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The Waste in Maintenance

If the General Assembly doesn't tackle the $200 million-a-year waste in road maintenance, lawmakers can't even pretend to be serious about curtailing state spending.

Early in a contract with the Virginia Department of Transportation, inspectors at VMS Inc. spotted a rough patch on Interstate 95 north of Richmond, near the Parham Road interchange. The company, which has a 10-year contract to maintain 1,250 lane-miles of Virginia's Interstate system, paved it over. Two years later, the same stretch of road started falling apart again.

When VMS engineers took a closer look, they discovered that there was a creek running under the road. The moisture was affecting the entire roadbed and accelerating the rate of deterioration of the pavement on the surface. Even though VMS was not contractually obligated to make capital improvements, it paid the expense of installing under-drains out of its own pocket.

Without the drains, explains VMS President Rich Herlich, the company faced the prospect of repaving the Interstate four more times over the life of its 10-year contract. It was cheaper to fix the underlying problem.

The repair worked. Says Herlich: "We haven't touched it since."

In theory, VMS didn't do anything that VDOT couldn't have done if it had been maintaining that segment of the Interstate itself. But that's not how VDOT conducts business. Herlich contrasts VMS's actions with a similar case near Fredericksburg. There's a spot that VDOT has repaved three times in the past 10 years, he says, because of water problems under the road.

The difference between VMS employees and VDOT employees isn't one of intelligence, expertise or professionalism: It's the incentive structure the two organizations are working under. As a profit-making enterprise with a 10-year contract, VMS concluded that it was more profitable to fix the drainage problem. VDOT, which operates in two-year budgetary framework, calculated that it made more sense just to keep on patching.

Therein lies a story. Acting on the premise that the state lacks the funds to build enough roads to relieve traffic congestion, Gov. Timothy M. Kaine has proposed raising nearly $1 billion a year in transportation-related taxes. The state Senate wants to raise somewhat more money through a different mix of tax increases. And the House of Delegates, though resistant to the idea of raising taxes, proposes diverting revenue streams from the General Fund to the Transportation Trust Fund.

The common thread of each set of proposals is that the Virginia's transportation system requires endless infusions of money. In other words, it's easier to suck the money out of the taxpayers (or the General Fund) than it is to press the state bureaucracy to conduct its operations in a most cost-effective manner.

Herlich estimates that the state could save about $200 million a year by outsourcing the maintenance of all of its Interstates as well as its primary and secondary roads -- that's about 20 percent of the nearly $1 billion a year the state spends on maintenance. And that's just today. VDOT anticipates that rising costs in the construction sector will inflate maintenance costs by four percent annually, while the addition of roughly 200 miles of road each year to the VDOT system will add another half a percent annually. At that rate, maintenance costs will double in another 15 to 16 years -- bringing potential savings from outsourcing to $400 million a year.

Admittedly, those sums, as large as they are, doesn't close the entire transportation funding gap that our solons foresee, nor do they touch a major underlying cause of traffic congestion, Virginia's dysfunctional pattern of land use. Furthermore, I'm well aware that Herlich has an axe to grind. As one of two companies to whom VDOT currently outsources Interstate maintenance, VMS surely stands to gain a lot of business if legislators heed his advice. But even with all those caveats, Herlich offers an incisive critique. Virginians need to listen to him.

Perhaps surprisingly, given his perspective, Herlich is not a VDOT basher. He actually considers VDOT one of the best run state transportation departments in the country. "I tell people to visit other states," he says. "VDOT has a heck of a road system."

Virginia's philosophy is to make road maintenance the top funding priority, and then to pay for new construction with what's left over. By contrast, in many states the philosophy is to build the roads, perform minimal maintenance, go back to the federal government for more money and fix what could have been maintained for a fraction of the cost through timely repairs.

"We've submitted proposals to more than 20 states, and we've taken a close look at their roads," Herlich says. "Go to Missouri. Ride on Interstate 40 between St. Louis and Jefferson City. It's in terrible condition. The answer is, they don't care. Virginia never had that mentality." By his standards, Virginia and Florida have the best-maintained roads in the country.

The problem isn't the engineers at VDOT -- it's the rules they work under. In a free-wheeling conversation with Herlich, I identified four major reasons why, despite VDOT's reputation as a superior transportation department, out-sourcing makes sense.

