Lease the Illinois Tollway? Public Ownership is Better

Transportation for Illinois Coalition
White Paper

January 2008

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The **Transportation for Illinois Coalition** is a diverse group of statewide and regional business, organized labor, industry, governmental and not-for-profit organizations that has joined together in a united and focused effort to support a strong transportation alliance for Illinois. The coalition takes a comprehensive approach and seeks to speak with one voice for all of Illinois regarding transportation funding needs at both the state and federal levels. The coalition believes that transportation is critical to the economy of Illinois. This comprehensive approach involves all modes of transportation, including rail, air, water, highways and mass transit.

Executive Summary

With the growing need for transportation improvements outstripping available resources, there has been nationwide interest in innovative funding methods. One of those methods is public/private partnerships. In Illinois, attention has been given to the possibility of leasing the Illinois Tollway as a means to raise money for the state.

In examining that concept, the Transportation for Illinois Coalition (TFIC) has identified a series of policy issues which would need to be resolved, has reviewed the tollway privatization study prepared for the Illinois Commission on Government Forecasting and Accountability (CGFA), and has assessed additional factors not included in that study.

While leasing the tollway to a private partner could raise substantial amounts, such sums would require very long leases and continuous toll increases throughout the lease period. Further, the proceeds from a lease could be substantially less if various options were included, such as: a toll freeze for a portion of the lease period; not allowing a non-compete clause; or adding a requirement for the private partner to fund future toll road improvements including reconstruction, additional lanes and extensions. Finally, TFIC has analyzed a public option, i.e., keeping the toll road public but raising tolls in the same manner as the privatization option would. TFIC has concluded that this public option is more efficient in that it would generate greater funding for transportation improvements. Or conversely, through more modest toll increases, the public option can generate substantial amounts for needed transportation improvements.

Based on all these factors, TFIC has concluded that public ownership of the existing toll road system is a better option.

Key points from the TFIC review include:

- The Illinois Tollway is a critical component of the state's and especially northeast Illinois' transportation network, stretching for 274 miles and serving 1.3 million drivers every day. **No action should be allowed which would put at risk the continued efficient operation of this vital asset.**
- Any funds which are generated from the toll road must be used for transportation purposes. **Illinois toll roads were paid for by the users; their payments should not be diverted to non-transportation purposes.**
- It appears that leasing the toll road to a private partner could generate as much as $5 billion to $18 billion for the state, after outstanding bonds were defeased. Tempering these sizeable estimates are the following factors:
  - — To generate such amounts, leases would have to last for at least 50 years; the $18 billion estimate required a 75-year lease.
  - — To generate such amounts, toll increases would have to begin immediately and occur every year; the $18 billion estimate required a 50% toll increase every 20 years plus a 3% increase annually.
  - — These estimates do not include any funding for major capital improvements beyond those currently underway as part of the toll roads

Congestion-Relief Program (CRP). During a 50 or 75-year lease term, needed major improvements to the toll road not accounted for in these lease estimates include reconstruction, adding lanes, and building extensions, such as western access to O'Hare. Including these improvements in the lease would reduce its value by as much as $4.5 billion. (It should be noted that once the first toll road segment was in place, the construction of all subsequent toll roads and extensions has been cross-subsidized by toll revenues from the existing system. A key concern of any lease discussion has been the need to preserve this financing method for future toll road needs.)

— These estimates do not include any provision for a toll rate freeze during the early years of the lease. While some have suggested including such a freeze, it also would reduce the value of any lease payments - by as much as $3.2 billion for a 10-year freeze. Further, at the end of the freeze period, tolls would have to be raised by as much as 100% to reach the level the tolls would have been had they been increased annually.

If the toll road were to stay public and to adopt the same aggressive toll increase schedule as a private partner, it could generate as much as $97 billion (net present value) for additional transportation improvements over a 75-year period.

— These estimates assume a non-compete clause, under which the region would have restrictions on expanding or constructing nearby facilities which could draw traffic from the toll road. But, northeast Illinois has a continuing need to expand its transit and highway facilities to serve growing transportation demand. A non-compete clause could jeopardize such projects.

