



TRANSPORTATION ASSETS: CASH COWS?

The long-term lease of public assets is the latest scheme for public officials desperate to raise money without raising taxes. And we are talking big money.

- Chicago received an upfront payment of \$1.83 billion for a 99 year lease of the Skyway toll highway, walking away with \$1.3 billion after paying off the approximately \$500 million in outstanding revenue bonds.
- Indiana took in \$3.85 billion for a 75 year lease of its toll road, pocketing approximately \$3.6 billion after paying off debt.

Public assets capable of generating revenues in excess of maintenance and operation costs are new targets for deal makers and investors seeking long-term, reasonably certain income streams. While toll roads are getting the most attention, Chicago also leased four municipal parking garages for 99 years and is seeking to lease the city-owned Midway airport and the city's parking meters.¹

Investors will make their money from future users paying higher tolls and fees over the life of the agreements. Indeed, analyses of the Skyway and Indiana Toll Road deals show that the private operators will continue to receive income from higher tolls long after the initial payment is covered.²

If the goal is simply to get an upfront payment today for future revenues, public owners can do this without a private lease. Future revenue streams can be “monetized” or “securitized” by selling bonds without giving up operational control. The bonds would be secured by future tolls or other revenues.³ This is similar to the up-front payments governments obtained through the bonding of tobacco settlement payments.

Governor Corzine has proposed this approach for New Jersey. While retaining ownership of its toll roads, the state would form a non-profit, public benefit corporation (PBC) for the purpose of managing the roads. The PBC's concession agreement would include an upfront payment to the state of \$18.9 - \$23.9 billion⁴ raised through debt funding, potentially from a significant use of tax-exempt bonds. The state will have no obligation for this debt. These funds would be used to reduce existing state debt and fund transportation improvements. Any additional financial benefits from the roadways will remain under the control of the state. Regular toll increases are part of the plan.

Of course, public agencies might also be content to accept tolls and fees as they come into the treasury and increase them as necessary. This was the choice of the Harris County (Houston, Texas) Commissioners following a formal review of lease/sale options for their toll roads by three financial firms. These studies found that to get the best price from a private operator, the county would have to turn over most of its control over future toll increases. One of the firms advised the Commissioners that they could imitate the private firms' practices in seeking to increase profits.⁵

With bonding or profit-oriented public operations as options, why is there a focus on private leases? Keeping these assets in public hands and generating surplus revenues -“profits”- requires raising tolls or fees, something public officials are reluctant to do, at least directly. Under a lease, increases are locked in from the start and in the out years public officials can hope the blame will be directed at the private operator. In Chicago and Indiana, concern about blame may have been softened because most of the toll road users are from other political jurisdictions. The bottom line – a vote for a lease is a vote for on-going toll or fee increases.

Legislative bodies should have a voice in shaping these transactions, including final approval. Consideration of the various alternatives should be required before any action is taken. Enabling legislation should provide for the protection of the existing work force and use of the proceeds.

The Illinois legislation allowing Chicago to lease Midway airport requires the private operator to pay employees “an amount not less than the economic equivalent of the standard of wages and benefits enjoyed by the lessor’s employees who previously performed that work.” In addition, the private operator and the city must offer employment “under substantially similar terms and conditions” to municipal employees working at the airport. There is also a labor neutrality and card check agreement covering unrepresented workers.⁶

As noted by Mark Florian, Managing Director, Goldman Sachs & Co., a leading promoter of leases: “It is possible for concession contracts to be written so as a concessionaire must use municipal employees for all or a portion of toll collection, maintenance, administration, etc.”⁷ Governor Corzine’s New Jersey proposal provides that the Public Benefit Corporation will offer employment to all employees currently working on the toll roads under the terms and conditions for current employee contracts.⁸

The Midway enabling statute also requires that at least 90% of the proceeds from the lease be used for infrastructure construction and maintenance and for contributions to the municipal employee pension funds. The Chicago Skyway payment was used to pay off city and Skyway debt, establish revenue generating reserves and fund social service programs. While most of the Indiana’s payment is dedicated to transportation funding, \$278 million was set aside to limit passenger vehicle toll increases through 2016.⁹

The bond rating agency Fitch reports that it “will negatively view the use of (lease/sale) proceeds for short-term needs of governments.”¹⁰

In addition to opposition associated with higher tolls, questions have been raised about the appropriateness and future implications of turning over control of critical assets to private operators. Pennsylvania Governor Rendell’s proposal to lease the state’s turnpike has met legislative resistance and Turnpike Commission opposition.¹¹ At a recent Congressional hearing Frank Busalacchi, Wisconsin Secretary of Transportation, asked:

“Should states be allowed to enter into long-term leases of the Interstate or National Highways that sell off – or lease for several generations – a part of our national system to a private entity? Is this in our national interest? Faced with uncertainty about future needs and goals, the states will try to spell out every detail of the partnership. But there is too much that is unknown about demographic trends, technological development, pollution concerns, equity needs, future congestion, and safety innovations. No contract, no matter how effective, can eliminate risk. We do not know enough to price or manage such long-term risks.”¹²

Representatives James Oberstar and Peter DeFazio, chairmen of the U.S. House of Representatives Committee on Transportation and Infrastructure and the Subcommittee on Highways and Transit, wrote to state governors and transportation leaders to

“...strongly discourage you from entering into public-private partnership (“PPP”) agreements that are not in the long-term public interest in a safe, integrated national transportation system that can meet the needs of the 21st Century. Although Bush administration officials have lauded PPPs at every turn, the Committee on Transportation and Infrastructure of the U.S. House of Representatives believes that many of the arrangements that have been proposed do not adequately protect the public interest. The Committee will work to undo any state PPP agreements that do not fully protect the public interest and the integrity of the national system.”¹³

Questions have also been raised about the wisdom of turning the operations of our critical public assets over to foreign owners, as has been the case for the Skyway and the Indiana toll road. In part, the November 2006 election shift in control of the Indiana House to the Democrats has been attributed to voter disenchantment with the lease that was championed by Republican Governor Mitch Daniels.¹⁴ In September 2006 a statewide poll found that 55% of likely voters disapproved of the lease, while 39 percent supported it.¹⁵ Under Republican control the lease passed the House 51 – 47, with all Democrats opposing.

