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SEARCHING FOR SOLUTIONS

A Policy Discussion Series

PARTNERSHIP FOR INVESTMENT

Symposium Summary: Bonding and Innovative Financing

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July 20, 1994
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The following is a list of other publications in the Federal Highway Administration's "Searching for Solutions: A Policy Discussion Series."

Number 1	March 1992	Exploring the Role of Pricing as a Congestion Management Tool
Number 2	June 1992	Exploring Key Issues in Public/Private Partnerships for Highway Development
Number 3	August 1992	Public and Private Sector Roles in Intelligent Vehicle-Highway (IVHS) Deployment
Number 4	August 1992	Assessing the Relationship Between Transportation Infrastructure and Productivity
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Number 7	December 1992	Edge City and ISTEA—Examining the Transportation Implications of Suburban Development Patterns
Number 8	July 1993	An Examination of Transportation Industry Productivity Measures
Number 9	February 1994	Bond Financing and Transportation Infrastructure: Exploring Concepts and Roles
Number 10	September 1994	Metropolitan American in Transition: Implications for Land Use and Transportation Planning
Number 11	October 1994	Summary of the Federal Highway Administration's Symposium on Overcoming Barriers to Public-Private Partnerships
Number 12	November 1994	Life Cycle Cost Analysis—Summary of the Proceedings: FHWA Life Cycle Cost Symposium
Number 13	December 1994	Conference on American Trade and Transportation (Border Crossings)
Number 14	June 1995	The Federal Highway Administration's Highway Cost Allocation Workshop

Foreword

This report summarizes a symposium sponsored by the Federal Highway Administration (FHWA) on bonding and innovative financing. Highway, transit, and other transportation infrastructure needs significantly exceed Federal, State, and local capital investments. This imbalance has sparked the national transportation community's interest in exploring innovative financing options, including bonding. The Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA) encourages innovative solutions to the Nation's transportation challenges and provides new opportunities for action. Using ISTEA's mandate as a framework, the symposium specifically focused on creative financing approaches such as bonding, credit enhancement, and revolving funds.

The July 20 Symposium included introductory remarks from FHWA Administrator Rodney E. Slater. The keynote speakers were Howard Yerusalim, then AASHTO President and Pennsylvania Secretary of Transportation and Beverly Swaim-Staley, Director of Finance for the Maryland Department of Transportation.

An afternoon of keynote presentation was delivered by FHWA Deputy Administrator Jane F. Garvey. In her presentation, Deputy Administrator Garvey explained the goals of the FHWA Innovative Finance Program (Test and Evaluation Program TE-045) and laid out ten precepts for public-private partnerships and their financing.

Three panels gave participants the opportunity to learn about and discuss innovative and emerging finance options as additional ways of increasing investment in transportation infrastructure and bringing projects more quickly to construction.

The first panel, chaired by Gloria J. Jeff, FHWA Associate Administrator for Policy, focused on State, Local, and Toll Authority perspectives on financing. Bob Cowans, Washington State, Maureen Gallagher, International Bridge, Tunnel, and Turnpike Authority, Eric Tucker, City of Detroit, and John Platt, Ohio Department of Transportation (ODOT) shared perspectives from their varied points of view.

A second panel, chaired by Madeleine S. Bloom, FHWA Director, Office of Policy Development, considered transportation issues in the bond industry. John Petersen, Government Financial Group, John Wenderski, Prince William County, Virginia, and Steve Martin, Office of the Secretary of Transportation discussed the various issues impacting current transportation bond financing. Mr. Petersen provided a broad framework for the discussion; Mr. Wenderski described local bond financing issues; Mr. Martin discussed credit enhancement and FHWA's Innovative Finance Program (Test and Evaluation TE-045).

A third panel focused on innovations in transportation financing. Michael Deich, White House, gave background on the Administration's Executive Order on Infrastructure Investment, Executive Order 12983; Kathy Ruffalo, Senate Environment and Public Works Committee staff discussed legislative activity impacting transportation and transportation financing; Tom McPherson, ODOT, Bruce Cannon, FHWA, and Jerry Poston, also FHWA described current progress in the area of Innovative Finance. Mr. McPherson's remarks described the work of the AASHTO Task Force on Innovative Finance; Mr. Cannon's and Mr. Poston's remarks described FHWA's work in that same area.

This report is the fifteenth issue of *Searching for Solutions: A Policy Discussion Series*. The series deals with emerging transportation issues such as congestion pricing and public-private partnerships as well as other relevant transportation policy topics. We anticipate generating a wide-ranging dialogue on these and other important challenges facing policy development.

In fact, since this symposium, important progress has been made in this area. Under direct guidance of FHWA Deputy Administrator Jane F. Garvey, FHWA has approved 49 projects in 29 States, with a total estimated project cost of about $3.5 billion. As a result of "lessons learned" from real project results, FHWA has made a change to its guidance on ISTEA Section 1044. This change is allowing States to take greater advantage of investment toll credit provisions by broadening the maintenance of effort determination. A second change, which will permit States to manage advance construction project financing more efficiently, is advancing through the regulatory process.

The FHWA Innovative Finance Program has taught important lessons which are best made through legislative change. The Administration's National Highway System designation proposal (S.775) is accompanied by legislative proposals that would bring about financial improvements identified by Innovative Finance, including State Infrastructure Banks. Senate NHS legislation (S.440) also embodies many of these Innovative Finance concepts.

Gloria J. Jeff

Associate Administrator for Policy

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Introduction and Opening Remarks

The Federal Highway Administration (FHWA) sponsored a **conference on Bonding and Innovative Financing** on July 20, 1994 to explore new and creative ways of financing transportation infrastructure investment. The conference brought together a diverse group of participants from all levels of government and the private sector to learn from each other and to share ideas on how to meet the Nation's infrastructure needs with limited financial resources. The conference was a follow-up to an earlier conference on transportation bonds and an outreach effort in support of FHWA's Innovative Financing effort.

The conference was opened by Gloria J. Jeff, Associate Administrator for Policy at FHWA (moderator) and Rodney Slater, Federal Highway Administrator. Their remarks set forth the challenge to find solutions beyond traditional financing methods. The afternoon session was kicked off by Jane F. Garvey, Deputy Administrator of FHWA, who emphasized the importance of addressing infrastructure investment needs and highlighted partnerships as the theme of the day.

Keynote speakers Howard Yerusalim, American Association of State Highway and Transportation Officials (AASHTO) President and Pennsylvania Secretary of Transportation, and Beverly Swaim-Staley, Director of Finance of the Maryland Department of Transportation, discussed how each of their respective States are dealing with financing and their ideas for the future. Three panels gave participants the opportunity to hear about current initiatives, ideas, and difficulties from different points of view. The first panel presented the perspectives of State and local bond issuers and their concerns regarding matters affecting bonding and credit. The second panel aimed to demystify some of the difficult questions about bonds, their markets, and their role in transportation projects. Speakers in the final panel examined innovations which may now, or in the future, improve infrastructure investment.

Opening Remarks

Gloria J. Jeff, Associate Administrator for Policy, FHWA (Moderator)

Ms. Jeff welcomed the participants to the conference and encouraged them to help the Administration find new ways of making the best use of their ISTEA funds, other public funds, and private investment.

Hon. Rodney E. Slater, Federal Highway Administrator

Mr. Slater began his remarks by commenting on the number of individuals that had gathered to help pave the way and shape the vision for innovative finance. He described the challenges of the transportation industry: mounting needs and limited resources, budgetary caps on discretionary spending, and the need to compete on an international level.

Mr. Slater described how natural disasters, such as tropical storm Alberto in July 1994, help underscore the importance of transportation infrastructure. He pointed out that the opening of the Santa Monica Freeway ahead of schedule after the earthquake demonstrated that the public was willing to pay the extra costs to get the system back in place; they value good work and are willing to pay for it. A goal of this conference was to identify ways to deliver a good product in a timely fashion at a reasonable cost.

Administrator Slater highlighted President Clinton's challenge to rebuild America and Secretary Peña's challenge to make transportation more human, which will result in quality of life improvements and a more competitive America in years to come. He expressed hope that this day be recognized in the future as a day when people came together and decided to do business differently.

First Keynote Presentation:

Pennsylvania's Innovative Financing Experience

Howard Yerusalim, AASHTO President and Pennsylvania Secretary of Transportation

Mr. Yerusalim began by stressing the need for innovative financing. He stated that revenues will not meet existing transportation needs and traditional financing methods will not be sufficient. Citing figures from the FHWA/FTA report on the status of the Nation's highways, bridges, and transit systems, he pointed out that:

- In 1992, we spent $38.7 billion on highway and bridge programs around the country. However, the Nation needed $51.6 billion to maintain current conditions and $67.3 billion to improve the system;
- On the transit side, we spent $4.3 billion with needs in the $6.6 billion to $16 billion range.