— These estimates assume a one-time upfront payment. Extending the payments through the life of the lease would ensure an ongoing revenue source for transportation improvements. Further, it would avoid a situation where motorists continued to see annual toll increases long after the upfront lease payment had been spent. With the most aggressive toll increase regime (the $18 billion lease scenario), such annual payments would amount to $550 million, assuming the lease included a 10-year toll freeze and funding for future major toll road improvements.

— If the toll road were to stay public and to adopt the same aggressive toll increase schedule as a private partner, it could generate as much as $97 billion (net present value) for additional transportation improvements over a 75-year period. While the Illinois Tollway would be very unlikely to adopt such an aggressive toll increase schedule, it has adopted modest increases as necessary for toll road improvements. The most recent of these increases, which went into effect in 2005, is funding a $5.3 billion Congestion-Relief Program, including the newly-constructed I-355 extension.

- Keeping the toll road public would:
  - — Avoid the continuous toll increases necessary for a private lease arrangement; although, with such increases, public sector could generate even more funding than private sector for transportation improvements.
  - — Avoid the loss of direct control for the 50 to 75-year lease term. Because it is impossible to foresee what transportation changes or improvements would be needed during such a lengthy time, it would be important for any lease to include potentially expensive provisions for re-opening and modifying the contract.
  - — Assure that user fees were re-invested in the transportation system and not diverted to other uses.
  - — Assure that the toll road continued to comply with current (and future) statutes on labor, environment, competitive bidding, etc. While such compliance could be included in a lease, it would affect the value of the lease to a private partner.
  - — Assure that the toll road continued to be managed as an integral part of the overall transportation network, including coordinated planning, coordinated scheduling of maintenance and construction activities, cooperation with transit operations and extensions, and other activities to support northeast Illinois' overall transportation goals. That also would include the consideration of traffic diversions that would result from toll increases. The larger the toll increase, the greater the potential for traffic diversions, which could pose a problem for congested local and arterial roads in northeast Illinois.
  - — Avoid the conflict between the public's right to know and private sector's need to keep information confidential that typically occurs in negotiating a privatization deal.

While leasing toll roads to a private partner may work in some locations, for the Illinois Tollway it is the wrong option – creating numerous policy challenges, likely to be costly to consumers and likely to be less efficient than keeping the toll road publicly operated.

Overview

Nationwide, as transportation capital costs have overtaken available funding, a number of areas are considering innovative ways to generate additional revenue. One of those ways is through the lease of an existing transportation asset to a private partner. In exchange for payments from the private partner, the public agency enters into a long-term concession or lease arrangement giving the private entity the right to operate the facility, to raise and collect tolls on it and to keep the profits from the operation. That is what the City of Chicago did with the Chicago Skyway and what Indiana did with the Indiana Toll Road.

In Illinois, there has been discussion about the possibility of entering into a public/private partnership to lease the Illinois Tollway. During 2006, there were legislative hearings on the issue; state legislation was proposed to allow public/private partnerships; and the Illinois Commission on Government Forecasting and Accountability (CGFA) commissioned a study by Credit Suisse which examined privatizing the Illinois Tollway.

This paper examines the issue of leasing the Illinois Tollway to a private entity. It includes the following sections:

- Public Policy Issues: Identifies 11 public policy issues that need to be examined when considering a toll road lease; decisions on these issues would have significant impact on the value of a lease to a private partner.
- Analysis by Credit Suisse: Describes the methodology and results of the CGFA study on privatizing the Illinois Tollway.
- Critical Factors Affecting Lease Value: Reviews factors which could significantly change the value of a toll road lease.
- Comparison: Public Option Vs. Privatization: Compares the revenue generated by privatization with the revenue generated by keeping the toll road in public operation.
- Conclusion: Concludes that leasing the Illinois Tollway is not a good idea given the following:
  - — Privatizing the toll road would pose numerous public policy challenges which could limit the value of the lease.
  - — Privatizing the toll road would be costly to consumers, requiring annual toll increases which were not linked to toll road improvements.
  - — It would be less efficient than keeping the toll road publicly operated given the policy challenges and the fact that more revenue could be generated for transportation improvements by keeping the toll road in public operation than by leasing it to a private partner.

