

**ALASKA STATE LEGISLATURE**  
**SENATE TRANSPORTATION STANDING COMMITTEE**

February 15, 2011

1:00 p.m.

**MEMBERS PRESENT**

Senator Albert Kookesh, Chair  
Senator Joe Thomas, Vice Chair  
Senator Dennis Egan  
Senator Linda Menard

**MEMBERS ABSENT**

Senator Charlie Huggins

**COMMITTEE CALENDAR**

SENATE BILL NO. 79

"An Act making a special appropriation to the Knik Arm Crossing fund; and providing for an effective date."

- MOVED SB 79 OUT OF COMMITTEE

SENATE BILL NO. 80

"An Act relating to the authority and obligations of the Knik Arm Bridge and Toll Authority, to bonds of the authority, and to reserve funds of the authority; authorizing the state to provide support for certain obligations of the authority; relating to taxes and assessments on a person that is a party to an agreement with the authority; and establishing the Knik Arm Crossing fund."

- MOVED SB 80 OUT OF COMMITTEE

**PREVIOUS COMMITTEE ACTION**

BILL: SB 79

SHORT TITLE: APPROP.: KNIK ARM CROSSING FUND

SPONSOR(S): SENATOR(S) MENARD

02/04/11	(S)	READ THE FIRST TIME - REFERRALS
02/04/11	(S)	TRA, FIN
02/15/11	(S)	TRA AT 1:00 PM BUTROVICH 205

BILL: SB 80

SHORT TITLE: KNIK ARM BRIDGE AND TOLL AUTHORITY

SPONSOR(s): SENATOR(s) MENARD

02/04/11 (S) READ THE FIRST TIME - REFERRALS  
02/04/11 (S) TRA, FIN  
02/15/11 (S) TRA AT 1:00 PM BUTROVICH 205

**WITNESS REGISTER**

MICHAEL L. FOSTER, Chair  
KABATA Board  
Anchorage, AK

**POSITION STATEMENT:** Provided an overview of the Knik Arm Crossing and provided information on SB 79 and SB 80.

ANDREW NIEMIEC, Executive Director  
Knik Arm Bridge and Toll Authority  
Anchorage, AK

**POSITION STATEMENT:** Provided supporting information related to SB 79 and SB 8080.

KEVIN HEMENWAY, Chief Financial Officer  
Knik Arm Bridge and Toll Authority (KABATA)  
Anchorage, AK

**POSITION STATEMENT:** Provided supporting information related to SB 79 and SB 80.

JAMIE KENWORTHY, representing himself

**POSITION STATEMENT:** Testified in opposition to SB 79 and SB 80.

JEFF OTTESEN, Director  
Program Development  
Department of Transportation and Public Facilities  
Juneau, AK

**POSITION STATEMENT:** Testified in support of SB 79 and SB 80.

**ACTION NARRATIVE**

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**CHAIR ALBERT KOOKESH** called the Senate Transportation Standing Committee meeting to order at 1:00 p.m. Present at the call to order were Senators Menard, Thomas, Egan, and Kookesh.

**SB 79-APPROP.: KNIK ARM CROSSING FUND**  
**SB 80-KNIK ARM BRIDGE AND TOLL AUTHORITY**

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CHAIR KOOKESH announced the consideration of both SB 79 and SB 80.

SENATOR MENARD, sponsor of SB 79 and SB 80 said these bills will ensure a private/public partnership procurement (P3) for the Knik Arm Crossing Project that generates the best value to the state of Alaska. The passage of this legislation will facilitate the Knik Arm crossing being open for traffic in the year 2015, thus expediting for Alaska the benefits generated from the crossing. Both bills were written in consultation with the Knik Arm Bridge and Toll Authority (KABATA), which has been recently successful in its assurance of the Record of Decision (ROD) from the federal highway administration. She said that a project is only as good as the person behind it, and introduced Michael Foster, chair of the KABTA board and engineer behind the Red Dog Mine. She also introduced Kevin Hemenway and Andrew Niemiec.

SENATOR MENARD explained that SB 80 will accomplish 4 things: First, an increase in KABATA's bonding authority from \$500 million to \$600 million; second, property tax relief for the crossing and associated facilities; third, contractual monetary obligations; and fourth, a project reserve fund.