Time horizon. Virginia's two-year budgetary cycle creates a perverse set of rewards. VDOT has an incentive to spend every dime in the budget, whether the expenditure makes sense or not. If the department doesn't spend it, it risks losing it in the next budget cycle. "In the past, the state paved 10 percent of its roads every year," Herlich says. "You had some pretty good roads that didn't need to be paved but got paved just to spend the money."

Likewise, the short-term focus creates a partiality to patching problems over rather than identifying underlying causes and fixing them with funds not allocated in the two-year budget. But the cost of repairs can increase at a geometric rate. "Pay me now or pay me later," says Herlich. "You're not talking about an asphalt resurfacing at $60,000 per lane-mile. You're talking a complete reconstruction at $1 million per mile!"

Accountability. Outsourcing creates someone to hold accountable. VMS's maintenance contract requires the company to meet 65 specific performance standards covering everything from the size of pot-holes to the condition of the guardrails, from the reflectivity of lane stripes to the height of the grass along the road. (Believe it or not, grass is not merely an aesthetic issue -- it affects motorists' field of vision, and it also affects drainage around the roads.)

VMS gets penalized financially if it fails to meet the performance standards. Who gets punished when someone falls short at VDOT? "VDOT isn't going to penalize itself. VDOT isn't going to give itself liquidated damages," Herlich says. The fact is, VDOT has a much bigger stick to enforce standards when it's dealing with a private contractor than when it's dealing with its own organization.

Flexibility in sub-contracting. VMS can perform work less expensively because it enjoys considerably more latitude in whom it sub-contracts to. VMS doesn't actually perform the maintenance with its own crews. It *manages* the maintenance and sub-contracts the actual work to private crews. VDOT suffers significant disadvantages. State rules limit bidders on contracts to companies that meet various licensing and bonding requirements. Typically, only a handful of large companies meet those requirements.

"We can go out and find contractors that never worked on an Interstate," Herlich says. "Mowers who work in an office park but never worked on an Interstate. Ironworkers to work on a guardrail. VDOT can get two bids, I can get 10."

Innovation and risk. VDOT employees, like most state employees, have an aversion to risk. Says Herlich: "If you're a VDOT official and try something that turns out wrong, nobody's going to say, 'Good try.'" No one ever got in trouble by sticking to the budget.

VMS, by contrast, encourages creative solutions and responsible risk taking. The company contracts with VDOT to maintain roadway standards at a fixed price for 10 years at a clip. If the company can find a way to save money, the savings go to its bottom line. As a consequence, VMS scours the country -- indeed, the world - for better ways to do things.

"As a private company," says Herlich, "we think something will work because it's worked other places. If it doesn't work, we'll fix it."

How much money could the Commonwealth save by outsourcing its road maintenance? It depends on how you count the numbers, of course. The state of Florida, which has outsourced 50 percent of its Interstate maintenance, says that it was saving 15 percent to 18 percent on the most routine maintenance tasks like filling potholes. The potential is considerably greater when the ability to think longer term is taken into account.

Herlich contends that VMS has saved the Commonwealth about 25 percent so far on its Interstate contract. Some in state administration may argue that the number is high, but the fact is, no one really knows. VDOT's books aren't set up in such a way as to readily calculate a number. Herlich suggests that VDOT savings would be *higher* if the bean counters took into account VDOT's overhead like insurance, pensions, legal expenses and environmental compliance

The comparison is a little trickier with secondary and primary roads, a realm where voters have an expectation that they can call up their local delegate and get a pothole fixed on their street. But Herlich thinks that savings of 20 percent are achievable.

Even if Herlich errs on the optimistic side, that's still way too much money to ignore. While some in the General Assembly equate fiscal responsibility with raising taxes, we can be grateful that at least a few are looking for ways to save money. Del. Leo Wardrup, R-Virginia Beach, has submitted a bill that would require all maintenance on Virginia's Interstate highways to be "carried out under competitively bid contracts awarded by the Commonwealth Transportation Board." (See HB 667.)

The fate of Wardrup's bill will serve as a barometer for the General Assembly's willingess to address Virginia's transportation woes through structural reform rather than higher taxes. It's only a start, but it's a darn good one. If legislators have the best interests of the citizens and taxpayers in mind, they need to give it fair consideration.

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