Mr. Yerusalim suggested that innovation will help discover new financing methods to narrow this gap between transportation infrastructure needs and the amount of funding available.

Past Experiences With Innovative Financing

Making the point that innovative financing is not a new idea, Mr. Yerusalim cited examples of projects in his State that have already used new financing methods. In 1988, Pennsylvania won the first FHWA award for innovative financing of the Thorn Run interchange near Pittsburgh. In order to address safety concerns, provide better access, and create more opportunities for economic development, the State and local governments needed $8.5 million to build a new interchange. The township formed a transportation development district (TDD), allowing them to assess property owners for the building of transportation facilities from which they would benefit. A total of $2.9 million in local funds was raised. Pennsylvania has come a long way, Mr. Yerusalim said, with projects underway that are much larger with greater investment from local communities and from private developers.

The second example Mr. Yerusalim cited was the completion of the Interstate system in his State. Combining discretionary funds with their normal apportionment for Interstate Construction, the State was $500 million short of the $1.8 billion required. The State decided to borrow money for the short-term (three to five years) in anticipation of future Federal funding. This is similar to advance construction where a State can independently raise up-front capital required for a project and preserve eligibility for future Federal-aid funding for that project. Instead of issuing bonds, Pennsylvania issued Federal Reimbursement Anticipation Notes. The debt was tied to a contract with FHWA specifying not only that FHWA would reimburse costs as the apportionments came through to the State, but also that FHWA would pay a portion of the interest because of the money saved in construction costs by building the facility sooner. The result of this innovation was that Pennsylvania opened these Interstate segments three to four years sooner than it would have if the State had waited for the actual apportionments to become available.

Pennsylvania's billion dollar bridge program was Mr. Yerusalim's third example. Faced with deteriorating bridges and a lack of funding, the Pennsylvania Department of Transportation (PennDOT) went to the State legislature to request a dedicated tax to support bonds and to leverage Federal funds. With that tax, PennDOT was able to fund $1 billion worth of projects. He posed the question: why was the legislature willing to borrow funds for this program? The answer:

- The need was there, and they recognized it;
- PennDOT had a plan to conduct a program that the legislature was interested in; and

- PennDOT was willing to work with legislators on a dedicated tax to fund the program.

Due to increased Federal funds and the availability of more State funds than anticipated, the program is self-sustaining. Mr. Yerusalim reported that although it started with the goal of 1,000 bridges for $1 billion, the program has included the replacement or major rehabilitation of 1,900 bridges for $2 billion since its inception.

The final example of past projects Mr. Yerusalim discussed that utilized non-traditional funding mechanisms involved toll financing. The legislature authorized $4 billion in bridge and highway improvements on the Pennsylvania Turnpike. The financing plan included two 30 percent toll increases and a major gasoline tax increase equivalent to approximately 5 cents per gallon, a portion of which was dedicated to the Turnpike for its toll road expansion. Through toll revenues, Pennsylvania built the first billion of that $4 billion program.

Current and Future Innovative Financing Projects

Mr. Yerusalim then discussed several projects currently underway that involve innovative financing. In the first case, Pennsylvania used ISTEA's flexible funding sources to help finance an Interstate Expressway. In another instance, the State used a public-private partnership to prepare and develop land surrounding the I-95 viaduct through downtown and south Philadelphia. The last example he cited was another form of public-private partnership, where large businesses are required to pay for improvements that are needed due to the increase in traffic generated by these businesses.

Pennsylvania has responded to FHWA's request for innovative funding projects, Mr. Yerusalim reported, with three proposals:

- To use advance construction, starting projects with State funds and converting them to Federal funds on an advantageous schedule;
- To allow investment from private entities to count toward the non-Federal matching share of enhancement projects; and
- To allow publicly donated rights-of-way to count toward the non-Federal matching share of a project.

While hopeful that these initiatives will be approved, Mr. Yerusalim emphasized that there is a long way to go. He mentioned that, in Pennsylvania, the improvement of I-95 is essential. With the help of FHWA, Federal Transit Administration (FTA), local transit authorities, and others, PennDOT developed a model 21st century corridor demonstration project that will include transit, rail, highway, and a new high occupancy vehicle (HOV) facility. Although Mr. Yerusalim is uncertain of the source of the $2 billion needed for reconstruction of I-95, he believes the project is critical for the State. He presented several methods to raise the funds:

- Tolling of existing Interstate facilities;
- Issuing bonds with a dedicated funding source; and
- Initiating congestion pricing.

In conclusion, Mr. Yerusalim emphasized cooperation and partnership with the environmental community, the U.S. Department of Transportation, and the private sector.

Second Keynote Presentation:

Maryland's Financing Strategy

Beverly Swaim-Staley, Director of Finance for the Maryland Department of Transportation

Ms. Swaim-Staley stated that Maryland is always looking for new ways to stretch its resources, particularly as the costs of maintaining highway and other transportation systems become more and more prohibitive. Her presentation focused on how Maryland DOT is unique in both its structure and approach to financing and then discussed past and present innovative projects.

Maryland's Financing Structure and Approach

Ms. Swaim-Staley pointed out that the Maryland DOT is an intermodal agency with responsibilities for its highway system, its motor vehicle administration, operation of the Baltimore-Washington International Airport (BWI), the Port of Baltimore, the City of Baltimore's mass transit system, and partial responsibility for the mass transit system surrounding Washington, D.C. In addition, as of 1995, Maryland DOT will own and operate its own vehicle emission and inspection stations.

These activities are supported by a transportation trust fund that is separate and distinct from other funds in Maryland. The fund receives revenues from a gasoline tax, titling tax, fees charged at BWI Airport and the Port of Baltimore, fare box recovery on the transit system, motor vehicle taxes and fees, and a small portion of the corporate income tax. Revenues, however, are not allocated to the particular mode that generates them.

Ms. Swaim-Staley then discussed the Maryland DOT's six-year planning process, an essential part of its financing program. In quarterly reviews, its Department of Finance staff reviews expenditures, projected cash flows, debt service, and capital and operating expenditure needs. Then the department plans the bond program based on needs over a six-year period, incorporating the Maryland DOT's ability to repay the bonds. The State of Maryland uses its bonding capacity to support its highway program.

The State is conservative in its approach to debt and maintains a AAA rating. Ms. Swaim-Staley described the role of its capital debt affordability committee, made up of the Comptroller, the Treasurer, the State budget officer and the Secretary of the Maryland DOT. In order to issue debt, the Maryland DOT must work with the committee to ensure that the State can back the amount of debt it is issuing. In fact, there are specific parameters to which the department must adhere.

Ms. Swaim-Staley indicated that the Maryland DOT generally issues three kinds of debt: consolidated transportation debt, county transportation debt, and, occasionally, Certificates of Participation. (Certificates of Participation are financial instruments, similar to bonds, backed by physical assets which are held by a trustee.) It usually issues bonds through a competitive process, working with the legislature to agree on a reasonable debt ceiling while maintaining flexibility for unforeseen emergencies. As security for their bonds, the Maryland DOT pledges its share of gasoline taxes, motor vehicle taxes, titling taxes, and corporate income taxes. It also has other revenues from operations and other sources to back the bonds if needed. The Maryland DOT revenue to debt service ratio is forecasted as 2.5 to 1, giving them an extra cushion.

Another unique feature of Maryland's financing structure is the Maryland DOT's relationship with the toll authority. The Maryland Transportation Authority is semi-independent from the State DOT. The Authority has its own trust fund and Board of Governors, but the two agencies work together on many systems and projects. Often, she pointed out, the Maryland DOT has been able to utilize the Authority's cash resources when needed for program enhancement. Further, the department is planning to use the Authority to finance new facilities at BWI Airport.

Ms. Swaim-Staley also believes that Maryland has a unique and beneficial relationship with its county transportation program. Because none of the counties have the authority to issue debt, the State has a county bond program whereby the department offers to issue bonds on behalf of the counties once a year. She indicated that an issue was recently raised because the county debt was on the State books as State debt. The Maryland DOT has since restructured the program, clarifying that it is the counties that are responsible for the debt, not the State. The counties, however, maintain the benefit of using the State's high credit rating.

Past and Future Innovative Financing Projects

Ms. Swaim-Staley described two of Maryland's innovative financing experiences:

- Maryland DOT completed a cross border lease transaction for commuter rail vehicles involving a Danish partnership; and
- Maryland DOT issued Certificates of Participation to update its motor vehicle administration facilities.

In addition, Maryland has always had an aggressive advance construction program.

