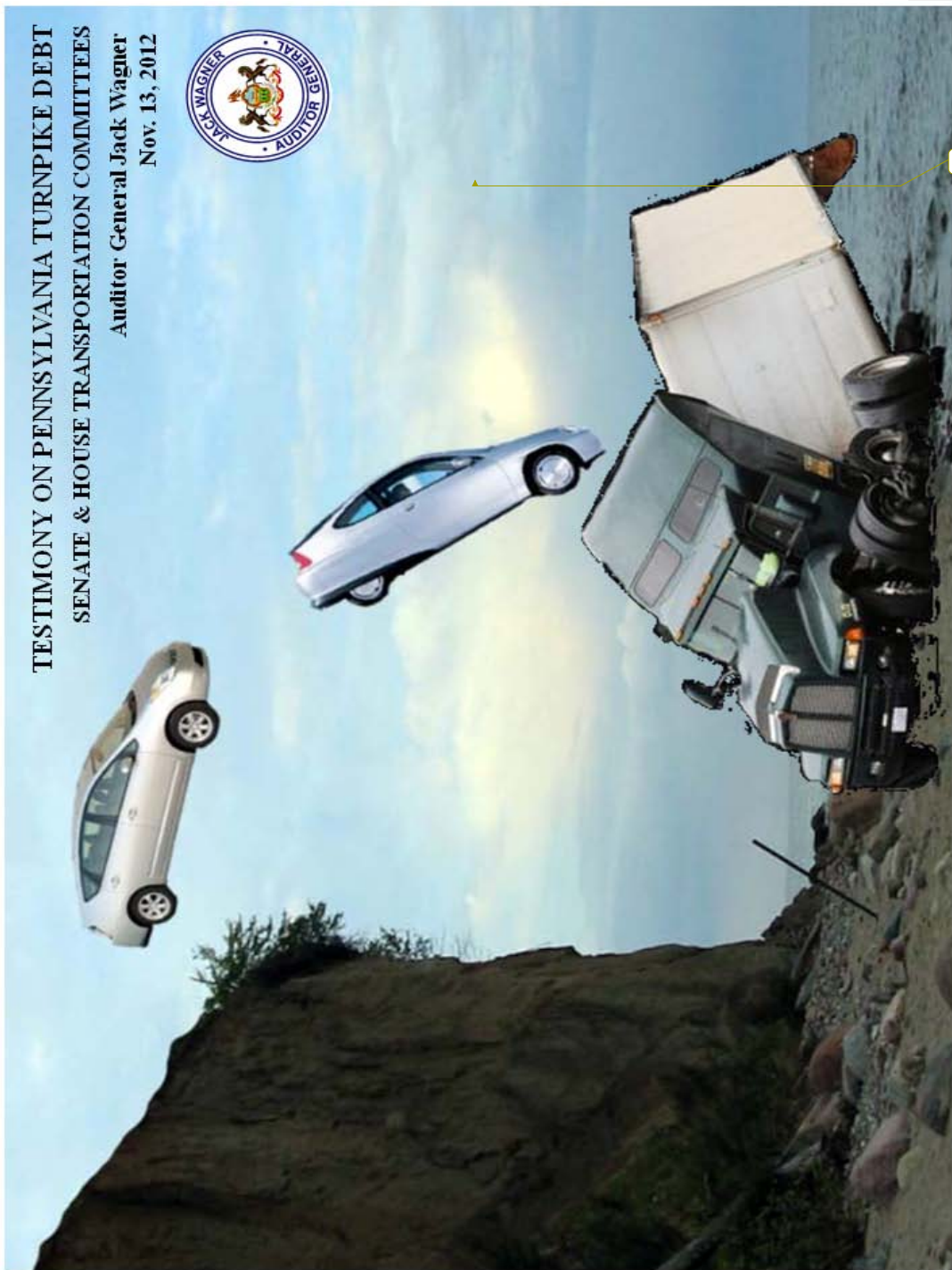


TESTIMONY ON PENNSYLVANIA TURNPIKE DEBT
SENATE & HOUSE TRANSPORTATION COMMITTEES

Auditor General Jack Wagner
Nov. 13, 2012



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Department of the Auditor General
Jack Wagner

Nov. 13, 2012

Good morning, Chairman Rafferty, Chairman Wozniak, Chairman Geist, Chairman McGeehan and members of the Senate and House Transportation Committees. Thank you for the opportunity to provide additional context to the testimony I provided you several weeks ago on the impending debt crisis at the Pennsylvania Turnpike.

