Oregon

John A. Kitzhaber, M.D., Governor

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TO: House Committee on Transportation and Economic Development

FROM: Clyde Saiki
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SUBJECT: Funding and Financing Transportation Projects

INTRODUCTION

The many and diverse elements of Oregon's transportation system are funded through local, state and federal programs, private investments and sometimes a combination of all these sources. Oregon relies heavily on highway user fees to fund highway, road and street improvements and maintenance across the state. These fees include fuel taxes, vehicle registration and title fees and weight-mile taxes. There is limited funding for non-highway projects.

The Oregon Legislature has made significant investment in the state's transportation system over the last decade through the three Oregon Transportation Investment Acts (OTIA), five funding cycles of *Connect*Oregon, and the Jobs and Transportation Act (JTA). Under these programs, ODOT and local governments have completed hundreds of important projects that have improved safety, created a more efficient freight transportation system, preserved critical transportation assets and improved the livability of Oregon's communities.

In these investment packages, the legislature prudently limited use of bonding to capital improvement projects. We bond for projects with a long, useful life, such as bridges and highways, which we expect to last for many decades. We do not bond for maintenance and operations. Sustainable long-term funding for maintenance and operations requires a separate funding mechanism other than bonding. Most of these investment packages were one-time infusions for specific projects rather than long term sustainable funding for maintenance and operations.

ODOT's current bonding is at a reasonable and prudent level. We have a disciplined financial management structure at ODOT and position our investments in the best way possible. That, plus our delivery of programs, places us in good stead as reflected in our credit rating. The marketplace sees ODOT as a good investment and ODOT has the highest state agency credit rating in the State of Oregon. To maintain our good financial standing and access to low interest rates new projects will require new revenue.

Bonding has allowed these investment packages to be frontloaded. ODOT's commitment to prudent and disciplined debt management and our strong credit ratings have allowed the department to borrow at historically low interest rates to complete a range of high priority transportation projects around the state. ODOT is now entering the phase where the work is finishing up and the debt must be repaid. Bonding is akin to taking out a mortgage: it allows you to fund a large asset (buy a house, build transportation projects) much sooner than if you had to save up the cash. And, like a mortgage, it requires repaying the debt over several decades.

ODOT faces long term funding challenges. By 2017, approximately $200 million of ODOT's State Highway Funds (about one-third of funds) will go to debt service each year, which will constrain future construction. This level of debt service will continue through 2036. Debt service on bonds, rising construction costs, uncertain federal funding and growing fuel efficiency in vehicles – all of these forces combine to reduce the resources ODOT will have to preserve and improve the transportation system in coming years.

BONDING IN OREGON

Public borrowing is an important tool in Oregon's efforts to create jobs while improving the State's infrastructure. However, public borrowing must be used carefully because the resulting debt repayment becomes a fixed cost in future State budgets. An over-reliance on borrowing can cause deterioration in the State's credit ratings, resulting in higher borrowing costs. Members of the legislative and executive branches of government, including the State Treasurer's office, work together to ensure the State's policies and actions will enhance and preserve the State's credit rating and maintain the future availability of low-cost capital financing. Each individual bonding program receives specific legislative authorization and is managed by a state government agency.