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She also explained that SB 79 will appropriate \$150 million into the project reserve fund created by SB 80. The fund will be housed in the Department of Revenue (DOR). This bill is supported by many, including the Alaska Trucking Association, the Alaska Support Industry Alliance, the Mat-Su Borough, City of Wasilla, and the Municipality of Anchorage It also has widespread public support, and the project is ready to go.

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SENATOR KOOKESH asked why there is no fiscal note associated with the bills.

SENATOR MENARD cited the memo from Legislative Legal Services, which says that a fiscal note shall be attached to a bill or resolution, unless it is an appropriations bill, before it passes the first committee of referral.

SENATOR THOMAS said he supports infrastructure and he believes that the question now is the legal liability of the state for completing or maintaining the bridge. However, SB 80, page 2, line 17, states "the monetary obligations incurred by the authority under the partnership or contracts are obligations of the state and satisfaction of those contracts from funds other

than authority funds is subject to appropriation." He hopes to be assured about the amount that could be at risk.

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MICHAEL L. FOSTER, Chair, KABATA Board, said he would give an overview and address SB 79.

He assured the members that the federal department of highways supports the Knik Arm project, and said that KABATA received a Record of Decision in December. The project has been listed under the National Highway System and lane miles are already listed.

He noted the article in the Anchorage Daily News, as well as a Dittman survey which shows overwhelming public support for the project. Mayor Sullivan also sent a letter encouraging the Legislature to pass these bills in a timely manner.

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MR. FOSTER noted there has been discussion about the appropriation to KABATA; he clarified that the actual appropriation was \$229 million. In 2006, \$128 million of that was reappropriated to other projects throughout the state. If that money was still allocated to the Knik Arm crossing, they would be asking for less. That \$128 million represented the reserve fund needed for the public/private partnership. The reserve fund would be managed by DOR, and allows KABATA to go out to market and obtain private capital. The infrastructure and revenue stream is owned by the State of Alaska. The capital to build the project is private sector capital; no state or federal capital will be used to construct the facility. The reserve fund is not to operate KABATA today; it is to be used when the bridge is open for use. During the first several years, the revenue stream may be less than the payment stream, and KABATA anticipates it will need the reserve at that time and for several years thereafter. After that, they expect that excess revenue will pay that reserve back, and they project over a 60 year time frame, \$8.6 billion will roll back into the reserve fund. This money can be used for Title 23 services statewide, which includes marine highways, boardwalks, bridges, ports, and infrastructure. He again pointed out that the money appropriated by these bills would not be used until 2015 or 2016, and is only used in the initial years to cover the currently projected shortfall. It is not a capital appropriation, but a short-term use with a payback based on revenue stream.

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ANDREW NIEMIEC, Executive Director, Knik Arm Bridge and Toll Authority, said that SB 80 will aid in the successful procurement of the Knik Arm Crossing, reduce the cost of project finance, and generate the best value to the state. Passage of SB 80 will facilitate the project being opened to traffic by 2015. The bill is designed to increase KABATA's bonding authority, address contractual monetary obligations, and establish and manage a reserve fund. An increase in bonding authority from \$500 million to \$600 million matches the \$600 million allocation of private activity bond capacity (PABS) that was provided by the U.S. Department of Transportation. That allocation remains with the project. Any PABS issued are a liability of the private borrower, not the state. The property tax language clarifies and clearly specifies that the bridge and associated connectors are not subject to property tax if operated by a private developer on behalf of the state. Any private facilities installed along with the project, but not for transportation use, would be subject to local property tax.

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AS 19.75.111(a) would be modified to clarify that monetary obligations under a public/private partnership for the purpose of constructing this project are obligations of the state, and satisfaction of those obligations is subject to appropriation. This only applies to those obligations that are subject to the public/private partnership, and not other contractual or corporate obligations of KABATA. This change is necessary to attract investors, and will keep tolls affordable.

The reserve fund will apply sources of revenue, including tolls and any appropriations, for specific purposes such as providing the annual payment to the private partner. Surplus funds would then be available for capacity improvements and other federally eligible transportation purposes. Surplus funds would be held by the DOR until a private partnership agreement is signed, at which time the funds would be available for deposit into the reserve fund. Procurement advisors under contract with the Department of Law have reviewed the proposed legislation for consistency with AS 19.75 and other related statutes. These provisions will enhance project credit and allow the developer to obtain the lowest cost capital, thereby providing the greatest benefit to the state.