Ms. Swaim-Staley also described the State's response to FHWA's Innovative Financing Test and Evaluation Program (TE-045). Under this initiative, the State proposed three different options for creative financing:

- Using approximately $5 million in developer contributions as the non-Federal matching share instead of public contribution would allow the State to use the public funds elsewhere to bring an additional project into its program immediately;
- Proceeding with partial conversion of advance construction funds would allow Maryland to carry out two major projects sooner; and
- Seeking to use Section 1044 toll credits as the non-Federal matching share, the state is asking FHWA to provide a more flexible interpretation of the current maintenance of effort requirements.

In conclusion, Ms. Swaim-Staley indicated that despite Maryland's strong trust fund, strong partnerships, and high credit rating, the State needs additional dollars. The State is looking for any innovative financing methods for highways and transit. She believes that Maryland needs to use creative ways to utilize its private, local, and regional partnerships. Developing innovative methods to stretch dollars is key to the State's success.

Discussion

The panel asked the two speakers if they will continue to utilize the partial advance construction concept and, if so, for what level of funding and for how long—through the end of ISTEA or beyond. Ms. Swaim-Staley responded that Maryland will continue to do so through the end of ISTEA for approximately $20 million. Mr. Yerusalim indicated that the State is working with FHWA on a proposal to use over $100 million on certain Interstate restoration projects in Pennsylvania. Under current law, States cannot advance construct beyond ISTEA authorizations; he noted, however, that perhaps it could be changed.

Noting the difficulty many States and localities have in receiving good bond ratings, a participant asked Ms. Swaim-Staley if the existence of Maryland DOT's multi-modal transportation trust fund was an advantage in acquiring their AA rating.[1] She noted that the Maryland DOT has always had an AA rating—even prior to the establishment of their multi-modal trust fund. She believes, however, it is helpful the department is multi-modal because it has diverse revenues and is not reliant on a single source like some agencies. In addition, the DOT worked with the State to set standards and criteria that were strict enough to qualify for a high bond rating. The department has also attempted to maintain the appropriate coverage levels and a fund balance—cushions that rating agencies like to see.

1 The State of Maryland's bonds are rated AAA, but the Maryland DOT's debt is rated AA.

Panel on State, Local and Toll Authority Perspectives on Bonding

Introductory Remarks

Gloria J. Jeff, FHWA Associate Administrator for Policy (Moderator)

Ms. Jeff explained that the first panel of the conference would focus on State, local, and toll authority perspectives on bond financing. Bob Cowans of the Washington State Department of Transportation and John Platt of the Ohio Department of Transportation would give views from the State level. Maureen Gallagher from the International Bridge, Tunnel, and Turnpike Authority (IBTTA), would discuss the perspective of the toll authorities. Finally, Eric Tucker of the City of Detroit would discuss local municipal issues and perspectives on bonding and transportation financing.

Ms. Jeff noted that States have clearly been the laboratories of innovation as they look for creative ways to fund projects. She indicated that in the 1980s and early 1990s, State and local government entities increased their annual capital spending by 6.5 percent, an amount greater than the rate of inflation, and have increased bonding from approximately $1 billion annually in the early 1980s to over $6.4 billion worth of bonds in 1993. State and local governments have both found innovative and creative ways to address funding shortfalls.

Panel Presentations

Bob Cowans, Director of Financial Planning for Washington State Department of Transportation

Mr. Cowans provided the participants with an update on Washington's private partnerships in transportation and presented observations on their financing strategies. In 1983, the legislature passed a bill that gave the Transportation Commission and the Secretary of Transportation broad authority to accept and negotiate agreements for public-private partnerships for transportation facilities. In response to Washington DOT's request for proposals, he reported that the department received 14 proposals involving toll bridges, transit parking, toll roads, a people-mover system at the airport, a new freeway interchange, a new ferry service, and a tunnel bypass loop. The projects ranged in price from $24 million to $1.4 billion, and 13 of the 14 would entail some Federal involvement.

Mr. Cowans categorized the financing strategies into three broad areas:

- Long-term tax-exempt debt issued by a special purpose entity;
- Long-term taxable debt issued by the project proposed; and
- Long-term debt, either taxable or tax-exempt, supplementing public funding. This would allow tolling at levels that will likely be acceptable to the public.

Mr. Cowans then offered some observations regarding the financing strategies. For some of the projects, the concept of equity capital was somewhat strained, with the equity being derived from pre-tolling existing facilities and the designation of the net toll revenues as equity capital. He indicated that there were substantial similarities in the security provisions of both taxable and tax-exempt debt proposals. In the proposals, however, the assignment of risk did not display uniformity. Lastly, he observed that the proposals had a wide range of public sector involvement.

Mr. Cowans reported that the next step in the process was currently underway. After a State DOT briefing, the selection board would review the proposals and select six to recommend to the Secretary for approval by the Commission. Mr. Cowans noted that he expected to begin negotiations with the six project proponents by September 1994, with an end of year completion goal.

In this process, Mr. Cowans indicated that the State and the Washington DOT have to address certain policy issues related to both the financial and political aspects of public-private partnerships that raise fundamental policy questions including:

- Are facility-specific user fees, such as tolls, a more appropriate way to finance infrastructure than more traditional methods like the gas tax? If so, will the public accept the concept of congestion pricing to influence transportation demand?

- To what extent does the implementation of public-private partnerships take the pressure off of State legislatures to provide support for transportation facilities and services that cannot be financed with direct user fees?

Mr. Cowans concluded that these are some of the issues that the Washington DOT has to face over the next few months. During that time, it will find some answers that will ultimately address the level of risk that the public, the legislature, and transportation officials are willing to take.

Discussion

Mr. Cowans was asked if he anticipates Washington DOT's normal operating program and Federal apportionments to be disrupted as a result of the private partnership program currently underway. Mr. Cowans responded that he does not anticipate any disruptions because most of the projects do not involve large amounts of Federal funds. In addition, regular apportionments will continue to be distributed and used in the same way.

Maureen Gallagher, Director of Research and Member Services, IBTTA

Ms. Gallagher began by demonstrating the importance of the bond market to toll facilities. She indicated that toll facilities have made extensive use of the bond market throughout their history. The approximately 5,000 miles of facilities have used revenue bonds to finance and operate their toll facilities, and credit markets have historically given them good ratings.

Ms. Gallagher discussed some of the factors that affect credit ratings for new facilities. Questions related to credit include:

- Does the tollway play a critical and essential role in the State?

- Will traffic be significant enough to maintain a steady stream of revenue to repay bonds?

- Are there any competing free facilities that will divert a significant amount of traffic and, in turn, hamper revenue?

- Is projected revenue sufficient to cover operations and maintenance costs as well as debt service?

- Can management interact with political, natural, and regulatory forces without compromising its agenda?

Some of the questions credit markets look at when rating existing facilities include:

- Is there any historical trend of operations and debt coverage?
- Has traffic grown?
- Does the facility contribute to the State's overall transportation development?
- What is the history of toll rate increases?
- What are the political, economic, and social conditions of the area? Will the new debt be supported?

Ms. Gallagher presented some background information on toll facilities and IBTTA's experience with innovative financing. She noted that most toll facilities in the U.S. are public agencies created by State legislation. Toll authorities are quasi-governmental agencies able to issue their own debt, collect tolls, and provide for the operation and maintenance of their roads. Though they serve the public, toll authorities often make financial decisions through a process similar to that of the private sector. For these reasons, they have gained a favorable reputation in the financial community. Ms. Gallagher believes innovative financing for toll facilities began in the 1980s, with projects like the Harris County Toll Road and the Jesse Jones Memorial Bridge, both of which are located in Texas, and the Dulles Toll Road in Virginia.

Ms. Gallagher explained that Federal legislation in 1987 was another important development in toll financing. This legislation, the Surface Transportation and Uniform Relocation Assistance Act legislation, included a toll pilot project in which nine States (seven initially) were given the opportunity to use Federal-aid funds to construct toll facilities at a 35 percent matching rate. This program was the precursor for the Intermodal Surface Transportation Efficiency Act (ISTEA) in 1991, which allowed toll facilities to use Federal financing at a 50 percent matching rate. Though there have been many successes with this financing option, problems stem from some of the regulations associated with Federal funds. Ms. Gallagher likened the Federal regulations to a catch-22 situation; accepting Federal dollars can often result in additional costs associated with meeting Federal regulations, and these costs can outweigh benefits. She believes revolving loan funds without the use of a State's Federal funding allocation could solve this problem.

ISTEA also created a public-private initiatives program to supplement transportation revenues that allows the States to apply their limited resources to other needed projects. As a result, the level of cooperation among the Federal and State agencies and toll authorities has improved.

Ms. Gallagher concluded by emphasizing that toll authorities are committed to public-private partnerships and innovative financing. She is anxious to see the results of FHWA's TE-045 initiative and offered IBTTA's assistance in promoting it.

