

Summary: “Leveraging Federal Funding: Innovative Solutions for Infrastructure”

Senate Committee on Environment and Public Works Subcommittee on Transportation and Infrastructure

Witnesses:

- The Honorable Eric Garcetti, Mayor, City of Los Angeles. Chair, U.S. Conference of Mayors Infrastructure Task Force
- Tim J. Gatz, Executive Director, Oklahoma Turnpike Authority
- Geoffrey S. Yarema, Partner, Nossaman LLP
- Kevin DeGood, Director of Infrastructure Policy, Center for American Progress
- Aubrey L. Layne Jr., Secretary of Transportation for the Commonwealth of Virginia.

Opening Statements

Subcommittee Chairman Inhofe (R-OK) opened the hearing by noting that last Congress the EPW Committee led a successful effort to pass the Fixing America’s Surface Transportation (FAST) Act but added that current investment levels are not enough. The U.S. Department of Transportation (USDOT) reports that there is over \$800 billion in backlogged projects. He noted that any new infrastructure bill will most likely include items beyond roads and bridges. He urged state departments of transportation (DOTs) and local governments to prioritize transportation and to work to meet modest matches of federal funding.

Subcommittee Ranking Member Cardin (D-MD) said the U.S. has neglected its infrastructure and that public investment has not kept up with need. He urged Congress and the Administration to explore new funding models and partnerships but emphasized that public investment must lead any effort. He called for more flexibility for cities in decision making and asked that Mayors be given more tools to help improve infrastructure.

Full Committee Ranking Member Carper (D-DE) said that, as a governor, he thought about the issue of infrastructure extensively and that he believes it is a bipartisan issue. A central role of government is to provide a nurturing environment and infrastructure is crucial to that end. He encouraged empowering public entities to work with private companies to meet our infrastructure needs, as the private sector can play a crucial role in improving national infrastructure. However, while public-private partnerships (P3s) are a useful funding model, they are not the only answer. Ranking Member Carper said P3s are not useful for routine maintenance projects and those of critical safety; but better suited for large, complex projects. Moreover, many states do not allow for P3s all together. The Ranking Member noted there is no silver bullet for infrastructure, but many potential “silver BB’s” that together can provide a solution.

Mayor Garcetti was excited when he first heard infrastructure discussed during the Presidential election. Municipal level civil servants agree that investment in infrastructure is possible and should be done. He told the Subcommittee that in November 2016, Los Angeles passed a \$120 billion package at the local level to improve local roads, transit and infrastructure. Mayor Garcetti said that he has had

policy successes by using the Infrastructure Incentives Initiative (I3), developed by the U.S. Conference of Mayors. The I3 consists of leverage, thinking about the life of projects, and using innovative technology. He encouraged its usage at the federal level as well and promised to support a large infrastructure proposal from the federal government. The Mayor concluded by saying that there is no better thing the U.S. can do for jobs and quality of life than to invest in infrastructure. He noted that American cities are already working to make improvements and urged the Federal government to help as well.

Mr. Gatz has been involved in the planning, construction and maintenance of Oklahoma's transportation system and infrastructure at many different responsibility levels since 1990. The conditional deficiencies of a long underfunded national transportation system cannot be resolved by the States alone but instead require federal investment and a long term national transportation improvement strategy. Mr. Gatz encouraged federal investment as well as the use of P3s. He urged tolling to be recognized as a viable, long term and sustainable transportation revenue mechanism to address transportation system needs and help fund infrastructure investments. He noted that the U.S. has a funding crisis that must be jointly met by state and federal partnership. Long term, consistent federal funding remains vitally important to the development and delivery of transportation improvement projects. Mr. Gatz called for new innovation to address the increasing transportation challenges.

Mr. Yarema began his opening statement by urging the U.S. to provide a significant supplement to existing federal infrastructure funding in order to remain the leader of the global economy. He then shifted his focus to the equally important question of how to spend new discretionary funds in the most impactful way possible. Congress and the Administration can achieve a paradigm shift and create lasting impact through his Infrastructure Incentives Initiatives, or "In3." In3 would expend new discretionary resources to: 1) Create significant leverage by incentivizing infrastructure owners to secure and commit their own revenue measures, bond programs and project revenues well beyond traditional federal-state funding splits; 2) Assure long term performance of projects by incentivizing infrastructure owners to avoid deferred maintenance and instead create lifecycle cost efficiencies through outcome-based standards; 3) Modernize business practices by incentivizing infrastructure owners to update outdated policies and project delivery approaches to better reflect 21st Century models, including P3s, and to capture the best of private sector capabilities; and 4) Incorporate new technology by incentivizing infrastructure owners to design projects in ways that are innovative. In practice, Mr. Yarema said the federal government would use new funds to create a discretionary program that rewards and assists non-federal project sponsors in achieving the four outcomes identified above. These new funds would be allocated towards programs of projects, not individual projects. For programs that receive funding, money would be contingent upon the project sponsor achieving the progress benchmarks outlined in their application. Mr. Yarema also called for changes to environmental review and permitting processes increases in the TIFIA program, removal of the cap on private activity bonds, tax incentives, and reduction of oversight burdens on state and regional governments.