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KEVIN HEMENWAY, Chief Financial Officer, Knik Arm Bridge and Toll Authority (KABATA), said this toll bridge will generate revenue. The Record of Decision was a significant milestone,

which allows KABATA to move forward with procurement. Under the proposed structure, the private sector will be responsible for the design, construction, financing, operation and maintenance of the facility for approximately 35-40 years. The private sector, not the state, will raise the equity and borrow the debt to finance the project. That debt will be non-recourse to the state. The private sector will also be responsible for the design-build contract and substantially all of the construction risk. They will do this in exchange for payments that will be used to repay their financing and to pay for operations and maintenance of the facility. At the end of the term, the facility will be returned to the state.

The state, through KABATA, will own the bridge facilities and will receive the toll revenue. That toll revenue stream will be used to make the periodic payments; in the event the revenue stream is insufficient, the reserve fund is there to provide credit enhancement to the creditors' lenders, but they do not have a direct interest in that account.

The competition for the project will be based on the lowest annual periodic payment and technical specifications. The proposals will be evaluated by a committee that includes input from the departments of law, transportation and revenue. Final approval will reside with the administration and KABATA board, many of whom are legislators. This is a regimented, disciplined procurement strategy. SB 79 and 80 establishes a framework to attract the proposal, but actual commitments don't occur until the contractual arrangement is entered into. The cost of financing is clearly a significant component.

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To the extent that capital cost is reduced, it will attract better proposals at a lower periodic payment. SB 79 and 80 are important to achieving that, precisely because they will lower the cost of financing and provide the mechanisms required to establish the contractual structures that the marketplace expects. KABATA is also working to lower the cost of capital through the Transportation Infrastructure Finance and Innovation Act (TIFIA) program. KABATA feels there is a good possibility of receiving TIFIA financing for the project. KABATA has also obtained, through DOT, \$600 million of private activity bond capacity that the developers can choose to use that allows them to borrow funds at tax exempt rates. This is directly related to the request to increase, under SB 80, the \$500 million bonding capacity to \$600 million. If developers choose to use the entire

capacity in their proposals, KABATA want to be in a position to accommodate them as a conduit issuer, but not a borrower.

There are numerous successful P3s in the U.S. and throughout the world. Failures have been rare, but in those cases the demonstrated risk transfer proves that P3 works. In none of those cases was the state obligated for the debt or other obligations of the private partner. Some examples are SR125 and the Dulles Greenway. In both instances of bankruptcy, there was no recourse to the state for project financing, and the state continued to own the assets.

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Traffic and toll revenue is a place where the state retains ownership, and there is front end risk. The base case forecast over the 35 year term of operations indicates that toll revenue would cover annual payment obligations by a factor of 1.7 times. There is about \$20 million over the first three years that gets repaid under the base case. He cautioned that the models are pro forma, prepared by KABATA and other consultants using best available market indicators. The real model won't be available until they attract proposals through the RFP process. Wilbur Smith Associates is the preeminent traffic control revenue forecaster; their studies are bankable on Wall Street, and their track record is exemplary. Over the last ten years their traffic and revenue studies have supported approximately \$33 billion worth of toll road financing, and the last five years represents about \$20 billion of the total. KABATA is confident that over the life of the crossing the state will recover its investment and earn a substantial return.

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In conclusion, SB 79 and 80 establish a framework to attract the most competitive proposals at the lowest cost and best value to the state. They do not commit the state to anything unless the private sector proposals are accepted and finalized, which would occur in the first half of 2012, at the earliest. Appropriations under SB 79 will be held by the Department of Revenue as fiduciary until acceptable proposals have been received for the project. Amendments under SB 80 serve to establish mechanisms to develop a successful public/private contracting framework, and the funds appropriated under SB 79 will serve as a project reserve, demonstrating to prospective private partners that the state is serious about the essential nature of the project and its role in the public/private agreement as project owner. Funds will be paid back over the term of the project. The project will produce a continuing revenue stream that will support other

infrastructure projects throughout the state, and is needed to support economic development, jobs, access to land for population and industrial growth, and for safety. It will benefit generations of Alaskans.

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SENATOR THOMAS said he is still struggling with page 2, line 17. The \$150 million is potentially obligated, but the toll revenue is obligated to pay the debt service first.

MR. HEMENWAY responded it is actually not paying the debt service, but instead is paying an annual availability fee. This is an annual payment to the developer that he uses to repay his financing and to pay for the operations and maintenance of the project. So the state's major contractual obligation is the commitment to make that payment.

SENATOR THOMAS asked if there was federal participation.

