Chairman Petri, Congressman DeFazio, and members of the Subcommittee, my name is Matthew Garrett, and I serve as the Director of the Oregon Department of Transportation (ODOT). I want to thank you for the opportunity to testify before you about Oregon's innovative approach to funding transportation projects through public-private partnerships.

The Context: Large Needs and Inadequate Revenue

Oregon has turned to public-private partnerships out of necessity. In Oregon, as in so many other states around the nation, there is a massive gap between the needs of the transportation system and our ability to meet these needs with our existing resources.

Oregon is growing rapidly, with a population that has swelled by nearly 40% in the last two decades. As more and more people have moved into places like the Portland metropolitan area, formerly free-flowing highways have become clogged with significant congestion. As the suburbs have continued their continuous outward march, turning quiet towns into cities, new routes and additional capacity on existing highways are needed to bring people from where they live to where they work and to move goods quickly and efficiently. The Portland metropolitan area will add another million people in the next 25 years, and the movement of freight by truck in Oregon is expected to double over the same period. Both of these factors will further increase congestion and impose significant additional costs on businesses that face difficulty getting goods to their destination in a timely manner.

Unfortunately, current revenues are not even close to sufficient to meet these needs. Oregon needs $1.3 billion in additional revenue each year in order to properly maintain and expand the state's transportation system. Oregon's gas tax has remained flat since 1993—the same year the federal gas tax was raised—and over time inflation has taken a significant bite out of both of these revenue sources. The significant additional funding provided to Oregon and other states under SAFETEA-LU because of your leadership is greatly appreciated and will help us make improvements to our transportation system, but it isn't enough to sustain the investments we need over the long-term.

Over the last several years the Oregon Legislature has provided ODOT several funding packages by raising fees on drivers and vehicle owners and bonding these revenue streams for years to come. However, even these significant investments—most of which were focused on preserving or rebuilding aging infrastructure rather than adding capacity— have left many needs unmet. What's more, Oregon has used bonding extensively to pay for transportation improvements, and while further bonding would address current needs, it would leave a large hole in future years that would sacrifice our long-term ability to improve our transportation system.

Looking into the future, as vehicles become more fuel efficient, gas tax revenue will increase less rapidly than vehicle miles traveled, reducing the ability of the gas tax to sustain adequate financing of transportation. And rapidly rising construction costs and the effects of inflation over time mean that even modest increases in transportation funding will buy less.

Oregon Innovative Partnerships Program

This large gap between transportation system improvement needs and our ability to pay for them has led Oregon to look at innovative financing sources as a way to fund highway construction.

As they say, necessity is the mother of invention, and in our state of need we are being quite inventive. Oregon was the first state to enact a gas tax, and with our Road User Fee Pilot Program getting underway this year we are the first to take a serious look at moving toward a per-mile tax, which would help keep revenues from falling off as cars become more fuel efficient.

We are also in the early stages of exploring the possibility of financing transportation improvements through public-private partnerships and tolling. In 2003 our Legislature enacted the Oregon Innovative Partnerships Program to allow new, cutting edge approaches to funding and financing transportation projects. This law directs ODOT to focus on innovation, speed and partnerships with private sector firms and other units of government; another goal—leveraging private sources of capital—was also at the front of the Legislature's agenda. In a separate piece of legislation, the 1999 Oregon Legislature directed ODOT to examine tolling as a way to help finance new capacity on highways.

Oregon's Innovative Partnerships Program allows ODOT to enter into partnerships with private-sector businesses and government agencies to study, design, finance, construct, operate, and maintain critically needed transportation projects. The involvement of private sector partners in early planning stages allows for the identification of design, construction, and funding innovations that help the state deliver transportation projects quickly and more efficiently. Oregon's efforts are unique in bringing the private sector into this process so early and so deeply.