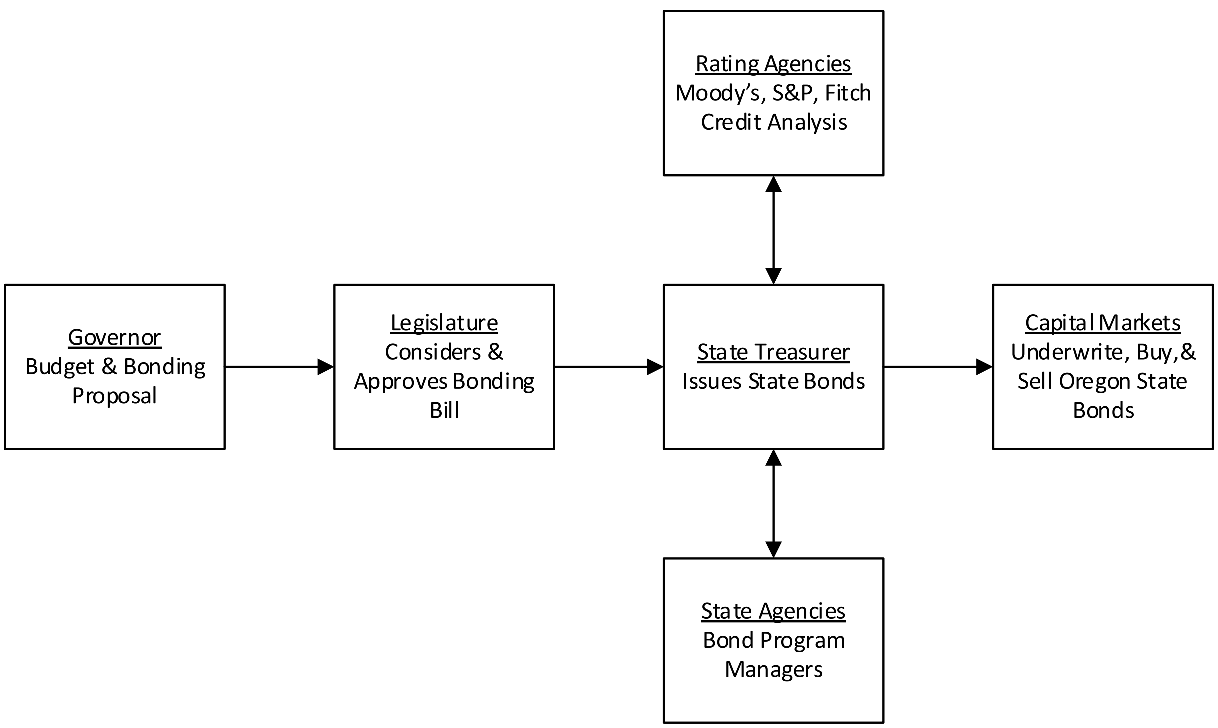

Figure 1: Oregon's Bonding Process

ODOT uses three primary types of long-term debt financing: direct revenue bonded debt, general obligation bonded debt, and appropriations credits.

Direct Revenue Bonded Debt
Direct revenue bonds are secured by a specific dedicated revenue stream, such as the State Highway Fund or lottery dollars. They do not constitute a general obligation pledge of the State of Oregon.

General Obligation Debt
General obligation (GO) debt is secured by the unlimited full faith and credit of the participating issuer, for our purposes the State of Oregon. Each GO bond program in Oregon was created by a constitutional amendment passed by state voters.

Appropriation Credits
Similar to direct revenue program debt, appropriation credits are not secured by the State's unlimited pledge to fund debt service. These credits are payable solely from funds appropriated or otherwise made available by the State Legislative Assembly. Because the legislature has to authorize the funds to pay the debt service separately each biennium, appropriation credits are seen as a higher risk financing vehicle and as such carry a higher interest rate. ODOT has used Certificates of Participation (COP), a form of appropriation credits, primarily for facility financing.

ODOT BOND PROGRAMS
ODOT currently manages multiple bond programs for the State of Oregon including the Oregon Transportation Investment Acts (OTIA), the Jobs and Transportation Act (JTA) and *Connect*Oregon. ODOT's bond programs are repaid by either the State Highway Fund – as with OTIA, the JTA and facility bonds – or by Lottery funds.

Oregon Transportation Investment Act (OTIA)
From 2001 through 2002, the Oregon Legislature approved $500 million in direct revenue bonds for OTIA I and OTIA II modernization and preservation projects. In 2007, the department completed issuance of the $500 million OTIA I and OTIA II authorization. The OTIA I and OTIA II programs, which included 184 projects, were completed in May 2010 with all program funds expended.

In 2003, the Oregon Legislature approved an additional $1.9 billion in direct revenue bonds for OTIA III to repair or replace state and local bridges, and for modernization projects. In 2010, the department completed issuance of the $1.9 billion OTIA III authorization. All projects are essentially complete.