MR. HEMENWAY replied there is some federal participation. As of today there is about \$65 million available for right-of-way and construction phases of the project. Some of that will be acquired prior to the partnership, so the remainder will likely go into some component of construction.

SENATOR THOMAS asked if there was federal participation.

MR. FOSTER replied the state's commitment to its private partner is the annual payment; as toll revenue exceeds payments, the revenue would pay back the reserve fund

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SENATOR THOMAS said his understanding is that if there is federal participation, the first thing to be repaid would be debt service, then reasonable return on investment, and then any private financing of the project.

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MR. HEMENWAY said the toll revenue would fund the lease payment to the developer and they will use that revenue for repayment of their financing, operations and maintenance, and reasonable returns of their equity investors. The toll agreement stipulates that any surplus toll revenue remaining after meeting the contractual obligations will be used for Title 23 eligible projects.

SENATOR THOMAS said he's looking at the potential for problems if things don't go according to plan. In that case, he is looking for what the state's obligation would be. Construction costs are increasing, and costs overruns could impact toll fees. He said he would like a simple answer to what happens if the worst situation occurs. Would the state only be out \$150 million, or would more funds be needed?

MR. FOSTER replied the toll is set by KABATA, and the capital cost is the private partner's responsibility. The state's responsibility is the annual payment to the private partner. If the private partner underestimates the cost, that is part of his business model. His annual payment does not get adjusted because it costs him more than he expected.

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SENATOR THOMAS asked why the page 2, line 17, language is necessary if that's the case.

MR. NIEMIEC responded that the major contractual obligation of the state is the commitment to make that annual payment.

SENATOR THOMAS asked if it wouldn't it be the same if the bonding wasn't sufficient to pay for the last third of the construction.

MR. NIEMIEC responded generally that is the responsibility of the private developer, not the state.

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JAMIE KENWORTHY, former executive director, Alaska Science and Technology Foundation, said the project will lead to a \$250 million liability on the state's balance sheet; with interest it would easily be over \$1 billion. SB 80 does not just transfer \$150 million to cover KABATA's current estimate of the first three years of the bridge deficit, it also says that KABATA can enter into partnerships that would become obligations of the state. That is AS 19.75.111. The current statute allows KABATA to issue \$500 million in bonds in its own name, but not the state's name. If these bonds that KABATA issues after the partnership agreement is made are obligations of the state, the state is on the hook for them. He suggested the committee ask the directors of AHFC about moral obligations; if the bonds fail, it would affect the agency's credit rating. It would also affect the state's credit rating.

The original definition of the public/private partnership was for a private sector firm to finance, build, and operate the Knik Arm project. Under these two bills the state would be responsible for the full bonding. If the Legislature is to sign that blank check, shouldn't that check at least be based on accurate traffic numbers? Wilbur Smith is now redoing the traffic numbers, more based on a Mat-Su population forecast.

All the revenue projections that KABATA has used are based on a 2030 Mat-Su population number nearly 50 percent higher than today. That projection was developed in 2007 by a Texas firm under contract to KABATA. The projected deficit for the first ten years of the bridge is \$25 million per year. Since March three events have occurred that make the projects finances much worse. First, they discovered the population error that caused revenue to be overestimated by 50 percent. Second, in November KABATA was turned down for a federal TIFIA loan for one-third project cost. KABATA is going to reapply, but he estimates their chances are between slim and none.

Third, rates for investment grade bonds are up to 5 percent; without a state guarantee, the bonds will not receive an investment grade and will not find a market. Attaching a guarantee to such iffy bonds would jeopardize the state's credit rating. The payments on a \$650 million bond at five percent interest, amortized over 37.5 years, would be \$38.3 million per year. You would need 20,900 one-way trips per day at five dollars each just to make the annual bond payment.

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The current traffic to and from the Mat-Su Valley is 29,000 trips per day, and most of the valley would continue to take the toll-free trip on the Glenn Highway. The KABATA estimate for bridge trips in 2030 is about 40,000. We are having trouble getting DOTPF current traffic estimates for the bridge and the Glenn Highway for the same year. He expects it will be about half of KABATA's estimate. Trip forecasts should account for the fact that a toll reduces demand. There will not be enough traffic to repay the bonds, even if they are interest free.