Our Innovative Partnerships Program encourages our partners to consider flexible financing options for infrastructure projects, including private-sector funding, lease-back tolling operations, special improvement districts, and federal and state bonds. Although tolling is by no means a foregone conclusion, it is emerging as the most likely way to finance the large projects under consideration. In one scenario, ODOT might negotiate a contract with a private firm under which they will build and operate a highway under a long-term private concession that will allow them to collect tolls on the facility.

Oregon's public-private partnership efforts are focused on using tolls or other financing mechanisms to expand highway capacity. Unlike some other states, we have not proposed leasing existing routes to generate revenue for other projects. However, our private sector partners are considering options for tolling existing routes in addition to tolling new capacity. This might be done because drivers may not use a toll road if a free alternative exists. This approach may help raise enough revenue to cover project costs, while tolling only a new route might leave a significant funding gap. We are sensitive to concerns about this idea, however, and are looking at ways to minimize the impact. This could involve tolling only through traffic and trips leaving the area, without charging purely local travel. Significant discounts could also be offered for local residents.

Turning to the private sector has numerous benefits. Working with the private sector can streamline the study, design, funding and construction of transportation projects and achieve cost and time savings by engaging the innovations, efficiencies and technologies unique to the private sector. During the project development phase the private sector is able to allocate human and financial resources as necessary to move a project forward and can quickly bring tremendous

resources to bear to solve problems; due to budget constraints the public sector is less flexible in its allocation of resources.

In addition, the private sector brings the ability to access a tremendous amount of private capital more effectively than the public sector can. Access to private equity capital is important to be able to make toll road projects work in Oregon. While both the public and private sectors can do debt financing by issuing bonds, only the private sector can secure equity financing by selling stock. Bonding for tolling projects, whether secured by a public entity or private sector firm, is likely to be subject to a significant discount due to uncertainty about tolling revenue. Such a financing discount may yield too little capital for the project to be built by bonding alone. By adding private equity capital to the financing, the private sector may be able to bridge the gap and yield enough financing for the project to be constructed.

However, even in turning to the private sector we are not giving up the government's role as guardian of the public interest. Under this program, ODOT will retain control over the ultimate direction of the project. ODOT will make all final decisions and will conform to strict environmental and land-use regulations and be sensitive to the needs of the communities the projects serve. What's more, the cost efficiencies of these projects won't come on the backs of laborers. Even though the private sector will be doing the bulk of work on these projects, prevailing wage and overtime requirements for construction workers will remain in place.

Projects Under Consideration

The Oregon Innovative Partnerships Program identified three significant transportation projects as possible public-private partnership projects: the Newberg-Dundee Bypass, the Sunrise Corridor and the I-205 South Corridor Improvements. The three projects were selected because they have the potential to significantly relieve traffic congestion in the communities where they would be built, and because there is currently no way to fund their construction, which would cost well over $1 billion.

Newberg-Dundee Bypass

The 11-mile Newberg-Dundee Bypass is located on the south side of the towns of Newberg and Dundee. The Bypass will provide relief from rapidly increasing truck and commuter congestion on Highway 99 that plagues the hearts of these communities and negatively impacts freight mobility. Traffic on this route is expected to increase from approximately 35,000 vehicle trips a day to as many as 56,000 over the next 20 years as these communities that lie just outside the Portland metropolitan area see significant growth.

Sunrise Corridor

The Sunrise Corridor is a proposed new highway corridor that would serve an area that was recently absorbed into the Portland metro area and provide a direct connection between I-205 and US Highway 26, two important routes. Two separate sections of the proposed corridor have been discussed over the years and are currently in different phases of planning. A new six-lane, limited access highway stretching five miles along the OR 212/224 Corridor east of I-205 would address the traffic congestion and safety problems in the Corridor. The Corridor currently carries more than 60,000 vehicles per day, and trucks generate more than 12% of this traffic. The Sunrise Project is currently the subject of a Supplemental Draft Environmental Impact Statement

(SDEIS) that will be completed in late 2007. Development of a new four-lane, limited-access parkway stretching eight miles further east along the Highway 212 Corridor would extend the Sunrise Project to serve the newly incorporated City of Damascus and surrounding areas and provide an improved connection between I-205 and Highway 26. This area was recently brought into the metro region's Urban Growth Boundary and is expected to absorb several hundred thousand new residents of the Portland area in the next few decades.