All OTIA bonds will be paid off in 2038.

Jobs and Transportation Act (JTA)
In 2009, the Oregon Legislature enacted the Jobs and Transportation Act (JTA), which among other things, authorized ODOT to issue $840 million in direct revenue bonds to finance a specific list of 51 projects set out in the JTA. The projects consist of 37 specific highway projects plus allocation for 14 additional projects selected by local governments in eastern Oregon. The estimated funding for the JTA projects and allocations totals approximately $960 million financed by $840 million in direct revenue bonds plus additional revenues allocated from the State Highway Fund.

In October 2013, the department issued $450 million in direct revenue bonds for JTA projects. The remaining $390 million authorization is projected to be issued in the 2015-17 biennium. All currently issued JTA bonds will be paid off in 2038.

***Connect*Oregon**
From 2005 through 2013, the Oregon Legislature authorized $382 million in Lottery revenue bonds to fund *Connect*Oregon multimodal transportation projects. *Connect*Oregon funding is restricted to non-highway purposes including ports, air, transit and rail. The Department of Administrative Services (DAS), on behalf of ODOT, has issued the entire $382 million dollar authorization. All currently issued *Connect*Oregon bonds will be paid off in 2035.

Other Lottery Bond Funded Programs
ODOT administers the debt service payment for other Lottery bond programs on behalf of various local governments. These programs include the following:

- In 2001, the Oregon Legislature authorized $6 million in Lottery bonds to fund a Short Line Infrastructure Assistance Program.
- In 2001, the Oregon Legislature authorized $35.5 million in Lottery bonds to finance a 15-mile South Metro Commuter Rail project that connects Wilsonville, Tualatin, Tigard, and Beaverton.
- In 2003, the Oregon Legislature authorized $8 million in Lottery bonds to fund industrial rail spur infrastructure improvements.
- In 2007, the Oregon Legislature authorized $20 million in Lottery bonds to fund Oregon Streetcar projects.
- In 2007, the Oregon Legislature authorized $250 million in Lottery bonds to partially fund TriMet's Portland-Milwaukie Extension Commuter Rail project.
- In 2013, the Oregon Legislature authorized $10 million in Lottery bonds for distribution to the Oregon International Port of Coos Bay for the purpose of acquiring, constructing or improving the Coos Bay rail link.
- In 2013, the Oregon Legislature authorized $3.5 million in Lottery bonds for distribution to the Salem-Keizer Transit District for the purpose of acquiring, constructing or improving the Salem-Keizer Transit Center.

Facility Bonds
The passage of the Constitutional amendment Article XI-Q, authorized the State to issue general obligation (GO) bonds for various State-owned office buildings, facilities and other capital projects. Article XI-Q GO bonds are higher rated and realize lower costs than traditional appropriation credits.

Beginning in 2007, the Oregon Legislature authorized issuance of appropriation credits and Article XI-Q GO bonds for the State Radio Project (SRP). Currently, the Department of Administrative Services (DAS), on behalf of ODOT, has issued $169.2 million for the SRP. The remaining authorization of approximately $40 million is projected to be issued in fiscal year 2016.

The Oregon Legislature authorized $64 million in Article XI-Q GO bonds in 2011 to finance the renovation of the Transportation Building on the Capitol Mall. The Transportation Building renovation project was completed in August 2012, on time and under budget. The remaining bond proceeds will be used for debt service.

