identifies links and references that will provide access to more detailed guidance for anyone interested in pursuing a PPP.

In addition to the report and manual, FHWA created a PPP website to provide a comprehensive, electronic source of information to States and the public. (*See*, http://www.fhwa.dot.gov/ppp/). The web page contains examples of different types of PPPs, case studies, a resource library, and links to other PPP websites. The website identifies States that have enacted statutes that enable the use of various PPP approaches for the development of transportation infrastructure and includes links to the statutes, brief summaries of the PPP legislation, and a brief analysis of those statutes. Summaries and analyses of five PPP agreements are also located on the website.

In order to allow States to experiment more with PPPs, FHWA established Special Experimental Project No. 15 (SEP-15). SEP-15 grew out of early initiatives, such as Special Experimental Project No. 14 (SEP-14), which experimented with innovative contracting methods, and TE-045, which experimented with innovative finance. The purpose of SEP-15 is to encourage innovation in project development and delivery. SEP-15 is aimed specifically at promoting increased project management flexibility, innovation efficiency, and timeliness, while simultaneously identifying new revenue sources. SEP-15 is assisting PPP projects such as the TTC-35 to be undertaken. SEP-15 is intended to assist with projects and is not a tool for broad programmatic changes. FHWA plans to use the lessons learned from SEP-15 to develop more effective approaches to highway project planning, project development, finance, design, construction, maintenance, and operations.

In addition to these efforts, DOT has sponsored a number of conferences and workshops to bring the public and private sector together to discuss issues related to PPPs.

SAFETEA-LU and PPPs

The Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) includes a number of provisions that support innovative financing and encourage PPPs. Private Activity Bonds, expanded tolling authority, TIFIA loans, and State Infrastructure Banks are tools that will attract private sector investment and participation.

By leveling the playing field between public and private sector borrowers, we expect new kinds of transactions to emerge in highway construction finance. Highway and surface freight transfer facilities are now eligible for up to $15 billion in tax-exempt Private Activity Bonds. Qualified projects, which must receive Federal assistance, include surface transportation projects under Title 23, international bridge or tunnel projects for which an international entity authorized under Federal or State law is responsible, and facilities for the transfer of freight from truck to rail or rail to truck.

SAFETEA-LU lowered the threshold required for total program cost to $50 million ($15 million for Intelligent Transportation System projects) for the TIFIA program. Eligibility now includes public freight rail facilities, private facilities providing public benefit for highway users, intermodal freight transfer facilities, access to such freight facilities, and service improvements to such facilities.

All States may now establish State Infrastructure Banks capitalized with Federal transportation funds authorized for fiscal years 2005-2009. This program gives States the capacity to increase the efficiency of their transportation investment and significantly leverage Federal resources by attracting non-Federal public and private investment.

States now have more flexibility to use tolling on highways, including on Interstates to a limited extent, to manage congestion and finance infrastructure improvements. Under the new Interstate System Construction Toll Pilot Program, the Secretary may allow up to 3 States to collect tolls on an Interstate highway, bridge, or tunnel for the purpose of constructing Interstate highways. The Value Pricing Pilot Program is continued and the Department believes this program will support our congestion relief efforts. The new Express Lanes Demonstration Program will allow a total of 15 demonstration projects to permit tolling to manage high levels of congestion, reduce emissions in nonattainment and maintenance areas, or finance added Interstate capacity for the purpose of reducing congestion. A State, public authority, or public or private entity may apply. SAFETEA-LU also continues the Interstate System Reconstruction and Rehabilitation Toll Pilot Program without change. States also have the authority to convert high occupancy vehicle (HOV) lanes to high occupancy toll (HOT) lanes under certain conditions.

There are other, non-finance related provisions that will assist in attracting private sector investment. For example, the change in the Design-Build provisions to allow certain actions related to entering into a design-build contract prior to the completion of the National Environmental Policy Act process should generate much more interest from the private sector in design-build projects, since it can be involved much earlier in the project definition stage of project development.

Some of the SAFETEA-LU changes in environmental provisions will improve cooperation between State and Federal agencies that participate in the environmental review process. The 180-day statute of limitations on bringing legal action after Federal agency approvals are published in the *Federal Register* will help to bring some increased certainty to the process and will provide assurances to our private sector partners.

Looking Towards the Future

As we continue to implement SAFETEA-LU, we must think about the next reauthorization, which will come upon us quickly. Highway facilities have been financed and managed in the same way for 50 years. We need to broaden our thinking and move forward to address today's challenges. Instead of thinking of roads and bridges as liabilities, State and local governments need to think of infrastructure as assets.

The two commissions authorized by SAFETEA-LU will provide much needed thinking on financing alternatives and on the future needs of the entire surface transportation system. The National Surface Transportation Policy and Revenue Study Commission, which is convening today, will review current methods and explore alternatives for investing in and managing our surface transportation systems. The Commission will be tasked with finding solutions that not only raise revenue for highway and transit projects, but also reduce the costs of congestion.

It is also critical that we initiate activities that will advise all of us about the viability of options that may exist or need to be established to help address the many challenges that will certainly face the Highway Trust Fund at the expiration of SAFETEA-LU. We intend to use the Open Roads program proposed in the President's fiscal year 2007 budget to facilitate new projects that will demonstrate the value of innovative ways to finance and managed highway capacity. The Open Roads program would provide funds to make practical tests of new, but not yet widely used, ideas, or ideas that have been used successfully in other countries. For example, there have been a number of value pricing projects studied and implemented, but they tend to focus on a single facility. We hope that an Open Roads applicant will test pricing on a broader network of roads to better demonstrate the potential for financing highways as a network, rather than as a single facility.

The $100 million of proposed funding for this pilot, which we intend to replicate in fiscal year 2008, will assist up to five States in demonstrating and evaluating potentially more efficient methods of charging for the use of major portions of their highway system. In implementing the program, we will look for innovative mechanisms that can augment current funding mechanisms, enhance highway performance, and reduce congestion. The lessons from this pilot program will benefit the entire Nation and will inform the next reauthorization act.

Conclusion

In closing, Mr. Chairman, I want to reiterate my strong support for this hearing and my appreciation for this Subcommittee's efforts to develop new solutions for our Nation's transportation needs. Congestion is not an insurmountable problem, but we must embrace new solutions if we are going to make any meaningful progress in reducing congestion.

PPPs maximize the strengths of both the public and private sectors. It is time to take advantage of the private sector's flexibility, innovation, creativity, expertise, and access to capital, while maintaining public oversight, accountability to taxpayers, and long-term strategic planning.

I would be grateful if you would include this letter in the official record of today's hearing, and I look forward to working with the Subcommittee to continue to ensure our Nation's transportation system is the envy of the world.

Sincerely yours,

Norman Y. Mineta

OFFICE OF THE SECRETARY OF TRANSPORTATION
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