

Testimony by Jamie Kenworthy to KABATA Board 4/29/10

I have one question and five quick points.

1. In the private sector scenario financials you presented to the Department of Revenue on March 23, will the private sector take the downside risk of covering any potential toll shortfall to cover debt service?

One slide implies the bidders taking most of the finance risk but your description of a state letter of credit for the P3 private scenario -- which you call "off balance sheet financing" -- implies that the state is the final backstop to cover any toll shortfall. So which is it, will the private sector cover any toll shortfall or will the State of Alaska?

My 5 points:

1. KABATA needs to rerun the traffic and toll numbers based on a Mat Su population in 2030 of 169,000, UAA ISER's current estimate. You used a 250,000 population for Mat Su 2030. Mat Su is now about 85,000. While it is the state's fastest growing region, for Mat Su to get to 250,000 by 2030, the Borough would have to add over 8200 people a year -- that's adding a Palmer a year to the Borough population every year for 20 years.

Your slides to the Department of Revenue describe the Revenue and Financial Model as "completed" and the project as "financially feasible" but without an accurate population and toll estimate the financial model is not complete and feasibility is not shown.

2. The private sector scenario you presented to the Department of Revenue is not plausible. You have the private sector putting in \$72 million in equity and taking out \$3.2 billion or 44 times their investment. That's 9% of the money in and 64% of the money out. Yes, equity takes more risk than debt and so has to earn more return, but with your proposal to have the state issue a Letter of Credit to backstop the toll shortfall, it is quite an unreasonable upside for the private sector to get so much upside for so little risk.

And TIFIA guidelines do not permit any equity withdrawal prior to paying interest on federal TIFIA Bonds as you show in your P3 scenario. Your P3 scenario has the private sector concessionaire taking out \$42 million in equity dividends in the first four years the bridge is open prior to starting to pay TIFIA Bond interest costs in Year 5.

3. On the public debt sector scenario, there's no precedent for the state to use a letter of credit (LOC) to backstop toll shortfalls. In this environment, bank Letters of Credit are extremely hard and costly to get. If available, they usually cost at least 2% of a project's budget, or an unbudgeted \$16 million. Why would the state with a AA credit rating pay a bank (with probably a lower rating) to insure the project? And why would a bank be willing to provide an LOC unless the state already has agreed to backstop the toll shortfall making the LOC unnecessary?

As your slides to the Department of Revenue indicate, the public scenario is a normal state revenue bond which would require the legislature to annually appropriate debt service as is the case with the Whittier Tunnel.

4. Under either the P3 private scenario or the public debt scenario, this project is a public project requiring an enormous state subsidy to be built; my estimate is at least half a billion dollars in subsidy. So KABATA should stop pretending this is a P3 project like Miami with the private sector taking the downside. Instead you have the State of Alaska taking the downside and the private sector keeping the upside which in Miami is fixed. So it's time you put these draft financials on your web site and let the public examine this as a proposed state financed project. To summarize my message in a sentence, this is a proposed publicly financed project and the public deserves accurate financials based on accurate population estimates to assess the project.

5. Finally, representatives of KABATA have described my estimate of Bridge costs and financing as misleading. Now that I have the draft financials you gave the Department of Revenue last month, I see that my estimate of total KABATA costs – including O&M, admin, toll collection, capital reserves etc – is lower than yours. My estimate of KABATA toll revenue was the same numbers the feds used to assess your TIFIA bond application and that was based on a 250,000 2030 population. Those population and toll revenue numbers now need to be reduced by approximately a third which I expect will lower your projected cover ratio of revenue to debt below the point of financial feasibility.

The only reason you do not show large deficits in the first 7 years after the Bridge opens is you have capitalized the interest payments in capital accretion bonds so the project has to pay more later. This is precisely the negative amortization Mr Hemenway told the Planning and Zoning Commission was not in the Bridge financing plan. So it seems fair and intellectually honest to either not label my numbers as misleading or for you to point to a single number that is misleading and show why it is misleading.

Thank you.