At the previous hearing, we heard testimony from Turnpike CEO Roger Nutt downplaying the turnpike's mounting debt. He said, "...there may not be any financial crisis if we manage things as we are."

I respectfully disagree. The turnpike's debt addiction is not something that can be managed away, as if it were nothing more than an administrative nuisance. It is similar to the fiscal problem of the city of Harrisburg, the Delaware River Port Authority, and the country of Greece.

In fact, all of this borrowing threatens the very existence of the Pennsylvania Turnpike. And it could put hard-working Pennsylvania taxpayers on the hook for billions of dollars in additional debt they didn't ask for and cannot afford. Because if the turnpike defaults and cannot make its debt payments, those obligations will fall to Pennsylvania taxpayers.

During the recently concluded presidential election, we heard great debate about the federal government's increasing debt problem. By comparison, it is far less severe than the Pennsylvania Turnpike's.

Over the past four years, U.S. debt has risen by about 50 percent. By comparison, the Pennsylvania Turnpike's long-term debt has skyrocketed by 200 percent over the past five years, since the enactment of Act 44 in 2007.

The net result of all this borrowing is that the Pennsylvania Turnpike's debt load has increased from \$2.6 billion to \$7.8 billion.

Since 2009, the turnpike's total net assets have plunged 1,318 percent, from a surplus of \$156 million to a deficit of \$1.9 billion. In layman's terms, what this means is that if the turnpike were a house, its mortgage would be considered underwater, because its value is now less than the total debt that has been placed upon it.

The only way the turnpike can continue operations, pay its debt, and keep borrowing money is by raising tolls on motorists. In other words, the turnpike is living hand-to-mouth, and has become little more than a pass-through, transferring fees from Pennsylvania motorists directly to Wall Street investment firms. During the fiscal year ended May 31, 2007, the turnpike paid \$179,032,000 in debt service payments; during the fiscal year ended May 31, 2011 the amount that the turnpike paid in debt service payments had increased to \$352,455,000.

This is not a sustainable business model for the long term. At some point, there will be a tipping point, at which motorists stop using the turnpike and use alternative highways because the tolls are too high. In terms of vehicle ridership on the Pa. Turnpike, the debt load per vehicle is significantly higher than it was in 2007. The debt load per vehicle as of May 31, 2007 amounted to \$8.93 compared to \$34.29 as of May 31, 2011, according to turnpike data. It's hard to say precisely when that tipping point will be reached or even if it has been reached...because the trouble with tipping points is that they are seldom recognized until after they have been passed. In other words, they are apparent only in hindsight.

At the last hearing we also heard testimony that attempted to minimize the cost of debt service to the turnpike. It was estimated that the cost of borrowing \$450 million a year, which the turnpike must do to provide Act 44 funding to the Pennsylvania Dept. of Transportation, was \$35 million per year. But, again, that is a false and misleading sense of manageability. It's like buying a \$2,000 flat-screen TV on your credit card and then making only the minimum monthly payment. Most of the monthly payment applies to interest charges and not the principal. For the fiscal year ended May 31, 2007, the turnpike paid \$121,952,000 in interest payments. In

comparison, for the fiscal year ended May 31, 2011, that number had increased to \$281,885,000 in annual interest payments.

Also at the last hearing, we heard testimony that the turnpike's borrowing must not be so bad because the Wall Street credit agencies have given its long-term debt a favorable rating. Let's not forget, it was these same agencies that gave favorable ratings to the exotic mortgage-based derivatives that collapsed the economy in 2008 – and that, again, we didn't realize were misleading until it was too late.

These Wall Street firms have a vested interest in giving favorable ratings to the turnpike debt because they are collecting fees and making profits off of this borrowing. In fact, they already have sold the Pennsylvania Turnpike hundreds of millions of dollars of interest-rate swaps that could backfire and cost Pennsylvania millions of dollars if the turnpike has guessed wrong on which way interest rates will move in the future.

I don't need to remind anyone in this room that Pennsylvania has not fully recovered yet from the 2008 financial collapse that have cost us millions of jobs, billions of dollars, and a declining standard of living. With state tax revenues still flat and millions of Pennsylvania families still struggling, now is not the time to be gambling away the commonwealth's future.

The Pennsylvania Turnpike's borrowing is reckless and it poses a grave danger to all Pennsylvania taxpayers, because they will be responsible for assuming these obligations if the turnpike defaults on its debt.

America's first superhighway is no longer super with a fiscal noose around its neck called Act 44. I call again on the General Assembly to repeal Act 44 and relieve the Pennsylvania Turnpike of its obligation to provide \$450 million annually to the Pennsylvania Dept. of Transportation.

Thank you.

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