Mr. DeGood began his statement by saying that P3s are not a means to overcome the infrastructure gap and instead posited that insufficient tax revenue is the binding constraint of local governments, not a lack of financing. He said that the President's campaign plan, which was centered on tax credits for private companies, would not solve the infrastructure gap but would increase the deficit. The

Administration's tax credit centered plan would undermine the purpose of investing, due to the expensive nature of equity capital. P3s are often thought of as a way to get capital off the sidelines, inferring capital scarcity. Instead, Mr. DeGood noted that the municipal bond market is robust and the TIFIA matching program offers low interest funding for local governments. He argued that the true value of P3s is risk transference, putting the burden on private entities to deliver projects on time and on budget. He clarified that the challenge of the public sector is negotiating a risk-adjusted price for services. Another peril of P3s is contractual limitations and long term binding language that protect private interests while limiting municipal governments. He closed his statement by acknowledging there is no shortcut to rebuilding America's aging infrastructure. Federal funding should be targeted to communities facing the greatest need and highest level of economic hardship.

Secretary Layne acknowledged that P3s can be a useful tool to advance large-scale projects or a package of projects. However, they are not the silver bullet to solve the bulk of transportation needs a state faces. Infrastructure deals are large complex entities that require strict negotiation to avoid pitfalls, including long life terms and costly concessions from local governments. P3s require understanding of both parties' interests and finding the alignment where a deal can be made. The Secretary strongly encouraged Congress to be careful of the pitfalls he mentioned, but acknowledged the potential P3s hold to help close the infrastructure gap.

Question & Answer:

Subcommittee Chairman Inhofe asked Mr. Yarema to respond to attacks on P3s and their use. **Mr. Yarema** answered that P3s require the right circumstances and are valuable to both urban and rural areas; but there is too little understanding of their use and the circumstances they require to be useful. In particular, Performance Contract P3s, without payment venues like tolls, are akin to a warranty. They require no payment until the project is finished, insuring performance as private companies are only repaid according to performance against the set standards laid out in the contract.

Ranking Member Carper recently met with and asked the Secretary of Transportation how she believed transportation projects should be funded. He asked the panelists what advice they would give her. **Mr. Gatz** advised the Secretary to keep all options open and to be innovative in exploring opportunities. **Mr. Yarema** answered that the Secretary should keep existing programs and funding in place, should invest \$100 billion of the proposed \$200 billion in funding into surface transportation projects, and should create an Infrastructure Incentive Initiative to leverage funding. **Mr. DeGood** said that if a person uses a service, they should help pay for its upkeep and maintenance. His advice would be that a user fee system works. **Secretary Layne** called on USDOT to help states develop a better understanding of development and use of P3s. He also recommended that outcomes drive funding and repayment.

Senator Deb Fischer (R-NE) asked Mr. Yarema to speak to performance based standards and their use. **Mr. Yarema** answered by saying projects are set with explicit expectations; these standards are then the measurement tool for how a project is evaluated. Standards are contractually binding; meaning payment is dependent on performance. Mr. Yarema believed this insures results and quality projects for states and local governments.

Senator Tammy Duckworth (D-IL) asked what financing opportunities are best suited for rural areas. **Mr. DeGood** answered that the use of urban and megadollar P3 deals can benefit smaller communities by freeing up federal dollars. He urged any federal infrastructure plan to include set aside dollar amounts that account for the unique needs and challenges of rural areas.

Senator Sheldon Whitehouse (D-RI) asked Secretary Layne what red flags he looks for when exploring a P3. **Secretary Layne** answered that it often comes down to risk. To mitigate risk, states must understand fully their infrastructure needs and project costs, and analyze the costs and benefits of paying a private entity for their services.

Ranking Member Cardin asked Secretary Layne if he believed that tax incentives from federal governments, encouraging P3s negotiated by states, or limitations put in place by the federal government on states negotiating those deals would be helpful. **Secretary Layne** did not agree but instead thought that private companies would find a way to exploit tax credits. He said private companies already see the opportunity to work with state and local governments and therefore need no further incentivizing. **Ranking Member Cardin** asked how the federal government could incentivize life cycle maintenance. **Mr. Yarema** proposed contractual obligation of life cycle cost by private entities in P3s.

Chairman Inhofe adjourned the hearing.