Discussion

Ms. Gallagher was asked if she believes that interest rates will continue to be the major factor in the decision to construct toll facilities as it was in the late 1970s and 1980s. She responded that interest rates are not the major force in current trends in toll facilities nor will they be in the future. Instead, social, economic, and governmental factors play a larger role in those decisions.

Eric Tucker, Director of Finance, City of Detroit

Mr. Tucker began by introducing some of the issues that local officials face when financing transportation. First, he noted that they must determine the goals of their transportation program. For example, are they building more roads to help concentrate the workforce into one area such as a downtown area, or are they trying to develop regional competition versus other jurisdictions? These questions are important to consider when choosing projects.

Once local governments determine their focus and decide to build new facilities, they must decide between bonding and pay-as-you-go financing. There is typically strong citizen opposition to issuing debt due to the fear of a tax increase. On the other hand, revenue bonds are considered equitable because the people who use the facility also pay for it.

The third issue that local officials must deal with in financing transportation is prioritization. Mr. Tucker indicated that local governments, in contrast to toll authorities, have many competing capital needs in addition to transportation. Projects must enter a queue with other needs to determine what will be funded at a particular time. Mr. Tucker also raised the issue of limits on outstanding debt. These caps affect how much an agency can borrow at any given time, thereby affecting project allocation procedures.

Once an agency decides to issue bonds, it must decide between general obligation and revenue bonds. Mr. Tucker explained that revenue bonds bring their own set of challenges in addition to the general obligation questions raised above. Issuers must ensure that people will not only use the road, but that they are also willing to pay a fee for use of the facility. In a local area, a toll road may not be viable if free alternate routes exist.

Mr. Tucker then discussed innovative ways of financing bonds. Financial intermediation with State bond banks is the best way for a locality to use its revenue to support its credit. On the revenue side, he suggested long-term contracts with users, such as selling franchises and charging impact fees on new development in the area.

In closing, Mr. Tucker again emphasized the difficulty of implementing tolls. He encouraged the consideration of gas and parking taxes in an effort to marry the cost of driving and the cost of building roads and to encourage people to use public transit.

Discussion

Mr. Tucker was asked how a city like Detroit can improve its creditworthiness. He replied that the city's problems are not difficult to identify. The city needs to strengthen its basic management approach to finance which includes getting an unqualified opinion of financial statements and collecting unpaid taxes.

John Platt, Assistant Director for Modes Transportation, Ohio Department of Transportation (ODOT)

Mr. Platt explained that constrained financial resources for transportation modes has led to creativity. With its 30-year multi-modal plan, ODOT has been able to use some of this creativity in its highway division. As a result, it is planning several innovative projects.

The first project Mr. Platt discussed was an intermodal facility (a rail-highway interchange) involving private, local, and State funds. Operated by a private entrepreneur, the facility will allow trailers and containers to be loaded onto flatcars and transported by railroad and unloaded from flatcars.

Mr. Platt highlighted three unique elements of this project's financing. First, ODOT believes that the project qualifies for congestion mitigation air quality (CMAQ) funds. The project results in a reduction of truck mileage (and, hence, emissions) within the county and in approximately five other non-attainment areas in the State. The second unique aspect of the project is its financing mechanism. It will involve a loan to the local area, backed by approximately 53 acres of land in which the State will have an interest as insurance in the event of default. A private operator will pay the local area a per-trailer-lift fee similar to a toll that will be used to repay the CMAQ funds over a period of time. Finally, legislation has been passed to establish a rail development fund by dedicating 50 percent of rail corporate franchise tax revenues to the fund, thereby providing another source of dedicated revenue for issuing bonds for this type of project.

Mr. Platt pointed out that in addition to economic and environmental benefits, the project will start a loan portfolio that will allow ODOT to set up a revolving loan fund in the future. In order to develop a capital revolving loan fund type of program, he believes that a State must have both a portfolio of loans and a dedicated funding source—giving it as many sources as possible to repay whatever bond financing is required.

Mr. Platt then described a series of highway projects involving the creation of a Transportation Improvement District (TID). Some of the possible revenue sources in the TID for backing bonds include:

- A tax increment financing mechanism with a value capture on increased value around interchanges or capital capture—a 10 percent payment to the TID when land changes ownership within a certain area,
- Overbuying land around interchanges so that the State can lease or develop properties,
- Leasing of the facility by the State,
- A vehicle license plate tax, and
- Revenue from congestion pricing and tolls.

Mr. Platt concluded by encouraging individual States to develop broad enabling legislation to allow financing creativity and innovation that will result in progress.

Discussion

Mr. Platt was asked if the enabling legislation for the Butler County TID was statewide or restricted for a selected area. He responded that the legislation was only for a selected area. He believes that the State legislature wanted to start with a smaller area, particularly to test and evaluate the concept. Mr. Platt, however, hopes the legislation will be expanded.

Afternoon Keynote Presentation

Jane F. Garvey,
Deputy Administrator,
Federal Highway Administration

Ms. Garvey remarked on how gratifying it was to see so many colleagues from State highway departments and from the financial community attending the conference. She stated that the goals of the meeting were to find ways to solve the infrastructure problem described by many panelists in the morning, to break the log-jam in public investment, to generate excitement in public management, and to signal that a new order has begun. Ms. Garvey emphasized that this conference was organized and attended with the belief that America's future productivity, competitiveness, job security, and independence dictate that we address infrastructure investment problems now.

Ms. Garvey explained that the goal of the innovative financing initiative is to increase investment in transportation and to gain a better understanding of which elements of ISTEA work best and which may need to be rethought as ISTEA reauthorization approaches. She stated that the response to FHWA's TE-045 initiative calling for innovative ideas from the States exceeded FHWA's most optimistic expectations. The proposals received are diverse, financially creative, and intermodal in nature.

Ten Commandments of Partnership

Ms. Garvey cited partnerships as the theme of the conference—partnerships between the Federal and State governments and between the public and private sectors. She then gave the participants ten commandments of partnership to think about while working together on innovative financing.

1. **Do not covet the status quo.** All participants should use new ideas and threaten the status quo. Do not wait for change.

2. **Do not be greedy.** While public officials need to understand the commercial market better, private investors need to understand that unless both sides profit, a public entity cannot sustain a partnership. They also must understand that partnerships for community progress should allow reasonable profits; if profits are more than reasonable, the public will not likely accept the project or the partnership arrangement.

3. **Voters do not care about Federal mandates.** Taxpayers do not want to hear Government complaints and excuses. They pay the Government to solve its challenges and to bring them the best ideas and choices for their consideration and approval. If there is a need, state it clearly and blame no one.

4. **Lower cost can lead to higher quality.** The unwillingness to believe this may be the largest obstacle to making the needed changes. As seen with the semi-conductor, the propeller, and the jet, the world moves from higher to lower costs while improving quality.

5. **Remember the big picture.** Though the problem of infrastructure is important, citizens and elected officials view crime and education as more pressing issues. The challenge is to convince them that spending money on transportation is part of the overall solution.

6. **Share the risks and rewards.** Public and private partners cannot each expect to reap the rewards and share none of the risks.

7. **Government is in the market place.** Its ideas and products must be competitive. Once government decides that its destiny is in the market place and time is valued properly, public/private partnerships will be seen as logical and, perhaps, compelling.

8. **Public-private partnerships are not created to fool voters**. Like all innovations, these partnerships must earn support from the people who pay for them. Openness and honesty must be the hallmark of a partnership.

9. **Do not privatize the public interest.** Both public and private partners must believe and live by the code of commitment that drives the best of business people and the best of public servants. This will ensure that both public and private interests are well served.

10. **Be a map maker, and your trail will be followed**. Be mold breakers and pattern creators.

Panel on Transportation Issues in the Bond Industry

Introductory Remarks

Madeleine S. Bloom, Director, Office of Policy Development, FHWA (Moderator)

Ms. Bloom introduced the second panel of the conference as one to demystify some of the difficult questions about bonds, their markets, and their role in transportation projects. While the popularity of highway bonds has grown significantly in the last decade, she pointed out that a barrier still exists in many cases between the transportation and financial communities—each with their own jargon and practices. The panelists were asked to address questions not always fully understood by transportation officials.

Ms. Bloom stated that panelist John Petersen of the Government Financial Group would present his observations on debt policy and bond instruments for capital transportation programs. John Wenderski of the Prince William County, Virginia Finance Office would discuss general characteristics of bond issuers and new ways of generating revenue. Panelist Steve Martin of the U.S. Department of Transportation would address ways of enhancing creditworthiness for highway issues.

Panel Presentations

John Petersen, President, Government Financial Group

Mr. Petersen set out to explain some of the more important trends in public finance and in the municipal securities market in general. Drawing from a paper that he and his colleague, Jason Gross, authored on bond financing and highways, he discussed the peculiarities of highway financing in the context of current problems and solutions.