I-205 South Corridor
The I-205 Corridor is a 25.5-mile-long, north-south freight and commuter route in the Portland metropolitan region. Development over the past decade, particularly in the south metropolitan area, has increased traffic volumes significantly. The transition from six lanes to four lanes at the Willamette River crossing in the south portion of the Corridor contributes to significant traffic congestion. A study is underway to identify needs and potential innovative solutions in the I-205 Corridor, including additional lanes in each direction and improved interchanges.

ODOT issued a Request for Proposals (RFP) for these three projects last spring. The RFP sought private sector interest in a two-phase contracting process. The first contract is for "pre-development" services to bring the project to the point it can secure private sector financing. By satisfactorily completing and delivering the work tasks under the contract so that the projects are demonstrated to be technically and financially feasible and acceptable to the public, the private partner would earn the exclusive right to enter into negotiations with ODOT on the "implementation contract" to actually build and perhaps operate and maintain the new facilities.

ODOT received proposals from two firms on Newberg-Dundee and one each on South I-205 and Sunrise. ODOT began an extensive evaluation process that involved internal and external experts and consultation with local government representatives. The proposals were evaluated on the qualifications and experience of the proposers; their approach and understanding of the project; their plans for gaining public support for the project; and the proposed compensation arrangements.

Oregon Transportation Improvement Group
The ODOT evaluation team unanimously invited the Oregon Transportation Improvement Group (OTIG) to interview, as the top ranked proposer on all three projects. OTIG is a consortium of companies with extensive experience and long histories of success in the financing, design, engineering and operation of state-of-the-art transportation facilities. OTIG is led by Macquarie Infrastructure Group (MIG), based in Sydney, Australia. Macquarie is one of the largest public infrastructure companies in the world and is traded on the New York Stock Exchange. Macquarie's technical advisor is Hatch Mott MacDonald, an engineering consulting firm with 33 offices across North America and staff resources of 12,000 worldwide.

The group was chosen because of its significant U.S. and international experience financing, developing and operating high-quality transportation facilities; its ability to fund the projects up front; its willingness to assume the financial risk for the timely construction and successful operation of the three projects; and for a proposed 30% reduction in costs if awarded all three projects.

ODOT is currently working with OTIG in a pre-development phase to evaluate the financial and technical feasibility of various options for building the projects through a public-private partnership. Activities undertaken during this phase will allow OTIG to make informed decisions regarding whether to go forward into the implementation phase. During the next year, OTIG will work side by side with ODOT and local communities as they investigate the feasibility of the projects. Coordination with local agencies will also address the need to study the projects in the local and regional contexts. No decisions have yet been made about when, or even whether, they might be built.

OTIG has agreed to bear the cost of conducting the pre-development studies, but ODOT will be required to reimburse these costs if ODOT or OTIG decide not to proceed with a project; none of OTIG's pre-development costs will be reimbursed if the projects move successfully into implementation. The total pre-development costs for the three individual projects are estimated at over $26.5 million, but ODOT's potential reimbursement is capped at $20 million. The recently approved contract includes several escape clauses that either party can use if predevelopment work shows the projects to be financially or technically infeasible.

If the pre-development work demonstrates that the projects are technically and financially viable, OTIG will have exclusive rights to enter into negotiations with ODOT to implement the projects. OTIG has proposed to finance, construct and operate these new facilities as toll facilities for a period of years that has yet to be negotiated. For a number of the early years, these projects are projected to operate at a loss. OTIG would operate the new facilities in exchange for the right to receive a return on its investment in the later years of its lease term.

