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RE: PA Transportation Funding Testimony

6-24-2010

Dear Rep. Markosek:

Your opinion regarding transportation financing was recently published in the Allentown Morning Call here- http://www.mcall.com/opinion/yourview/mc-markosek-geist-transportation-fund20100619,0,6811252.story

I was unable to attend any of your transportation funding hearings across the state, but would like to submit the following informal testimony for your consideration. If it is of further interest, please feel free to contact me at your convenience.

Sincerely,

Daniel Lee Van Epps

Daniel L. Van Epps

ISSUES TO CONSIDER
FOR THE STATE OF PENNSYLVANIA TRANSPORTATION FUNDING
6-24-2010

Daniel L. Van Epps

The following are select issues and potential solutions regarding Pennsylvania's transportation issues.

PA's Interacting Distribution Modes

The State of Pennsylvania likely has the following modes of transportation- Airways; Roadways (Tollways, Freeways, Secondary Roads, Streets); Railways (Large Class I's, Medium and Small Class II's & III's); Pipelines; Shipping (Riverways, Seaways); Trails; Public Transit; Others (Tramways, Canals?).

Modal Business & Governance Model Differences

Transportation systems consist of providers offering rights of way and/or infrastructure and/or facilities, and/or carriage service. These functions may be owned and/or operated by government agencies, private corporations, or third parties as non-profits or for-profits. The accounting methods may be closed-loop (all project revenues offset only project expenses), subsidized (grants or loans from other non-related projects), or cross-subsidized (a railroad cross-subsidizing one of its unprofitable rail line segments from a more profitable one). Some modes are more technologically efficient than others, in addition to other factors including energy consumption, pollution, land use, etc. The complexity in the various business and governance models across each mode of transportation inhibits ideal standardization that causes differences and increasingly leads to problems.

Intermodal Traffic Shifts

A prime example of those problems is traffic shifting among modes. Private railroad companies are currently trying to capture more trucked freight. They are the modal choice for long-haul shipments in corridors served by rail, and are coordinating with large trucking companies to carry their trailers and containers in bulk volumes. This squeezes out smaller trucking-only companies except for time sensitive and other special shipments especially to and from sites not served by rail. Now railroad companies are increasingly competing for medium-haul shipments with the support of numerous government agencies and the public to relieve congestion on roads and highways. Conrail once received subsidies from PA and other

states to increase clearances for intermodal traffic, and now CSX and Norfolk Southern are receiving similar commitments for double stack intermodal clearances. While laudable to relieve highway congestion and save its infrastructure from wear and tear, those tollway, freeway, road, and street providers are not compensated for subsequent traffic losses to the private railroad companies to retire their bonds, conduct regular maintenance, engage in major capital expenditure projects, etc. Remaining roadway users must then be asked to increasingly finance those systems.

On another front, telecommunications and its applications such as email, chatting, and videoconferencing is increasingly competing against transportation providers for certain traffic types such as personal travel and others that can be digitized and distributed online including letters, magazines, newspapers, advertising fliers, videocassettes, CDs, DVDs, etc. Note the many problems USPS is having vs. the Internet regarding first class mail and advertising. PennDOT is apparently leasing its rights of way to private telecommunication providers to host their infrastructures, thereby exacerbating the shift.

Public-Private Partnerships and Privatizations

PPPs and privatizations commoditize public assets that often were originally constructed and subsequently maintained with public funds. Changing public transportation systems to the PPP/privatization model merely lowers employees' wages, decreases their benefits, and de-organizes labor, but increases regulatory costs over the new private sector providers that are free from the risks of financing and constructing those systems. An example of the regulation necessary is a private tollway concessionaire also owning a trucking company that could cross-subsidize the two operations, or give its trucking company discounts and other benefits vs. third party trucking companies operating on the roadway. That scenario is equivalent to the real world private monopolized railroad and pipeline companies, although the private railroads are currently facing re-regulation and loss of their anti-trust exemption in Congress in favor of forced open access to better promote competition.

PPPing/privatizing public transportation systems gives concessionaires virtual assets (i.e., long term leases considered by financial analysts to be assets) and private sector owners real assets for their portfolios useful for future mergers and acquisitions that can yield them significant profits. The state does not benefit financially from those M&A transactions.

PPPed/privatized public transportation systems create competition with adjacent public transportation systems – again two different business and governance models competing vs. being standardized with each other. A past Merrill Lynch conference call discussing the benefits of PPPing public toll roads featured

an official from Australia's Macquarie Bank (part concessionaires of the PPP'd Indiana Tollway) stating they seek PPP candidate systems in corridors with low demand elasticity – it is more efficient for users to use the PPP system than to use the public system due say to higher speeds, less traffic lights, etc. Apparently some concessionaires were pushing for new state laws and other regulations to force users to use their PPP systems vs. the public systems.

Wall St. Financiers

Not much has to be elaborated upon regarding these banks' and investors' fraudulent schemes that include Collateralized Debt Swaps (affecting various PA governments, the PA Turnpike Commission, UPMC, etc.), Interest Rate Swaps, shorts betting against governments and companies to succeed, wealth management Ponzi schemes, etc. Other banking games yet to be discovered could affect not only public and private transportation system providers but also carriage service providers, shippers, and end users too. It should be quite obvious now that these large financiers are only looking after themselves and their shareholders, and not their customers.

