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On
Building American Transportation Infrastructure through Innovative Financing

Before
The Senate Committee on Commerce, Science, and Transportation

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Mr. Chairman, Senator Hutchinson, and Members of the Committee:

Thank you very much for the opportunity to testify on the need for innovative financing – such as a national infrastructure bank – as we work to improve America's transportation infrastructure. This subject is important to our nation's future, and I commend the Committee for holding today's hearing.

The Carlyle Group is a global alternative asset manager with approximately $150 billion in assets under management. Carlyle invests in small, medium and large companies, real estate, infrastructure projects and financial services firms. Whether an investment is in a small, growing company, a large infrastructure project, or a real estate asset, our strategy is the same: we seek to build long-term value in a company or asset through investments, improvements in management, and efficiency enhancements. Today, we have investments in approximately 80 companies based in the United States, 77 percent of which are small or medium-size businesses (fewer than 2,500 employees), as well as about 125 real estate projects, which include commercial, residential, and health care or data centers. Combined, these companies employ more than 216,000 people in the United States in all 50 states.

I am the co-head of Carlyle's infrastructure group, which has raised $1.2 billion specifically to invest in infrastructure projects with its primary focus on the United States. And we are quite proud that public and private pension funds contributed over forty percent of the fund that we manage and invest on their behalf.[1]

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[1] The actual amount that fund investors contribute to a particular transaction frequently varies from the level of commitment those fund investors have made to a particular fund. This differential stems from a number of factors, including the investments made by a management team or co-investors.

Carlyle Infrastructure Partners invests in companies that contract with state and local governments throughout the United States to provide services, such as treatment of biosolids at the end of the wastewater treatment process, school bus transportation, and other infrastructure-based services. I would like to highlight our recent innovative partnership with the State of Connecticut to redevelop, operate, and maintain Connecticut's 23 highway service areas across the state.

In this case, our fund formed a 35-year public-private partnership with the State of Connecticut to finance the redevelopment and operations of highway service areas at a time when the Connecticut state budget was under great stress. We were able to create a project that garnered support from all sides of the political landscape, as well as important stakeholders in the business community, organized labor, local communities, law enforcement, and environmental groups. Carlyle and our partners plan to invest approximately $180 million in improvements and upgrades to the service areas over the next five years, investments that we estimate will create approximately 375 additional permanent and construction-related jobs – a 50% increase above the 750 jobs that supported the service areas before we started our project. In total, the state is expected to receive nearly $500 million in economic benefit from the redevelopment effort.

Our partnership with the state of Connecticut is a good example of the benefits of innovative financing and project delivery. State and federal entities benefit when the best attributes of publicly-owned infrastructure are combined with private sector capital and expertise to create genuine partnerships. Creating innovative funding models -- including a national infrastructure bank -- would help develop projects along the lines of Connecticut.

In that context, I will focus on three general points this morning:

1. The need for innovative financing in critical infrastructure, and the opportunity it presents for genuine partnerships between the public and private sectors;

2. The establishment of an infrastructure bank as a means to develop innovative financing and to aid the delivery of infrastructure improvements;

3. The need for transportation policy reforms that must accompany innovative financial practices in order to maximize private investment.

1. Innovative financing – particularly direct private investment -- is essential to reforming our nation's transportation funding public policy.

The condition of our national infrastructure and the reliance of our nation's economic security on increasing the capacity of our national transportation system are welldocumented.[2] Furthermore, this Committee is keenly aware of the shrinking federal, state, and local resources available to address these needs.

As former Secretary of Transportation Norman Y. Mineta said in a speech last April:

"What traditionally has been a quantitative funding issue for our nation's infrastructure has now become a qualitative policy issue. In other words, fighting the perennial battle of getting more money from traditional sources won't suffice. The needs are great – and getting greater -- and more money isn't coming.[3]"

This shift from "how much to fund" to "how to create more funding" as described by Secretary Mineta is an important opportunity for this Congress. Financial experts estimate that the amount of available private sector equity capital raised to invest in global infrastructure assets is $38 billion.[4] Several major financial institutions and a growing number of private equity firms have formed infrastructure funds to invest in various infrastructure assets. In addition, several pension funds representing public and private sector employees have identified the benefits of infrastructure investments: the potential to receive increased returns over government-issued securities, at lower risk than traditional equity investments. Recently, Richard Trumpka, the president of the AFL-CIO announced that organized labor would invest more than $10 billion in U.S. infrastructure.[5]

By making programmatic and regulatory changes in federal law, Congress can encourage state and local governments to develop innovative financing models that access this available private capital. It is important to note that advocating well-crafted funding models that access direct private investment does not mean selling off America's public infrastructure to private interests as some have asserted.

The assumption that critical infrastructure projects must be either publicly-financed or privatized is a false choice. State and local officials responsible for infrastructure project delivery do not have to be limited to a set of binary decisions if they want to consider leveraging private investment: organized labor vs. a non-union workforce; existing permitting procedures vs. relaxed environmental standards; or using public debt vs. surrendering public control to private interests. Innovative funding models can provide a third way for designing, building, operating, maintaining, and financing our capital projects.