Public Policy Issues

The 274-mile Illinois Tollway system is not a discrete, stand-alone element of Illinois' transportation network. Rather, passing through 12 counties and serving 1.3 million drivers daily, the Illinois toll road is critical for the movement of people and goods in and through Illinois. With commuters comprising 75% of its traffic, the tollway has a daily impact on the people of northern Illinois.

Given the importance of the toll road system to Illinois, TFIC has identified 11 public policy questions which would have to be resolved prior to any lease agreement. These questions fall into three broad categories: financial, policy, and transportation. How each of these questions would be decided would have significant impact on the value of the lease to any potential private partner. Each of these issues is detailed below.

Financial Issues

- **Ability to Finance New Toll Road Additions**
  One of the traditional benefits of Illinois' tollway system is the ability to use the success of completed segments to help build new segments. The first toll road segment built, the Tri-State, had to pay for itself. All extensions since that time have been financed using the system as a whole since no new extension could cover its initial construction or operating costs. First the Northwest was financed using the base system, then the East-West, then the North-South in DuPage County and now I-355 in Will County. Leasing the system to a private partner would likely eliminate the ability for "cross-subsidizing" the construction of new segments. It might be possible to fashion a lease agreement that would require the use of toll revenues for constructing additions to the system, but that would significantly reduce the lease payment from the private partner.

- **Use of Lease Revenues**
  A long-term lease of the tollway has the potential to generate significant dollars. The Skyway lease in Chicago generated $1.8 billion, and the lease of the Indiana Toll Road generated $3.8 billion. In Indiana these moneys are to be used for highway purposes, while in Chicago they are not. In the public discussions of an Illinois toll road lease held during 2006, there were many ideas for how potential proceeds could be used. But TFIC believes this is critical: **Illinois' toll roads were paid for by the users; any funds generated for the public sector through a lease should be used for the benefit of the users.**

  A related question deals with whether the public is best served by a one-time payment of benefits or by payments stretched over many years. With a one-time payment to the public sector, funding can be quickly put to work and improvements realized, but the partnership provides no ability to generate funds for future needs. When payments to the public sector are stretched out over the life of the agreement, future needs can also be met. However, the amount of the annual payments could seem relatively modest in comparison to a single up-front payment.

- **Increased Costs to Users**

  In a lease arrangement, a private partner needs to generate enough revenue from tolls to cover the cost of the up-front payment to the public owner as well as to provide a return on equity to investors. In order to protect the public, partnership agreements generally will index future toll increases to an index like the Consumer Price Index (CPI). For example, the Skyway agreement allows 7.9% average annual toll increases through 2017 and toll increases after that at the greater of 2% per year, inflation, or nominal gross domestic product per capita.

  Public agencies, on the other hand, only raise tolls when it is necessary to meet increased costs or expansion needs that have to be justified and presented to the public before approval. Typically public owner toll increases do not keep pace with the CPI. In fact, for I-Pass users, tolls on the Illinois system have risen only 33% in nearly 50 years.

  In summary, what are the costs to the highway user for private as opposed to public financing and operation? Should the public have any input into future toll increase commitments? If so, how could that be accomplished within the framework of a public/private partnership?

Illinois' unfunded transportation needs are extensive. This year, TFIC recommended a $5 billion annual increase in Illinois' highway, transit, rail and airport programs.

- **Flexibility to Increase Other Transportation Resources**

  Illinois has a strong record of support for periodic transportation funding increases. However, the promises of additional money from a lease arrangement, without raising state highway user fees, could make future support for raising fees more difficult. Legislators who might be nervous about fee increases can point to private partnerships as a reason that public initiatives are unnecessary. To pass initiatives in the General Assembly, all parts of the state must benefit from the program. Focusing on just a toll road lease could make it more difficult to reach legislative consensus on a package that meets all of the state's transportation needs including rural widening/resurfacing and bridges, public transportation, passenger and freight rail, and other infrastructure investments.

  Illinois' unfunded transportation needs are extensive. This year, TFIC recommended a $5 billion annual increase in Illinois' highway, transit, rail and airport programs. How could a toll road lease agreement be structured to enhance future public initiatives or to be part of overall transportation funding strategies?