An implementation contract would offer OTIG a long-term concession of a negotiated length, during which time OTIG could collect the tolling revenue. This contract would specify exactly how the private sector would build, operate, and maintain the facility. For example, the contract could specify certain arrangements to ensure safety and security; could set appropriate toll levels; and would set standards for operation and maintenance of the facility to ensure that OTIG would operate a quality highway and turn it back to the state in a good condition.

Although OTIG will have the first shot at securing the implementation agreement, ODOT will have leverage in these negotiations because the state is not absolutely locked into contracting with OTIG to build these highways. ODOT is required to conduct good faith negotiations, but if we are not able to secure an acceptable agreement, we have the right to walk away and sign a contract with a different firm after a one-year waiting period has passed.

If the projects move forward, OTIG has agreed to conduct a competition for design and construction, ensuring that Oregon will receive the highest value on its investment. OTIG will function as a developer of any projects that are built, but it is not a construction company. OTIG would request proposals for design and construction of any projects that might be built under the program, thereby opening up millions of dollars in projects for construction companies along with hundreds of well-paying construction jobs.

Newberg-Dundee Bypass Feasibility Review

The Newberg-Dundee Bypass is the farthest along in this process, making the project the test case for whether a public-private partnership can move forward and succeed. ODOT has already selected a corridor for this project and received a record of decision on a location Environmental Impact Statement (EIS) from the Federal Highway Administration; the two other projects under consideration have not reached this point in the environmental review process.

OTIG recently released a Summary Feasibility Review for the Newberg-Dundee project that indicates that highway tolling would be the most financially viable source of funding the Bypass. There are a number of tolling options available and a number of traffic and revenue variables that require further study before any firm conclusions can be reached. A more detailed study of these variables will be conducted over the next three to four months.

OTIG will be exploring two general tolling options: tolling only the Bypass and access tolling. Access tolling would toll all traffic passing a point on the corridor regardless of the route it takes. OTIG's preliminary analysis indicates that tolling only the Bypass may not generate enough revenue to pay for the project, leaving a large funding gap that the public would have to bridge using unidentified resources. Moreover, leaving the existing route untolled would encourage people to use the existing route to escape the toll, reducing the congestion relief provided by constructing the Bypass.

Under access tolling, cars taking either route would be tolled as they pass a point on the existing highway on the north end of the corridor prior to the Bypass. This option would toll all through traffic using either route as well as local residents leaving or entering the region on the corridor. However, the option OTIG is exploring will likely leave purely local traffic that stays within the region free—even if it uses the Bypass—and it would likely provide a discount for local residents who take the corridor to and from Portland. OTIG's early analysis indicates that this option might provide adequate funding for building the Bypass without requiring significant investment of additional public resources. Allowing cars to use either route for the same fee would also maximize congestion relief.

It is important to note that this is an early assessment of the project's feasibility and is not a formal proposal. OTIG will continue its research over the next several months and will likely release its final review by the end of this summer. At that point we will know under what conditions, if any, a public-private partnership will be feasible for this project.

Conclusion

While this pre-development phase is designed to determine the technical and financial feasibility of these projects, one of the most important outcomes of the process will be determining public support for tolling, which is not common in Oregon. ODOT and OTIG cannot and will not move forward with projects that do not have public support. If the public indicates that it will not support the construction of a toll highway, we will not proceed with a public-private partnership. Unfortunately, given the challenges of financing these projects, that decision could mean that the projects will be faced with many years of uncertainty as to when financing might be made available.

Although we are still in the relatively early stages of exploring the use of public-private partnerships on these three projects, we are moving ahead quickly to determine whether this new approach could be put to use. With funding levels inadequate to pay for the major expansion of our transportation system that is needed to meet current and future challenges, we must look to new and innovative ways of doing business that hold promise for delivering important projects. We do not expect that public private partnerships will become the only or even the primary means of paying for projects that increase highway capacity, but if our experiment proves successful they could add another tool to our highway funding toolbox and help us deliver important projects that otherwise might not materialize.