With billions at stake for cash hungry governments, asset sales and lease agreements will continue to be offered up. But as John Foote, a senior fellow at Harvard’s Kennedy School of Government, former toll road industry executive and student of the Chicago and Indiana deals, advises:

“The public sector should not be seduced by the dollars without first examining all the issues...These deals aren’t always in the public’s best interests.”¹⁶

With regard to the public interest, Phineas Baxanall of U.S. Public Interest Research Group (PIRG) Education Fund finds:

“Although offering a short-term infusion of cash, privatization of existing toll roads harms the long-term public interest. It relinquishes important public control over transportation policy while failing to deliver the value comparable to the tolls that the public will be forced to pay over the life of the deal.”¹⁷

For more information on state policy issues, see: www.afscme.org/budgetandtaxes.

References and Notes

- ¹ “City of Chicago, Chicago Park District Close Parking Garage Concession Sale,” US States News, December 15, 2006; “Midway Airport Sale Given Go-Ahead”, Financial Times, October 5, 2006; “Airlines Leery of Midway Plan; Southwest, AirTran Question Privatization,” Chicago Tribune, September 22, 2006; “City Looking in Parking-Meter Lease”, Chicago Tribune, October 18, 2007
- ² Dennis J. Enright. “Then there were two...Indiana Toll Road vs. Chicago Skyway – An Analytical Review of Two Public/Private Partnerships – A Story of Courage and Lost Opportunity” NW Financial Group <http://www.nwfinancial.com/>, <http://www.paturnpike.com/PPP/pdf/indianatollroadfinal.pdf>
- ³ While the focus of this paper is on transactions involving existing infrastructure, related arrangements including upfront concession payments are also being proposed for new infrastructure. “More Tolls Down the Road North Texas Tollway Authority Set to Expand Vision, Role with New Projects.” Dallas Morning News, July 23, 2007, pg. 1a
- ⁴ State of New Jersey – Asset Monetization, January 2008, <http://www.state.nj.us/sos2008/background.pdf>
- ⁵ Bill Murphy. “Harris County Won’t Sell or Lease Toll Road; Financial Advisor Suggests Imitating a Private Company Will Boost Profits” The Houston Chronicle, June 21, 2006
- ⁶ Local Government Facility Lease Act, Illinois Public Act 094-0750 (Senate Bill SB2872, 94th Session) <http://12.43.67.2/legislation/publicacts/fulltext.asp?Name=094-0750>
- ⁷ Mark Florian, Managing Director, Goldman, Sachs & Co. House Transit and Pipelines Subcommittee, Hearing on Understanding Contemporary Public Private Highway Transactions – The Future of Infrastructure Finance, May 24, 2006 p. 3
- ⁸ New Jersey – Asset Monetization, pgs. 7,
- ⁹ Pat Guinane. “Public to Private – Leasing public assets to for-profit companies poses a tantalizing proposition for cash-strapped state and local governments” Illinois Issues Online, June 2006 <http://illinoisissues.uis.edu/features/2006june/public.html>
- ¹⁰ “U.S. Toll Privatizations: Seeking the Right Balance” Fitch Ratings - Special Report, March 22, 2006 p. 4 http://www.fitchratings.com/corporate/reports/report_frame.cfm?rpt_id=269604
- ¹¹ Pennsylvania Turnpike Commission, <http://www.paturnpike.com/ppp/>
- ¹² Frank J. Busalacchi, Secretary, Wisconsin Department of Transportation. Testimony on Protecting the Public Interest in Public Private Partnerships to the Subcommittee on Highways and Transit of the House Committee on Transportation and Infrastructure, February 13, 2007 p. 3 <http://transportation.house.gov/hearings/Testimony.aspx?TID=232>
- ¹³ The complete letter and a related position paper is available at <http://transportation.house.gov/news/PRArticle.aspx?NewsID=219>
- ¹⁴ Mary Beth Schneider and Theodore Kim. “Blue Streak: Indiana House tilts back to the Democrats” The Indianapolis Star, November 8, 2006
- ¹⁵ “Poll finds majority against Indiana Toll Road lease” The Associated Press State and Local Wire, September 18, 2006
- ¹⁶ Joseph A. Giannone. “Wall Street Sees Wave of U.S. Public Asset Sales” Reuters, December 7, 2006
- ¹⁷ Phineas Baxandall, Ph.D.. “Road Privatization: Explaining the Trend, Assessing the Facts, and Protecting the Public.” U.S. PIRG Education Fund. September 2007. Executive Summary, p. 1 <http://www.uspirg.org/home/reports/report-archives/transportation/transportation2/road-privatization-explaining-the-trend-assessing-the-facts-and-protecting-the-public>