Not highly publicized though equally important are Net Debt Service Coverage Ratios required by debt ratings agencies to achieve and sustain a government agency's debt rating. While ratios for small commercial businesses may be around 125% revenues:expenses, the Ohio Turnpike Commission has had to raise theirs to 200% to maintain their nearly top rating during certain capex revenue bond-funded projects. These inflated revenues to supposedly protect bondholders adequately are generally achieved by raising toll rates. However too high tolls risk tollway users migrating to public roadways, though that does not seem to be of concern to the debt rating agencies. PPP and privatization concessionaires may be waiting in the wings to acquire these high-debt/high risk systems and could cut backroom deals with financiers to help acquire and jointly profit from them. Berkshire Hathaway ignores debt ratings when analyzing its investments and instead conducts its own homework, raising the question why bond issuers need to acquire (and finance) ratings at all. (Interestingly Berkshire Hathaway owns 19% in Moody's, and provides bond insurance through one of its subsidiaries.)

Even financial representation should be questioned. At a past Ohio Port Authorities Council meeting, executive directors discussed the need to retain multiple bond counsels as a check on the primary bond counsel to eliminate any bias in favor of the bondholders, underwriters, etc., which some port authorities had apparently experienced.

Other Potential Tollway Problems

One rationale for merging PennDOT and PTC has been the potential savings in construction, maintenance, and other costs. In Ohio, even though ODOT is a department and OTC is an independent agency with differing business and governance models, they are both exploring cooperation in joint materials purchases that can save additional costs when acquired in greater bulk, and both petitioned the state to examine the recent pricing power by road salt providers, resulting in better savings in subsequent years. OTC is also utilizing the State of Ohio Department of Administrative Services' Cooperative Purchasing Program to acquire maintenance vehicles and possibly other supplies. Minnesota and Wisconsin were apparently teaming up for road salt purchases. Thus inter-agency cooperation and "Regionalism" can be viable alternatives to mergers and consolidations to preserve different business and governance models.

Most tollways are likely guilty of gas tax double-dipping. This is where users who purchase gasoline at stations located off of the tollways then use the tollways and consume the gas there, effectively subsidizing non-tollway roads and highways during their tollway use. PTC, the state, US DOT, and the IRS should explore a program to authorize tollway users to redeem their toll receipts on their income tax returns for reimbursement based upon the average vehicle type gas consumption per mile. Satellite-based location and tolling being analyzed in Oregon may be an alternative to gas taxes.

Some tollways give large users volume discounts on their fleets' tolls. Theoretically there should be no discounts in a closed-loop accounting system as each user pays their fair share for the wear and tear they cause and the administration required. Adam Smith observed the following regarding tolled roads in his "The Wealth of Nations" (Book V, Chapter 1, Part III, Article 1):

> "When the carriages which pass over a highway ... pay toll in proportion to their way to or their tunnage, they pay for the maintenance of those public works exactly in proportion to the wear and tear which they occasion of them. ... This tax or toll, too, though it is advanced by the carrier, is finally paid by the consumer, to whom it must always be charged in the price of goods. As the expense of carriage, however, is very much reduced by means of such public works, the goods, notwithstanding the toll, come cheaper to the consumer than they could otherwise have done; their price not been so much raised by the toll, as it is lowered by the cheapness of carriage."

A lingering problem is how to fairly assess tolls to address variable costs (i.e., roadway wear) vs. fixed costs (i.e., administration). Light vehicles inflict almost zero weight damage to well-constructed roadways compared to trucks,

but those users should contribute to other administrative costs nonetheless.

Regarding variable cost assessments, OTC recently changed its tolling assessment from tons-mile to axles-mile, noting that unlike say a railroad train car that has a balanced load weight across all of the car's axles, a truck-trailer combination has different load weights per axle. Still that methodology may not assess heavier axles more than lighter axles, and lighter trucks are assessed the same toll as heavier trucks for the same type of truck/number of axels. The exact formula for determining tolls considering weight, axels, distance, etc., vs. more precise wear and tear they inflict and the costs to repair them should be open for further investigation.

Although retrofitting a freeway to a tollway may be feasible in theory, constructing tollbooths and controlled entrances and exits may incur costs and be problematic especially in tight urban areas where requisite land acquisition is limited and potentially neighborhood-splitting. Some freeway entrances and exits might have to be closed, potentially inconveniencing travelers and businesses catering to travelers at those sites. (Nonetheless it could also be argued that there might be too many entrances and exits on freeways that require additional costs to maintain.)

Misunderstandings by the public regarding the business and governance models of tollways and freeways can inhibit changes and spread problematic misinformation. Many complaints are that tolls are really taxes, and that once the freeways and tollways were paid for they were thereafter supposed to be free of charge. Transportation system providers need to better explain the constant need for maintenance, future capex's, and administration costs. For example: Infrastructures are not perfect and do not last forever – Mankind and Mother Nature continually inflict wear and tear upon them, and only Mankind is going to maintain them else have Mother Nature reclaim them.