Mr. Petersen identified the first of two emerging trends affecting transportation financing: the changing pattern of congestion. He stated that not only has the amount of traffic on the Nation's highways increased, but also the traffic has extended outward from the cities with the development of suburbs and circumferential highways. Congestion has become an important political issue—not as a local, city, or municipal problem, but as a regional or multi-State problem.

The second trend that Mr. Petersen observed is the development of a broader modal sense in decision making. This is an important trend that will result in comprehensive transportation planning. ISTEA is the embodiment of a multi-modal approach to transportation problems.

Mr. Petersen then addressed other changes in the transportation environment. Historically, there has been a proclivity in highway financing to rely heavily on pay-as-you-go financing. In the infrastructure area, highways constitute approximately 40 to 45 percent of all spending, but only 10 to 15 percent of the funds for construction purposes are financed through debt. He has, however, observed an increase in the percentage of debt financing. This source of financing is necessary as transportation needs are not being met with the available current revenue sources. Mr. Petersen suggested that States use tolls and other user fees more extensively to meet funding requirements.

Mr. Petersen noted a change occurring in the alignment of responsibilities and methods of financing at the State and local government levels. There is more of a "menu" approach, or a spectrum of possibilities in financing and partnership arrangements, both among the government levels and between private and public entities, from which to choose. In general, local government bodies and private entities are developing means to assist State governments in transportation financing. For instance, if a State government is not able to meet the needs of a community, special districts can and have been instituted to supplement revenue raising opportunities. In addition, there is greater decentralization occurring in the provision and financing of services. Mr. Petersen believes that this brings greater opportunity to experiment and to consider privatization; it allows officials to look for new ways of doing things.

Mr. Petersen then discussed two trends in the securities and bond markets of interest to seminar participants. He believes that some of the experimentation with different bond structures in the past will occur again. With such a large municipal securities market, government agencies can design types of security that will appeal to a variety of investors. There are funds desiring higher yields and investors willing to take the risk to obtain those yields.

The second trend in the municipal securities market involves its regulation and the role of the smaller borrowers, i.e., local governments. If the municipal securities market starts to behave like a corporate securities market, combining types of facilities in a security package will be beneficial. Consolidation and pooling will help alleviate the problems of tracking and trading small issues. Most likely, there will be increased incentive to create bond banks and pools and to develop other methods to consolidate indebtedness.

John Wenderski, Director of Finance, Prince William County, Virginia

Mr. Wenderski began by discussing some of the transportation issues in his county. First, the State would like to shift road maintenance responsibility to the county. Prince William County is currently undertaking its first major road project using general obligation bonds. In this process, the county is shifting a significant portion of its debt from schools to roads. Although he noted that local governments believe they can best serve local needs and can control local outcomes by being responsive to local citizens, the resources available to meet citizens' needs are limited.

Mr. Wenderski observed two factors that are critical to successful transportation financing for most communities. The first involves positive interaction with State and Federal officials in dealing with roads. Because localities often look to the State for funding, they will not be able to undertake the needed projects without ensuring that elected officials and administrators at the State level are aware of their needs. The second critical factor is the ability to use real estate taxes to finance transportation. Real estate taxes fund the majority of operations for most communities, and other types of taxes can be difficult to get approved locally.

Mr. Wenderski suggested some other financing tools that have been effective in his county. They include:

- Highway districts, which are helpful in mitigating project costs to a locality;
- Tax increment financing (financing based on expected increases in public revenues resulting from increased economic benefits from the financed project), which can be risky; and
- Rights-of-way leasing.

Local agencies can improve their credit ratings by improving the management of their finances. Mr. Wenderski explained that Prince William County raised its rating while its revenues were declining by establishing policies to guide financial decisions and by providing local agencies with a framework for spending money, issuing debt, and managing capital programs. The program incorporates some basic elements that many governments (including the Federal government) do not, such as the preparation of a capital improvement program. This six-year program identifies where a government will spend its limited resources and thereby ensures that facilities are prioritized. Another policy that his county uses to ensure good credit ratings is to set self-imposed limits on debt capacity as a percentage of revenues and as a percentage of assessed value. In addition, the county maintains its fund balance at appropriate levels.

Mr. Wenderski believes that the transportation community has not planned ahead in the past, and they are not talking today about planning for tomorrow. Bankers, engineers, and road builders must all keep in mind that current problems are not the problems that they will face in the future. Others will arise in the future, and new methods must be developed to pay for them.

He indicated that before rezoning property, the county recalculates the amount of commercial and industrial property compared to the residential amount. In this way, it understands the impact of rezoning decision. He added that a residential unit with a four-member family will cost the county more than it will generate in taxes. For example, the four-member family will generate approximately $3,000 in real estate taxes, but assuming the family has two school-age children, it will cost the county more than $10,000 in school requirements. Adding the capital infrastructure of the schools will result in an additional $500.

In closing, Mr. Wenderski suggested some local approaches to innovative financing. He mentioned that public-private partnerships have been successful. Because Prince William County is in a development corridor, it has many opportunities to join private entities to improve infrastructure. The second approach involves the Federal government issuing letters of intent to provide appropriations in the future to leverage Federal highway funds.

Discussion

John Wenderski was asked if Prince William County has ever considered growth limits to balance economic development and infrastructure demands. He responded that the county has followed a comprehensive management plan since 1990. This plan identifies and designates areas appropriate for growth. Currently over half of the homes are in one-quarter of the county. Growth is expected along the corridors of two expressways that traverse the county.

Steve Martin, Director of Financial Development, Office of Budget and Programs, Office of the Secretary of Transportation

Mr. Martin opened his remarks by thanking those who submitted proposals for their time, effort, and creativity, thanking the AASHTO task force on innovative financing for their help in facilitating this initiative, and thanking congressional staff for their willingness to support this experiment.

Mr. Martin prefaced his presentation by indicating that his credit enhancement discussion would follow in three segments: **(1)** the status of FHWA's TE-045 initiative, **(2)** the context of FHWA's TE-045 initiative within the U.S. Department of Transportation's initiative, and **(3)** the specifics of credit enhancement.

Mr. Martin began with several observations regarding how the FHWA Innovative Financing initiative is working. He pointed out that the financing ideas are being generated real-time without a predetermined product. As a result, this endeavor is not only risky, but it also has incrementally evolved. Mr. Martin indicted that FHWA is looking for financial ideas and input, to incorporate in the transportation arena, from professionals in other venues. He stated that the TE-045 concept is not a solution to financing problems, but serves as a vehicle that allows evaluation of different financing tools while projects are implemented.

Secondly, Mr. Martin explained how FHWA's project fits into the context of DOT's overall initiative involving each of the modal agencies. Financing initiatives are currently underway in other DOT agencies; however, Mr. Martin noted that each of the agencies has its own set of vocabulary, financing terms, and agreements associated with its products. In assisting FHWA in its initiative, DOT wants to standardize the financing practices of the modal agencies, maintaining some flexibility to ensure continued financing innovations. He observed that standardization may result in additional investment in transportation infrastructure. Many investors have expressed interest in transportation infrastructure but have not had the time to learn the nuances of FHWA, Federal Rail Administration (FRA), and FTA programs. Federal standardization can promote investment by minimizing the amount of time and effort needed to understand this market.

Many transportation and capital market professionals believe that transportation financing's eventual destination is securitization similar to that used in the mortgaged-backed asset markets. Mr. Martin noted that the success of this type of securitization requires projects to be standardized, similar to home mortgages, so they can be bundled. The combined revenue streams will leverage existing resources and will result in recapitalization of the Highway Trust Fund.

Mr. Martin then discussed some of the specific issues of credit enhancement. The responses to FWHA's TE-045 indicate that different levels of government, in some cases below the State level, are interested in transportation revenue generation by implementing such mechanisms as fees and tolls. Mr. Martin noted that local officials are willing to levy local taxes to complete projects in their districts sooner, rather than waiting for Federal funds (from a national gasoline tax increase, for example). Mr. Martin pointed out that DOT's goal is to assist State and local governments with their new revenue initiatives. There is particularly a need to help those agencies issuing debt for the first time.

Mr. Martin described some credit enhancement tools that DOT is considering. One of the credit enhancement vehicles allows DOT to underwrite local and State debt with subordinate, or junior, loans to ease the risk associated with implementing toll and other user-fee projects. Subordinate loans may be critical during the transition years; further evaluation may indicate that this tool may be more beneficial when targeted toward specific situations or projects.

