



The Senate's Assault on Transportation Public-Private Partnerships

by Baruch Feigenbaum



INTRODUCTION

In March 2012, the U.S. Senate approved its MAP-21 surface transportation reauthorization bill. While MAP-21 has a number of parallels with H.R. 7, it also contains several provisions intended to discourage and restrict the use of long-term public private partnerships (PPPs) for transportation infrastructure. This brief describes those provisions and explains how and why they would deprive states of a much-needed tool for expanding investment in highways and transit.

DEFINING TRANSPORTATION PPPS

Public-Private Partnerships (PPPs) for infrastructure are long-term contracts between public and private entities for the financing, construction (or reconstruction), operation and maintenance of specific infrastructure facilities. PPPs are used for both highway and transit projects. State departments of transportation, public transit agencies and highway contractors

all support PPPs. PPPs are one of the few infrastructure development mechanisms supported by both the Brookings Institution and the Heritage Foundation.

PPPs are a method of financing a project by raising all the needed construction funds up front and paying them off over time from dedicated revenues (such as tolls or a dedicated transportation tax). This enables states and the federal government to overcome the problems created by traditional highway funding mechanisms, which involve paying with cash from current tax receipts. Such cash funding means that large projects are either (a) deferred for many years until all the funds are saved up, or (b) built in bits and pieces over a long period of time.

PPPs deliver needed transportation infrastructure years or even decades sooner than when financed with cash. Over the past two decades, nearly 40 long-term transportation PPPs have been financed in the United States. PPP toll projects are under construction or in operation in a growing number of states, including California, Florida, Indiana, Illinois, Texas and Virginia.

PPPs have significant advantages over conventional procurement methods, especially for major projects.

- PPPs shift risk from taxpayers to investors, increasing the likelihood that the project will be completed on time and within budget.
- PPPs provide a more business-like approach, ensuring proper maintenance over the life of the project.
- Operating as business entities, PPPs are more customer service-oriented.
- PPPs are also known for “value-engineering,” which reduces project construction costs.
- PPPs enable innovations such as variable tolling, which was introduced to the U.S. by a private company in California.

Private Activity Bonds (PABs) are tax-exempt bonds for PPP projects. PABs were first authorized for highway and intermodal projects by the SAFETEA-LU reauthorization. PABs are issued by or on behalf of a government for the purpose of financing projects developed under long-term PPP agreements. These bonds increase private-sector involvement by enabling private developers/operators to access the same kind of tax-exempt interest rates available to public-sector projects. This lowers the cost of capital, allowing PPP projects to be more competitive than would otherwise be the case.

PABs may be used for any highway or intermodal project that receives federal assistance under Title 23. This includes any project for an international bridge or tunnel built by an international entity authorized under federal or state law that receives federal assistance under Title 23. Eligible intermodal projects that receive federal assistance under Title 23 or Title 49 are those used for the transfer of freight from truck to rail or rail to truck.

PABs have been a part of highway and intermodal transportation financing since they were authorized by SAFETEA-LU in 2005. Their use for other modes of transportation infrastructure dates back to 1968, with Congress broadening the eligible categories over time. Prior to SAFETEA-LU, PABs could be used for airport facilities, docks and wharves, high-speed rail and mass transit—but not highways.

THE ANTI-PPP PROVISIONS IN S.1813

Section 40309, starting on page 1457, line 24 and titled “No Private Activity Bond Financing of Applicable Leased Highway Property,” prohibits the use of PABs to finance the acquisition, via lease, of an existing toll road that may need capacity additions or complete reconstruction. In addition, since a state DOT may use the lease proceeds to pay for other new-capacity investments elsewhere in the state, this provision



The Chicago Skyway is an example of a toll road that was privatized via long-term lease. Illinois has received a \$1.83 billion cash infusion from the lease proceeds to pay off debts.

could also reduce the extent of such investment. Current law already prohibits the use of PABs to finance the acquisition costs of an existing (“brownfield”) toll road. But the language of this provision could preclude the subsequent use of PABs to finance major capital improvements to the leased toll road. It could thereby deter much-needed investment to reconstruct aging toll roads and/or to add new lanes to them.