Other Potential Solutions for Investigation

Multiple state tollway main line

A multiple state tollway such as I-80/I-90 under a sole administration comprised of officials from member states could better standardize financing, tolls, construction, administration (including resource sharing, purchasing, debt ratings, and collateralizing powers), etc. than individual states providing a tollway segment alone. Note the proposed multi-state Ohio River "Marine Highway One" barge advocates are lobbying for.

Tollways administering multiple transportation modes

PA and other Northeast and Midwest states have lost 50% of their rail line routes, and even more in route capacities (i.e., multiple track main lines being reduced to single tracks) that now cause rail network congestion, restrict efficient traffic routing, and increase the risk of contingencies. PA and other states subsidize private railroads that as aforementioned shift traffic to rail at the expense of publicly-financed transportation systems. Tollway providers should be authorized to construct, acquire, and restore rail lines and administer them like highway tollways without engaging in carriage service against private sector providers. This model would relieve private railroad companies from owning and maintaining systems (like the trucking industry does), and promote badly needed competition in the rail industry. Users could then determine the choice of infrastructure(s) desired for their goods and personal carriage, and traffic shifts among modes under the same administration could be better accounted for.

Toll all PA Interstates

Apparently at a recent hearing one suggestion was to toll all of the state's Interstate highways, and use other funding methods to finance secondary roads, streets, public transit, etc. The suggestion would standardize at least all of the limited access Interstate highways and tollways under one model. Gas taxes (minus the double-dipping), licensing fees, etc., could then be used for the more openly accessible secondary roads and streets, and not have to compete for funding with the tolled roadways. The measure might help reduce other states' gas taxes subsidizing PA's roads and highways, with PA receiving 113.3% more in gas taxes back from the federal government than it pays in.

State banks

Even though the federal government bailed out many Wall St. investment banks, they are still rationing the investments they do make together with higher interest rates and tighter terms and conditions. Although PennDOT has a state infrastructure bank to help finance select transportation projects, perhaps the state should establish the "Bank of Pennsylvania" like the state of North Dakota did with their "Bank of North Dakota". The state bank could concentrate upon financing major capex projects perhaps with revenue bonds and at better interest rates and other terms and conditions. There may be opposition to the

state engaging in the financial sector, though the bank could be restricted to financing only its political subdivisions, but likewise the state cannot be held hostage by Wall St. anymore particularly when they've been betting on the state and its subdivisions to fail.

Fraud vigilance

The state must insist upon and pursue transparency not only at PennDOT and PTC, but with their suppliers in terms of prices, product quality, work quality, conflicts of interest, etc. We cannot afford more Big Dig fiascos that contribute to the austerity much less going concern of the state. The state transportation agencies need sound, trusted individuals dedicated to their employment who need not be babysitted as risks.

Stakeholder voices

Users and those with other interests in bettering transportation systems should have more opportunities to provide feedback and ideas to system providers. Your hearings are a good start, although we cannot wait for a crisis to happen before having hearings. Likewise, transportation providers should make their planning, meetings, etc., more publicly accessible. Videoconferencing, streaming, posting agendas and detailed meeting packets online would greatly help with transparency and marketing efforts.

Economic Model

Our economic model features Production <> Distribution <> Consumption, with Distribution including Transportation and Telecommunication. Distribution links Production and Consumption, and none survives without the other. The Production sector however has more jobs and the Consumption sector more users than the Distribution sector has jobs, making Distribution more critical of the three. PA has an extensive overall transportation system because it had a tremendous production sector. Will PA downsize (or as some say "rightsize") its transportation systems to better match its existing production sector, or instead fight to regain those industries it lost to more fully utilize (and better finance) its transportation systems? Thus government agencies tasked with economic development and retention must be significantly involved in the investments and decisions made in the Distribution sector and their implications upon other sectors.

The Competition

Those implications are critical as PA competes for commerce and jobs not only against the region, but more importantly against international concerns that have unfair advantages the state must cope with until Congress rectifies the imbalances. However neither the federal government nor Wall St. can be counted upon anymore for amount of help necessary. The state must look after its own affairs by providing cost-competitive distribution to retain, develop, and retrieve industries and heavy commercial production and service providers, and lower the costs of living for the public using its transportation systems.

About the Author

Daniel L. Van Epps is an Ed.D. candidate in Technology Education/Systems Analysis at West Virginia University. He holds a fiber optic certificate from Lansing (MI) Community College, a BA and MA in Telecommunications/Information Systems and Technology from Michigan State University, a Masters Certificate in Intelligent Transportation Systems from the University of Michigan, and has taken a graduate railroad business course at Carnegie Mellon University. Originally from Detroit, MI and a graduate of Dover (OH) High School, he is currently an independent researcher, non-profit lobbyist, consultant, and the executive director of the non-profit Conotton-Sandy-Tuscarawas Valley Community Improvement Corp. He has previously testified to the Ohio Legislative Transportation Task Force and the Ohio Department of Transportation's 21st Century Transportation Priorities Task Force regarding transportation financing and multi-modal tollway provision issues.

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