He pointed out that other credit enhancement tools are needed in the high-risk phase of project construction, such as during the environmental evaluation process. Credit enhancement during the construction stage may also attract private investors to the project. States and local agencies would prefer the bulk of credit enhancement in the riskier initial phases of a project, rather than evenly distributed over the project life. Mr. Martin stated that segmenting the project's construction phase into risk categories will prevent the State from paying high interest charges during low-risk times. This risk segmentation will decrease the overall average interest rate.

Since funding from the Highway Trust Fund is less risky than annual appropriations from other Federal programs, a possible credit enhancement may result from the differentiation of highways from other types of general fund Federal programs. Credit instruments or enhancements, such as bond insurance, can be developed that take advantage of the nature of the Highway Trust Fund. Mr. Martin noted that historically these tools have not been demanded but they could alleviate the current funding constraints. He indicated that different types of vehicles exist to implement greater credit enhancement, such as ISTEA re-authorization and the Baucus and the Borski bills.

DOT has been investigating ways to make issuance of revenue bonds less difficult. Mr. Martin indicated that one way to alleviate the difficulties is to use future trust fund apportionments to secure current credit instruments. He explained that DOT could offer contingent lines of credit for debt service reserves and to help projects through riskier periods. In addition, using these lines of credit may cost less than traditional capital market instruments since DOT has a future trust fund allocation that secures the line of credit. Mr. Martin noted that DOT has also considered taking subordinate loan positions for amounts that, if part of a bond issue, would cause the project to exceed its debt coverage ratio. In this way, he demonstrated that DOT actually promotes the use of revenue bonds over general obligation bonds, without encumbering the issuer with the higher coverage required for revenue bonds. In addition, Mr. Martin believed that issuance costs could be reduced with the mechanism to fund debt service reserves on a contingent basis, possibly after construction.

Mr. Martin noted that DOT is also evaluating State revolving funds for transportation, as proposed by the Baucus Bill. DOT is currently investigating the revolving loan program and its applicability under existing FHWA mandates.

If the authority to create State revolving funds is permitted, the State can be the instrument for providing financing rather than engaging the U.S. Treasury.

Mr. Martin then reflected on outstanding questions concerning credit issues. He posed the question: How can DOT provide lines of credit without providing a loan guarantee, and how can DOT provide financing instruments that maintain the tax-exempt status of a Government issue? He stated that there is existing knowledge of these issues, particularly within EPA and to an extent within FTA, that DOT can use in its discussions of ISTEA re-authorization.

In closing, Mr. Martin stated that the list of general credit enhancements he enumerated was not exhaustive. He reiterated that DOT is looking for input to help develop credit enhancements that provide the greatest benefit. He concluded by thanking the FHWA task force members and noted their hard work in reviewing the 60 projects that were submitted by various states.

Panel on Innovation in Transportation Bonds and Finance

Introductory Remarks

Madeleine S. Bloom, Director, Office of Policy Development, FHWA (Moderator)

Ms. Bloom introduced the third panel by pointing out that no single level of government can address the current infrastructure deficit. New partnerships between the private and public sectors and among different levels of government are required. While traditional grant reimbursement programs remain the core of FHWA's infrastructure assistance, traditional roles are being challenged and expanded. ISTEA's public-private provisions and planning and management systems provide examples of the changing emphasis in infrastructure financing from more dollars to smarter dollars.

Ms. Bloom stated that the third panel would focus on Federal actions that may now, or in the future, improve infrastructure investment. Michael Deich of the National Economic Council (NEC) would discuss Executive Order 12893 on Federal infrastructure, Kathy Ruffalo of the Senate Environment and Public Works Committee would discuss Federal legislation, and Tom McPherson from the Ohio DOT would update seminar participants on the status of AASHTO's task force on innovative financing. Finally, Bruce Cannon and Jerry Poston of FHWA would present FHWA's Test and Evaluation Project.

Panel Presentations

Michael Deich, National Economic Council, White House

Mr. Deich observed that many of the financing methods discussed at this conference still require at least some measure of public subsidy—Federal agencies need to justify to the public why it is in their interest to subsidize infrastructure. In order to further investment goals, he believes that agencies should develop new information that provides measures of how infrastructure contributes to the economy and quality of life.

On January 26, 1994, President Clinton issued Executive Order 12893, *Principles of Federal Infrastructure Investment*, to develop broadly accepted measures of the role of Federal infrastructure in economic growth and to promote more cost-effective Federal investments. Mr. Deich explained that in doing so, agencies are instructed to:

1. Conduct systematic economic analysis of their major investment programs. The order requires agencies to quantify, to the maximum extent possible, programs' costs and benefits and to examine qualitative measures that reflect values not easily quantified;

2. Conduct periodic reviews of management practices including operations and maintenance activities, contracting practices, and pricing policies;

3. Minimize the legal and regulatory barriers to private sector financing, ownership, construction, and operation of infrastructure facilities to promote private sector participation; and

4. Work with States and localities to implement planning and information management systems that can support the first three principles of the Executive Order.

Mr. Deich indicated that the agencies' plans reflect wide differences in their institutional capabilities and in the extent to which their programs' benefits and costs can be measured. He then discussed four programs that illustrate the possible range of final implementation plans.

Mr. Deich observed that the Water Resource program will be able to implement the Executive Order relatively easily as it has been required for years to conduct a cost-benefit study of every project it undertakes. The Highway program is also well-positioned to implement this order because FHWA has been developing a new model designed to place monetary values on the benefits and costs of different highway investment strategies.

In contrast to programs for which both benefits and costs are fairly easy to quantify and monetize, environmental protection programs, such as the Clean Water State Revolving Fund and the Drinking Water Revolving Fund, have benefits that are often intangible. EPA's implementation plan will focus on the effects of the Clean Water Act and will likely outline a multi-year program to study the baseline costs and benefits of the existing Clean Water Act requirements. These monetized benefits will be supplemented by measures of environmental and other non-market benefits that can be quantified but not monetized and other qualitative measures. Transit programs also must measure benefits that are not easily quantified. He expects that FTA will expand its analytic capabilities and begin to work towards true cost benefit analysis of its programs.

Mr. Deich concluded by urging the participants to examine other agencies' activities. Ultimate success will depend on Federal, State, and local agencies working together and learning from each other.

Michael Deich responded to a panel member that although some transit projects may not be justified by economic criteria alone, many of transit's benefits are social which often tend to get lost in the cost benefit analysis.

Kathy Ruffalo, Professional Staff, Senate Environment and Public Works Committee

Ms. Ruffalo began with a brief explanation of the S1714 bill, also known as the Baucus Bill. Introduced in November 1993, the bill focuses on the concept of State revolving loan funds. Ms. Ruffalo explained that, under the bill, States would be allowed to deposit certain portions of their Federal funds into revolving loan funds to be used for direct loans, Interstate subsidies, or bond insurance. In essence, this will allow States to use Federal funds as capital reserves. Upon repayment to a revolving loan fund, these funds loose most of their Federal identity, although they still would be designated for Title 23 transportation purposes. S1714 would also make technical changes to the toll sections of ISTEA and expand some of ISTEA's innovative provisions by allowing nontoll projects to have some of the same advantages as toll projects. This would benefit States in which tolls are not a viable option. Though the bill was not passed by Congress, Ms. Ruffalo believes that it served a purpose by demonstrating Congressional willingness to examine this issue.

She applauded the Administration and DOT for their forward thinking and proposals and urged action. However, Ms. Ruffalo did express some concern regarding DOT's direction. To ensure its support, Congress requires sufficient safeguards that the proposals being submitted are feasible, without high default rates.

Ms. Ruffalo then discussed the appropriations bill for the year. Both the Senate and the House set obligation limits below full funding. With tighter budget caps and controls, the prospects for full funding next year are not good. She indicated that this is partially a result of the continuing large number of demonstration projects that tend to get funded, forcing lower limitations for the formula programs. Demonstration projects are also a problem in the National Highway System bill.

Tom McPherson, Chief Budget Officer, Division of Finance, Ohio Department of Transportation

Mr. McPherson discussed the work of AASHTO's task force on innovative financing. The task force is working to identify the different financing tools available and the successes that have already occurred in a reference document for its members. It is also analyzing the issues and trying to support legislation to make innovative financing easier. Mr. McPherson acknowledged, however, that no single financing tool is applicable or best in every situation; conditions and circumstances will dictate the actions one should take.

In their meetings, members of the task force discussed barriers to implementing ISTEA provisions and ways for State DOTs to reduce the risk of bond financing. They also heard a report on FHWA's initiative to look for financing methods other than the traditional motor fuel tax, including alternative fuel taxes, congestion pricing, and emissions fees. Since their first two meetings, the task force has met with different groups to identify all the tools and their applications. AASHTO will be conducting a survey of State agencies, requesting input on their successes to be included in their reference document.