MR. KENWORTHY questioned how KABATA can project a huge return. He suggested that the private sector should decide if this project is feasible. Perhaps in 30 years this will become feasible, but right now it is speculative. If the RFP process goes forward, the Legislature should repeat the conditions that the Anchorage Assembly originally set, to make sure this project does not crowd out other projects. One, no further state funds;

two, no state guarantee; and three, a private sector willing to finance, build, and operate the project.

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He also pointed out that last year the TIFIA application said that all shortfalls would be covered by annual appropriations by of the state Legislature to make the bond payments and cover operating funds.

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SENATOR THOMAS asked what interest rate he was using to come up with \$38 million.

MR. KENWORTHY replied five percent.

SENATOR THOMAS stated that conduit financing isn't using state bonding authority, just state employees.

MR. KENWORTHY said the businesses backed by the banks are taking the risk. If AIDEA does its own appropriation and is not using a conduit, then they are putting the bonds on the street and it is not an obligation of the State of Alaska. However, everyone understands that it is a moral obligation. The interest rates on those bonds are higher than a state general obligation bond, but significantly lower than if just a private sector firm came to the marketplace. AIDEA cares about its credit rating, and the State of Alaska cares about AIDEA's credit rating.

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JEFF OTTESEN, Director, Program Development, Department of Transportation and Public Facilities (DOTPF), said the TIFIA issue isn't dead. Yesterday President Obama announced a \$450 million allocation for TIFIA in the federal budget. He also announced a \$5 billion per year infrastructure bank that would be \$5 billion for six years. This would be a new opportunity for KABATA coming from the federal side. Last summer Secretary LaHood visited the site, so there is clearly some federal interest.

MR. OTTESEN said that this state was built on risk and who would be a better risk than the state itself. The traffic from the North Slope and the Interior would pay for this bridge. Mat-Su isn't the only source of traffic. It's a bridge for Fairbanks, the North Slope, and tourism traffic. But the growth that does occur in Mat-Su will be reflected by this bridge. If this isn't built there will be a need for more highway improvements.

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He confirmed that this project was accepted by the FHWA as part of the National Highway System. This is important, because the project doesn't compete with AMATS.

Finally, P3 is becoming a way of life in transportation, and not for just infrastructure. In Europe P3s are being used to develop vaccines, for example. In Washington State a P3 is developing a toll bridge that will replace an existing bridge and tolling will start prior to the bridge being built.

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SENATOR THOMAS said he doesn't mind risk he just wants to know what it will be. If the risk is \$150 million that's one set of circumstances, but it's another if it's \$700 million. The language in the bill is unclear. The explanation seemed to clarify that there is more potential risk.

MR. OTTESEN responded the risk is on the P3, and it boils down to traffic. He said it is important to look at the next traffic predictions being done by Wilbur Smith.

SENATOR THOMAS asked if there is a guarantee on the numbers.

MR. OTTESEN replied there is no guarantee, but Wilbur Smith has a reputation of being credible.

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CHAIR KOOKESH asked for a response from the project with regard to Mr. Kenworthy's testimony.

MR. FOSTER said the reserve fund allows KABATA to go to market and obtain the best available annual payment to take the initial risk. A lot is based on traffic modeling. The consultant is doing a new model. But the real test is to get a private partner. Passing these bills allows KABATA to go to market and attract proposals. However, if the risk is disproportionate it won't move forward. KABATA believes it will get attractive proposals. He said the idea of the P3 partnership is shared responsibility. The risk to the state depends on the reliability of the traffic model.

CHAIR KOOKESH asked about the TIFIA application.

MR. FOSTER explained that they submitted the application and were encouraged. This is a DOT project. Initially they didn't expect approval because KABATA didn't have a record of decision,

but now they do. There is \$450 billion, which is threefold the previous TIFIA. They feel confident they will get that TIFIA and therefore the ability to get the loan for financing for the private partner.

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CHAIR KOOKESH announced a brief t ease

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CHAIR KOOKESH reconvened the meeting.

SENATOR MENARD introduced Janet Kincaid, KABATA board member.

CHAIR KOOKESH stated that he intended to move the bills today; two of the members are on the finance committee and will have an opportunity to address the finance issues. He closed public testimony and asked the will of the committee.

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SENATOR MENARD moved to report both SB 79 and SB 80 from committee with individual recommendations and attached fiscal note(s). There being no objection, SB 79 and SB 80 moved from the Senate Transportation Standing Committee.

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There being no further business to come before the committee, Chair Kookesh adjourned the Senate Transportation Standing Committee meeting at 2:15 p.m.