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[2] See studies, *2009 Report Card for American Infrastructure,* American Society of Civil Engineers, March 25, 2009; *Well Within Reach: America's New Transportation Agenda,* the Miller Center of Public Affairs at the University of Virginia, October 4, 2010.

[3] *"Should there be a National Infrastructure Bank?"* Norman Y. Mineta, Speech before the U.S. Chamber of Commerce, April 12, 2010.

[4] *"Road Map to an American Partnership"* The Combined Infrastructure Working Group, June 2009.

[5] *"AFL-CIO Announces Major Commitment to Action on Infrastructure Investment and Training,"* AFL-CIO press release, June 29, 2010

At Carlyle, we believe these goals can be accomplished by developing genuine partnerships with public officials and other key stakeholders. As I outlined in describing the characteristics of our Connecticut project, innovative planning, stakeholder involvement, and a commitment to taking the best elements from the public and the private sides can create a project that accesses new sources of capital in a way that supports new infrastructure development.

2. The establishment of an infrastructure bank as a means to develop innovative financing and to aid the delivery of infrastructure improvements.

A national infrastructure bank can accelerate large capital projects by leveraging direct private investment into projects that are critical to the nation's infrastructure.

Several international entities have implemented infrastructure banks, and we can learn from their experiences. The European Investment Bank (EIB) is one and there are others. Giving states and regions the opportunity to access this funding with U.S. government backing would be critical and should not threaten Congressional prerogatives. The EIB provides loans and makes guarantees. The loans and guarantees are expected to be repaid or extinguished.

The EIB lends money for very long terms (e.g. 40 years) at a low interest rate and, in doing so, provides for a level of subordinated capital that allows other participants, both banks and private sector investors, to participate in a project that would otherwise struggle to obtain financing. The lending policy of the EIB is driven by the government, but the actual credit decisions on specific loans and guarantee proposals presented to the bank are determined by a professional staff operating independently within the bank.

This process achieves an important policy goal. Congress and other federal decision makers would still determine the appropriate policy goals: identifying the targets for infrastructure investment; prioritizing modes of transportation; deciding where to increase capacity; testing new infrastructure technologies; and determining other critical policy questions. The bank's expertise can help assess the creditworthiness of a certain class of projects and determine whether these projects can gain investment funding, or if they should be viewed in a different category of projects that merit funding from the federal government and other state and local sources.

Congress should look at the infrastructure bank as a true bank that must make difficult credit decisions. The institution's primary purpose is to lend to large projects with long-term maturities at a small margin over its borrowing cost. The bank would provide a project with a base of capital that could then attract, either at the same time or later, outside private investment that we need to support our nation's infrastructure. The bank should cover its costs, but not operate as a profit-making venture. The purpose of the bank should be to utilize its expertise to attract additional investment from the private sector for public infrastructure priorities, rather than replacing existing funding from government institutions.

3. For innovative financing practices like the infrastructure bank to be successful, Congress must provide additional reforms to our current transportation public policy.

The creation of an infrastructure bank should be a manifestation of deeper, more profound changes to our national transportation policy; otherwise the bank and other innovative practices risk contributing to existing shortcomings in our transportation financing policies. Specifically, outcome-based performance standards should be encouraged at the baseline policy level. Clear, transparent, and concrete performance metrics are needed to measure the success and benefits of major transportation projects.

Life-cycle costs should be an established criterion when evaluating a major capital project. Without it, an "apples-to-apples" comparison of the benefits of private investment vs. public debt financing is not possible and a flawed "cost of capital" analysis of the private investment option is likely. Additionally, requiring rigorous standards for analysis of expected users of a project, such as traffic studies, should be implemented so that accurate projections that affect costs and benefits are possible.

Congress should establish measurable performance metrics on the economic benefits of a major project, or the environmental benefits a infrastructure project will provide.[6] Such standards will provide financing entities like the infrastructure bank with the ability to provide more extensive and more accurate data to better assess the impact and worth of an infrastructure project.

Having innovative financing models – including an infrastructure bank -- that attract private capital directly to critical infrastructure projects will bring other benefits with respect to how projects are completed. These benefits include increased accountability and a shifting of financial risk from taxpayers to investors; unlike funding received from public debt financing, the private investment partner assumes the risk of success or failure. The private partner works with the public partner throughout the entire spectrum of the project – the design, construction, operation, and the maintenance. Therefore, the private partner has a different role, and risk equation, than a bondholder because the private partner is accountable for the project being completed on time and on budget.

Mr. Chairman and Members of the Committee, the need for investment in our nation's infrastructure is significantly larger than any one revenue source, and there is a need to design policies to access different revenue sources while being good stewards of the nation's infrastructure and meeting the challenges its current condition presents. A national infrastructure bank is one method by which private investment can serve as one

[6] "*Transitioning to a Performance-Based Federal Surface Transportation Policy*" The Bipartisan Policy Center, June 23, 2010.

of those revenue sources. Coupled with genuine reform, the bank could provide needed funding for our national infrastructure.

Thank you once again for the opportunity to testify.