Mr. McPherson outlined some of the future actions of the task force. After completing the current analysis, AASHTO hopes to identify the barriers to implementing innovative financing of transportation infrastructure and to support any legislation that will make financing easier.

Mr. McPherson closed by recognizing the efforts of FHWA in this process. He believes that this is an exciting time for transportation with many new ideas and many actions that can be taken.

Bruce Cannon, Chief, Legislation and Strategic Planning Division, FHWA, and Jerry Poston, Chief, Federal-Aid Program Branch, FHWA

Mr. Cannon presented some of the lessons that FHWA has learned from its initiative to date. In his introduction, he stated that TE-045 will work because it is fueled by real projects and real ideas from States willing to risk their money and their reputations. The strategies included in the 60 proposals received from 26 States as of July 1 are outlined in Table 1.

Table 1
Concepts Proposed in FHWA TE-045

Toll Financing	16
Matching Variations	24
Income Producing	6
Bonds	14
Partnering	20
Revolving Loans	11
Post-ISTEA Financing	7
Others	32
TOTAL	**130**

Both Mr. Poston and Mr. Cannon gave illustrative examples of these types of projects based on proposals they have received.
Mr. Poston began by describing some theoretical projects involving matching variations. The first example dealt with early reimbursement, i.e., allowing a State's Federal funds to flow at a greater rate than the pro-rata share of the total project to help them in the early stages of the project. The second example involved soft match—a provision of ISTEA allowing a State to use certain expenditures of toll revenues as credit toward the non-Federal matching share requirements on highway projects. Under TE-045, FHWA could allow a State to use credits even if its non-Federal capital transportation expenditures do not exceed the previous three years' average, as the law requires. This could serve as an inducement to accelerate State expenditures on capital transportation investments.

The third example Mr. Poston presented could test the guidance concerning State revolving loan funds. In this example, a State is constructing an intermodal facility—a rail highway interchange—with a public-private partnership and Federal-aid funds. The State would loan the funds to the private partner to construct the facility. The loan would be repaid by fees for cargo transfers. FHWA must decide if a facility like this one qualifies as a highway and if the fee revenues can be considered toll revenue.

After displaying a map of the proposals received, Mr. Cannon illustrated some of the innovative financing features by describing one theoretical highway project in detail. That project would involve the construction of 1,200 miles of freeway in the central region of the country at an estimated cost of $2 billion. Using traditional financing without a coordinated State initiative, the freeway would probably not be completed until 2020 or 2030. If the State decided to use bonds, Federal Reimbursement Anticipation Notes, or a letter of intent by FHWA to reimburse the States on the debt service on those bonds, the payments over the next 25 years would total $4 billion with completion in 2005-2010.

Mr. Cannon then outlined how some innovative financing strategies could be used to construct this highway. The first concept involved the use of public-private partnerships to generate concession revenue. A State could form a partnership to develop rest areas and use the rest area revenues to purchase additional rights-of-way. These could then be leased to private entities, generating State revenue and could thereby reduce Federal and State contributions by 25 percent compared to the bonding scenario above.

Creating partnerships involving the local areas is another way to further reduce the Federal and State participation for bond reimbursement costs. Local governments could contribute to project costs by establishing assessment districts around interchanges, generating revenue from the benefits brought by highway-induced development.

Mr. Cannon also suggested placing toll facilities on the rivers crossed by the new highway. This could reduce the Federal and State participation by utilizing user fees to repay the loan. In addition, the use of Design Build and similar public-private concepts could advance the completion of the project. The final option Mr. Cannon discussed involved a private toll authority's use of State-financed bonds, garnering the tax-free features, and Federal and State letters of credit to enhance the creditworthiness of the bonds.

Using this illustrative example, Mr. Cannon outlined some of the various innovative financing features that could be used on a project drawn from States' proposals. In closing, he observed that some of the more creative proposals reflect an interactive partnership between the private sector and State and local governments to advance initiatives. He added that this partnership may be difficult to advance but has tremendous potential.

Conclusion

Ms. Bloom thanked the panelists and invitees for their participation and valuable contribution. She indicated that FHWA would be publishing the proceedings which would be made available to participants as well as the public.

Appendix A: Agenda

July 20, 1994 • 8:45 - 4:30
Federal Highway Administration
400 7th Street, SW • Washington D.C. • Room 2201

8:45 - 9:00 • Coffee, Registration

9:00 - 10:15 • Opening Remarks — Rodney E. Slater, *Federal Highway Administrator*
• Moderator — Gloria J. Jeff, *Associate Administrator for Policy*
• **Keynote Speakers**
Mr. Howard Yerusalim, *AASHTO President and Pennsylvania Secretary of Transportation*
Ms. Beverly Swaim-Staley, *Director, Office of Finance, Maryland Department of Transportation*

10:45 - 10:30 • **Break**

10:30 - 12:15 • **Panels**

• State and Local Bond Issuers Perspectives (State, Toll Authorities)
• Matters affecting bond issues, credit, and State and regional concerns

• **State Perspective**
Bob Cowans, *Director of Financial Planning, Washington State*
• **Toll Authorities**
Ms. Maureen Gallagher, *IBTTA*
• **Local Perspective**
Eric Tucker, *Finance Director, City of Detroit*
• **Intermodal Perspective**
John Platt, *Assistant Director for Transportation Modes, Ohio DOT*

12:15 - 1:00 • **Box Lunch**
"Partnerships for Investment"
Jane F. Garvey, *Deputy Federal Highway Administrator*

1:00 - 2:45

• Bond Industry State of the Art
• Transportation issues, ratings, insurance

• **Perspective on Current Role of Bonds in Transportation Capital Program: Designing Debt Policy and Selecting Bond Instruments**
John Petersen, *President, Government Financial Group*
• **General Characteristics of Current Successful Issuers**
John Wenderski, *Director of Finance, Prince William County, Virginia*
• **Enhancing Creditworthiness for Transportation Issues**
Steve Martin, *Director of Financial Development, Office of Budget and Programs, OST*

2:45 - 3:00 • **Break**

3:00 - 4:30

• Innovations in Transportation Bonds and Finance

• **Executive Order 12893**
Mike Deich, *NEC, White House*
• **Federal Legislation**
Kathy Ruffalo, *Professional Staff, Senate Environment and Public Works Committee*
• **AASHTO Innovative Financing Effort**
Tom McPherson, *Chief Budget Officer, Division of Finance, Ohio DOT*
• **FHWA Test and Evaluation Project**
Bruce Cannon, *Chief, Legislation and Strategic Planning Division, FHWA*
Jerry Poston, *Chief, Federal-Aid Program Branch, FHWA*

Closing Remarks
Madeleine S. Bloom, *Director, Office of Policy Development, FHWA*

Appendix B: List of Participants

Adams, Charlotte M.
Federal Transit Administration
400 7th Street, SW.
Washington, D.C. 20590

Allen, Paul J.
Ogilvy, Adams, and Rinehart
Suite 300
1901 L Street, NW.
Washington, D.C. 20036

Banks, Kip B.
Committee on Budget
Room SD-618
U.S. Senate
Washington, D.C. 20510

Barrett, David J.
Vice President
Morgan Stanley and Co.
801 Pennsylvania Avenue, NW.
Suite 955
Washington, D.C. 20004

Barton, Michael A.
Commissioner
Department of Transportation and
Public Facilities
3132 Channel Drive
Juneau, Alaska 99801-7898

Basso, Peter J.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Bennett, Nancy
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Bergman, Robert A.
House Public Works Committee
2165 Rayburn House Office Building
Washington, D.C. 20515

Berkshire, Linda K.
ConnieLee
2445 M Street, NW.
Washington, D.C. 20037

Binder, Susan
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Bloom, Madeleine S.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Boffi, Jr., Dante E.
Director
Department of Transportation
2 Capitol Hill, 210 State Office Building
Providence, Rhode Island 02903

Bonine, Larry S.
Director
Arizona Department of Transportation
206 South 17th Avenue, Room 100A
Phoenix, Arizona 85007

Bower, Dwight M.
Director
State of Idaho Transportation Department
West State Street
P.O. Box 7129
Boise, Idaho 83707

Bradshaw, Tom
Managing Director
The First Boston Corporation
55 East 52nd Street
New York, New York 10055

Brown, Greg
Senior Staff Associate
National Association of State Budget Officers
400 North Capitol Street, NW.
Washington, D.C. 20001

Burnett, William G.
Executive Director
Department of Transportation
125 East 11th Street
Austin, Texas 78701

Caldwell, Harry
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Canby, Anne P.
Secretary
Department of Transportation
Bay Road, Route 113
P.O. Box 778
Dover, Delaware 19903

Cannon, Bruce
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

F. Canny, Joseph
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Carlson, E. Dean
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Clawson, David
American Association of State Highway and
Transportation Officials
444 North Capitol Street, NW.
Suite 225
Washington, D.C. 20001