Section 40309, starting on page 1455, line 3 and titled “Depreciation and Amortization Rules for Highway and Related Property Subject to Long-term Leases,” lengthens the amortization and depreciation period for PPP projects from the current 15 years to 45 years. PPP projects are structurally identical to investor-owned utilities, which (similar to virtually all businesses) can use accelerated depreciation. By singling out PPP projects for discriminatory depreciation rules, this provision would significantly reduce the returns available to investors in such projects, thereby making such investments less attractive—and therefore less likely to occur.

Section 1105, starting on page 53, line 17 and titled “Further Adjustments to Privatized Highways,” reduces a state’s federal highway apportionment by the amount of privatized miles that were originally publicly financed. This provision is specifically intended to make PPPs less attractive to states, by reducing their level of federal funding the more they engage in self-help efforts to supplement federal funding. This sends exactly the wrong message to states that seek to leverage their limited federal funding so as to make responsible investments in transportation infrastructure.

The Indiana Toll Road and the Chicago Skyway are two examples of toll roads that were privatized via long-term leases. While such leases may not be appropriate for every state, both Illinois and Indiana have received substantial benefits. Illinois received a \$1.83 billion cash infusion while Indiana received \$3.8 billion. Both states used lease proceeds to pay off debts, and Indiana used much of the proceeds to fully fund a 10-year highway investment program.

Some worry that the private sector will continually hike tolls or neglect maintenance. Neither of these is permitted by the terms of the long-term lease agreements. Drivers on the privately operated Indiana

Tollway pay \$4.65 to travel 152 miles, which is 3 cents a mile. The Indiana Tollway private operator will invest \$4.4 billion in road repairs and upgrades during the term of the lease, including the addition of new lanes in congested northwest Indi-

ana. Meanwhile, drivers on the publicly operated Ohio Turnpike pay \$11.25 to go 236.4 miles, which is 5 cents per mile. Ohio is just beginning to widen its portion of the Turnpike. In New Jersey, drivers on the publicly operated New Jersey Turnpike pay \$10.40 to travel 113 miles, which is 9 cents per mile. New Jersey cannot afford to widen all of its congested Turnpike segments.



WHAT THE HOUSE CAN DO TO FIX THIS PROBLEM

The House should ensure its reauthorization bill does *not* include any of the anti-PPP provisions of S.1813, such as:

- Reallocating any funds from one state to another based on its use of PPPs;
- Imposing discriminatory depreciation rules on PPP projects;
- Restricting the use of PABs for PPP projects.

On the positive side, the House bill could include PPP-friendly language such as:

- Ensuring that PABs are available for all qualified highway and intermodal projects by removing the current cap of \$15 billion authorized under SAFETEA-LU. This cap serves no useful purpose, as projects can only utilize PABs if they are vetted as credit-worthy by the bond markets;
- Exempting PABs permanently from the alternative minimum tax;
- Allowing deferred interest payments for PABs;
- Allowing the use of PAB proceeds for land acquisition costs of up to 25% of total project costs as compared to 25% of bond proceeds.

WHY ATTACK NEEDED FINANCING MECHANISMS?

PPPs are a critical financing mechanism that states need to increase investment in needed infrastructure projects. The anti-PPP provisions clearly violate the prerogatives of states. Washington D.C. already tells states how to construct highways, how to conduct environmental reviews, how to hold public hearings, how to safeguard archeological relics, etc. Many of these federal regulations substantially increase construction costs. The proposed anti-PPP provisions would limit financing options for these projects. The federal government should not be restricting states' options, especially when it cannot afford to provide states with increased transportation funding. Supporters of anti-PPP language appear to be acting on behalf of special interest groups such as truckers (anti-tolling) and public employee unions (anti-PPPs). If enacted, such anti-PPP provisions will reduce needed national infrastructure investment.

PPPs provide employment, spur economic growth in the private sector, and, through corporate taxes, put much-needed cash in state and federal coffers without raising taxes.

Truckers overwhelmingly support the anti-PPP provisions because they seek to prevent any expansion of tolling. Trucks contribute a disproportionate share of wear and tear to highways. Pavement lasts two years longer on a section of the Georgia 400 that restricts trucks compared to a section that trucks use. Every 10% increase in a truck's weight causes 40% more wear and tear on a highway. Under the fuel tax system, trucks do not pay a proportionate share. Trucks are somewhat less fuel-efficient than cars but degrade highways substantially more than cars. Truckers oppose tollroads because they will have to pay something closer to their proportionate share. Tollroads typically charge 5-axle trucks about four times as much as automobiles. The American Trucking Association is effectively trying to ensure that truckers do not pay their fair share of highway maintenance costs.