ODOT MANAGEMENT OF DEBT SERVICE

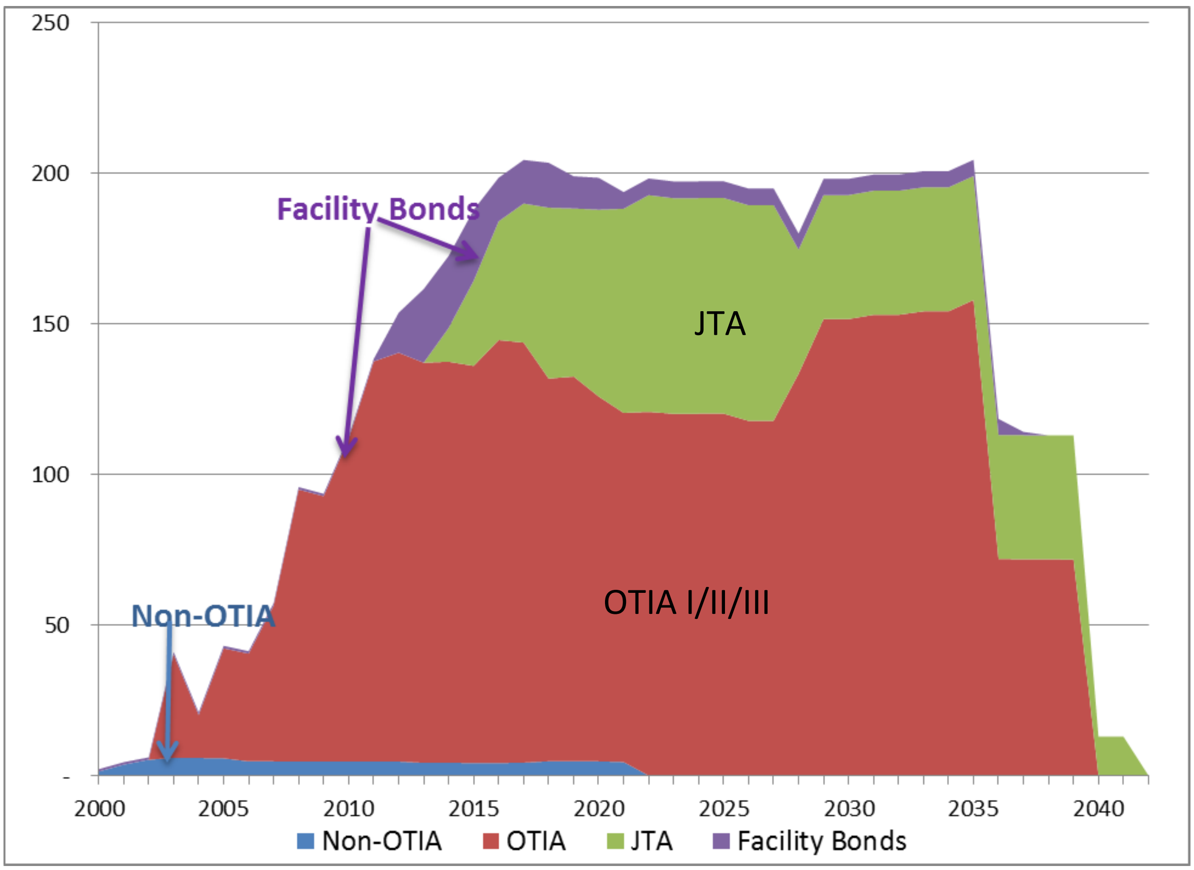

Figure 2: ODOT State Highway Fund Supported Debt Service Profile (with Local Bridge), Debt Service in Millions ($) by Fiscal Year.

Debt service funds account for the accumulations of resources for the payment of principal and interest on general obligation bonds, revenue bonds and certificates of participation. We continuously monitor opportunities to refinance existing debt to secure lower interest rates. This is especially so in the historically low interest rate environment of recent years. Since 2012, the department has realized approximately $90 million in debt service reductions over the life of our bond programs through issuance of refunding bonds. We have and will continue to prudently manage our existing bond programs for other opportunities for debt service reductions.

CONCLUSION

Bond programs managed by the Department consist of Lottery revenue bonds, highway user tax revenue bonds, general obligation (GO) bonds and appropriation credits. Because resulting debt repayment becomes a fixed cost in future ODOT budgets, debt service will constrain our ability to do new projects in the next two decades without new revenue. While we have made important investments in our transportation infrastructure over the last decade, further one-time infusions for new infrastructure will fail to address Oregon’s growing need for maintenance and preservation of its existing transportation system. In the long term, the condition and performance of the transportation system will be diminished without a significant and sustainable source of revenue.