Corbett, Daniel
Transportation Branch
Office of Management and Budget
New Executive Office Building
Room 9208
Washington, D.C. 20503

Crunican, Grace
Federal Transit Administration
400 7th Street, SW.
Washington, D.C. 20590

Cuttrell, John
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Downey, Mort
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Dye, Marvin
Director
Department of Transportation
2701 Prospect Avenue, Box 201001
Helena, Montana 59620-1001

Egan, John
Commissioner
Department of Transportation
1220 Washington Street
The State Campus
Albany, New York 12232

Erickson, Ralph
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Fernandez, Nuria
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Fitzig, Lisa
Senior VP
Kidder Peabody
10 Hanover Square
New York, New York 10005

Flowers, Dan
Director of Highways and Transportation
Arkansas State Highway and Transportation Department
P.O. Box 2261
Little Rock, Arkansas 72203

Garahan, Patrick J.
Secretary
Agency of Transportation
Administration Building
133 State Street
Montpelier, Vermont 05633-5001

Garvey, Jane F.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Gibb, Ken
Co-Director of Municipal Finance
First Albany
6 East 43rd Street
New York, New York 10017

Giglio, Jr., Joseph M.
Chairman, Municipal Group
First Southwest Company
1700 Pacific Avenue, Suite 500
Dallas, Texas 75201-4652

Gillespie, John W.
Managing Director
Public Finance Department
Bear Stearns
1 Federal Street
Boston, Massachusetts 02110

Gilstrap, Jack R.
American Public Transit Association
1201 New York Avenue, NW.
Washington, D.C. 20005

Green, Micah
Public Securities Association
1445 New York Avenue, NW.
Washington, D.C. 20005

Healy, Robert
American Public Transit Association
1201 New York Avenue, NW.
Washington, D.C. 20005

Hochman, Jill
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Holloway, IV, Walter C.
Vice President
First Southwest Company
1700 Pacific Avenue, Suite 500
Dallas, Texas 75201-4652

Howard, Tom
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Hughes, Bill
House Public Works Committee
2165 Rayburn House Office Building
Washington, D.C. 20515-6256

Huheey, Robert
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Hunt, Sam
Secretary
Department of Transportation
1 South Wilmington Street, Suite 154
Raleigh, North Carolina 27611

Imhoff, Peter
Managing Director
Dillon, Read and Company
535 Madison Ave
New York, New York 10022

Jackson, Shelton
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Johnson, J. Chester
Chairman
Government Finance Associates
71 Broadway, Suite 1301
New York, New York 10006

Jones, B.K.
Interim Director
Department of Highways and Public Transportation
Silas N. Pearman Building, Box 191
Columbia, South Carolina 29202

Kane, Anthony R.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Kelly, Don C.
Secretary
Transportation Cabinet
Kentucky State Office Building
High and Cliftin Streets
Frankfort, Kentucky 40622

King, Larry M.
Deputy Secretary for Planning
Department of Transportation
1200 Transportation and Safety Building
Harrisburg, Pennsylvania 17120

Kruesi, Frank
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Lamm, Lester P.
Highway Users Federation
1776 Massachusetts Avenue, NW.
Washington, D.C. 20036

Lauver, Jean
Committee on Environment and Public Works
Suite SD-458
U.S. Senate
Washington, D.C. 20510

Lexton, Michael L.
Managing Director
Lehman Brothers
3 World Financial Center
New York, New York 10285

Lighthizer, O. James
Secretary
Department of Transportation
Box 8755
BWI Airport, Maryland 21240-0755

Link, James
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Linton, Gordon J.
Federal Transit Administration
400 7th Street, SW.
Washington, D.C. 20590

March, James W.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Marchese, April
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Maring, Gary
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Marino, Ronald J.
Vice President, Public Finance
Smith Barney Shearson
1345 Avenue of the Americas
New York, New York 10105

Martinez, Robert E.
Secretary of Transportation
Commonwealth of Virginia
202 North 9th Street, 608/Box 1475
Richmond, Virginia 23219

McCarthy, Jim
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

McConnell, Ted
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

McDonald, George
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

McDonough, Francis J.
Vice President
Municipal Finance Department
Goldman, Sachs, and Company
85 Broad Street
New York, New York 10004

McPherson, Thomas
Chief Budget Officer
Division of Finance
Department of Transportation
25 Front Street, Room 704
Columbus, Ohio 43215

Miller, Charles L.
Secretary
Department of Transportation
1900 Kanawha Boulevard East
Building 5, Room 125
Charleston, West Virginia 25305-0430

Moore, Jr., George S.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Morrison, Sid
Secretary of Transportation
Department of Transportation
Box 47316
Olympia, Washington 98504-7316

Nowak, Patrick M.
Director
Department of Transportation
425 West Ottawa Street, Box 30050
Lansing, Michigan 48909

Patin, Jude W.P
Secretary
Louisiana Department of Transportation and Development
P.O. Box 94245, Capitol Station
Baton Rouge, Louisiana 70804-9245

Patterson, John
Congressional Budget Office
Ford House Office Building
2nd and D Streets, SW.
Washington, D.C. 20515

Petersen, John E.
President
Government Finance Group
4350 North Fairfax Drive
Suite 760
Arlington, Virginia 22203

Phaup, Marvin
Congressional Budget Office
Ford House Office Building
2nd and D Streets, NW.
Washington, D.C. 20515

Placide, Wayne B.
Director
First Southwest Company
1700 Pacific Avenue, Suite 500
Dallas, Texas 75201-4652

Poston, Jerry
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Rapaport, Mitchell
Office of Tax Legislative Counsel
U.S. Treasury, Room 4028
1500 Pennsylvania Avenue, NW.
Washington, D.C. 20540

Reznick, Scott
President
Commonwealth Development Associates
6420 Sherwood Road
Philadelphia, Pennsylvania 19151

Rich, Robert A.
Vice President
J.P. Morgan Securities
60 Wall Street
New York, New York 10260-0060

Roberts, G. Mack
Transportation Director
Alabama Department of Transportation
1409 Coliseum Boulevard
Montgomery, Alabama 36130

Rochlis, Steven
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Ruane, T. Peter
American Road and Transportation
Builders Association
501 School Street, SW.
Washington, D.C. 20024

Ruffalo, Kathy
Committee on Environment and Public Works
Suite SD-458
U.S. Senate
Washington, D.C. 20510

Schenendorf, Jack
Committee on Public Works and Transportation
2165 Rayburn House Office Building
Washington, D.C. 20515

Scheppach, Raymond C.
National Governor's Association
444 North Capitol Street, NW.
Washington, D.C. 20001

Scher, Peter L.
Committee on Environment and Public Works
Suite SD-458
U.S. Senate
Washington, D.C. 20510

Schoelhammer, Paul
Committee on Public Works and Transportation
2165 Rayburn House Office Building
Washington, D.C. 20515

Shackelford, Wayne
Commissioner
Department of Transportation
2 Capitol Square
Atlanta, Georgia 30334

Slater, Rodney E.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Slye, Susan
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Smelkinson, Ira
Vice President
Merrill Lynch Capital Markets
World Financial Center
North Tower
New York, New York 10281-1309

Spencer, John W.
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Frankel Stoll, Louise
Office of the Secretary of Transportation
400 7th Street, SW.
Washington, D.C. 20590

Van Loben Sels, James W.
Director
Department of Transportation
P.O. Box 942873, Room 1100
Sacramento, California 94273-0001

Vidal, Guillermo V.
Executive Director
Colorado Department of Transportation
4201 East Arkansas Avenue
Denver, Colorado 80222

Wallick, Daniel W.
Managing Consultant
Public Financial Management
Two Logan Square, Suite 1600
18th and Arch Streets
Philadelphia, Pennsylvania 19103-2770

Wallick, Ruth M.
Government Finance Officers Association
1750 K Street, NW.
Washington, D.C. 20006

Watts, Ben
Secretary
Florida Department of Transportation
605 Suwannee Street, Mail Station 57
Tallahassee, Florida 32399-0450

Weiss, Michael
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Williams, Carl B.
Assistant Director, Federal Fiscal Plan
Department of Transportation
1120 N Street
Sacramento, California 94273-0001

Williams, Gerry
Federal Highway Administration
400 7th Street, SW.
Washington, D.C. 20590

Wray, Jerry
Director
Department of Transportation
25 South Front Street, Room 700
Columbus, Ohio 43215

Yaksich, Nick
Director, Highway Division
Associated General Contractors of America
1957 E Street, NW.
Washington, D.C. 20001

Young, Carroll
Secretary
Highway and Transportation Department
Box 1149
Santa Fe, New Mexico 87504-1149

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