Public employee unions (and some construction unions) also support anti-PPP provisions for their own selfish reasons. In PPPs the private sector hires its own workers. While some of these workers are non-unionized, others have full union benefits. In fact many PPPs provide management efficiencies that do not affect workers' rights or pay. Still, union employees typically earn a higher salary than the market rate. According to the Bureau of Labor Statistics, the average union wage of \$50,000 is far above the market rate of \$38,000.

PPPS HAVE A LONG RECORD OF SUPPORT

Former Presidents Ronald Reagan, George H. W. Bush, and Bill Clinton encouraged public-private partnerships. President Reagan created a President's Commission on Privatization, which laid out a privatization/PPP agenda for the federal government.

President George H. W. Bush issued Executive Order (EO) 12803 on Infrastructure Privatization in April 1992. The aim was to reduce federal barriers to privatizing (by lease or sale) state and local infrastructure assets (including airports and highways) that had received federal funding. EO 12803 directs federal agencies that have made such grants (including FHWA and FTA) to approve such requests. The only conditions attached to such transactions are that (1) the proceeds from the sale or lease be used in accordance with the provisions of the EO (and pre-existing federal law), and (2) that some sort of mechanism be in place (e.g., the long-term concession agreement) to ensure that the facility continues to be used for its original purpose and that user charges will be structured to protect users from abuse.

In 1994, President Clinton issued EO 12893 on Principles for Federal Infrastructure Investment, which complements Bush's EO (which remains in force). Clinton's EO directs each agency with responsibility for transportation (and water, energy and environmental facilities) to "seek private-sector participation in infrastructure investment and management" and seek to work with state and local governments to "minimize legal and regulatory barriers to private-sector participation." It also endorses market pricing for infrastructure.

Ten Largest U.S. PPP Projects

| Rank | Contract Amount (billions) | Project Name | Owner | Private Risk |
|------|----------------------------|------------------------------|----------------------|---------------|
| 1 | \$3.85 | Indiana Toll Road | IN Finance Authority | 75-year lease |
| 2 | \$2.80 | I-635 Managed Lanes | Texas DOT | DBFOM (Toll) |
| 3 | \$2.10 | Denver Eagle P3 Rail | Denver RTD | DBFOM (AP) |
| 4 | \$2.05 | North Tarrant Express | Texas DOT | DBFOM (Toll) |
| 5 | \$2.00 | I-495 HOT Lanes, VA | Virginia DOT | DBFOM (Toll) |
| 6 | \$1.83 | Chicago Skyway, IL | City of Chicago | 99-year lease |
| 7 | \$1.81 | I-595 Managed Lanes | Florida DOT | DBFOM (AP) |
| 8 | \$1.67 | Hudson-Bergen Light Rail, NJ | NJ Transit | DB/Equip+ O&M |
| 9 | \$1.36 | SR 130 Segments 5-6 | Texas DOT | DBFOM (Toll) |
| 10 | \$0.98 | Jamaica-JFK Airtrain, NY | Port Authority NY/NJ | DB/Equip+ O&M |

These executive orders enable the marketplace to best allocate resources. Sound business practices can provide substantial increases in productivity and efficiency that benefit both sectors in a public-private partnership. PPPs also provide employment, spur economic growth in the private sector, and, through corporate taxes, put much-needed cash in state and federal coffers without raising taxes. Without PPPs many elected officials will have to choose between raising taxes and cutting services.

MORE ON PPPS

While PPPs are not appropriate for every project, they help fill a vital financing role. Almost 40 transportation PPPs have been procured nationwide. The table above lists the ten largest.

CONCLUSION

PPPs are a much-needed tool that allows states to expand investment in highways and transit. This mechanism provides financing support that does not raise taxes. The provisions that discourage PPPs are an attempt by special interests to prevent truckers from paying their fair share of the costs of road construction and maintenance and to benefit members of public-sector unions at the expense of other construction workers and taxpayers. These provisions would make it more difficult for state and local governments to provide the kinds of transportation infrastructure that are necessary for a modern, competitive economy.

ABOUT THE AUTHOR

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RELATED REASON PUBLICATION

Robert W. Poole, Jr., *Why the House Should Give States Greater Tolling Flexibility* (Reason Foundation, April 2012).



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