Policy Issues

- **Flexibility to Modify/Terminate Agreement**

  Privatization concepts look at very long lease times — 75 years in the case of the Indiana Toll Road and 99 years for the Chicago Skyway. Unforeseen circumstances can arise during that time which may necessitate the modification or termination of the agreement.

  For example, if the Illinois Tollway were leased, it is expected that the partnership agreement would include provisions for annual toll increases, to be

imposed by the private partner, in order for the private sector to make a profit. Most of the tolls are paid by Suburban Cook and Collar County residents. If the proceeds from the lease were used to benefit downstate and /or Chicago and the toll increases were perceived as "too high," it might be politically necessary to modify or terminate the agreement. In fact controversies did arise, fairly early in the lease period, concerning public/private toll roads in Toronto and in Orange County, California. In Toronto's case, the matter was in court for several years, with the courts ruling in favor of the private concessionaire. In California, Orange County was able to terminate its agreement, but at a cost of more than $200 million paid to the private partner.

Additionally, flexibility is needed to respond to changing transportation circumstances during the life of the lease. Today we cannot foresee what needs our transportation systems will have 30 or 40 years from now, and certainly not in 70 or 80 years.

How could a lease be structured to preserve the flexibility to respond to changing future circumstances?

- **Public Disclosure of Agreement Details**
  While public agencies are supposed to be transparent, private businesses strive to be opaque to protect proprietary information and maintain competitive advantages. As public/private partnerships are considered around the country, conflicts have arisen regarding the extent of the public's "right to know" **before** agreements are finalized.

- **Extent of Administrative Discretion**
  It is important to consider how much administrative discretion should be given to transportation agencies to negotiate and commit to public/private partnerships. The Chicago City Council had to approve the Skyway agreement. The Indiana state legislature had to approve the Indiana Toll Road agreement. What level of oversight or approval should be required for public/private partnership commitments? How much administrative discretion should be granted?

- **Compliance with Current Statutes on Labor, Environment, Competitive Bidding, etc.**
  Public agencies are required to adhere to state statutes and regulations with respect to numerous areas that are designed to protect the broad general public interest. These include:

  — Disadvantaged business enterprise law
  — Prevailing wage law
  — State procurement code requirements, including competitive bidding for construction
  — Qualification-based selection law for hiring engineering and design firms
  — Providing for an adequately staffed tollway system
  — Ensuring tollway employees have the right to join a union and bargain collectively for wages and benefits

How would a private entity ensure that some or all of these public policy goals were met?

Transportation Issues

- **Use of Non-Compete Provisions**
  The inclusion of "non-compete" provisions increases the amount a private partner would be willing to pay for a long-term lease since the private sector's risk is reduced by removing the

possibility of future transportation improvements being constructed in or near the corridor. While the Skyway agreement does not include a non-compete clause, the Indiana Toll Road agreement has a limited non-compete clause.

If included in a contract with a private partner, non-compete provisions could prohibit state, local and transit agencies from making future improvements in or near the corridor. In the case of the Illinois Tollway, there are a number of highway and transit improvements currently under consideration, including the O'Hare Western Bypass, completion of the Elgin-O'Hare Expressway, the Illinois 53 corridor in Lake County, the Illiana corridor, and the Metra Star line. Preserving state and local power to make these improvements (and other improvements which could arise during a long-term lease) is critical to maintaining a strong transportation system for the future.

- **Ability to Manage Road Network as a System**
  It is difficult enough today to coordinate and manage the transportation system in the Chicago area with IDOT and the Tollway managing the Interstate system; CTA, Metra and Pace operating the public transportation system; and six counties and hundreds of municipalities managing the local road system. Careful consideration would be needed as to how to integrate a private partner into the system.

  A private partner would manage its facilities to maximize returns to shareholders and investors, not to maximize public benefit. Frequently public and private goals are consistent, but not always. For example, increased use of public transit — a public policy goal — may not be compatible with the goal of maximizing toll revenues. Or, goals could differ with respect to the scheduling of major road construction. This scheduling should be coordinated among all transportation agencies in order to divert traffic from construction zones. But there is no incentive for a private owner to want to schedule work on its system so there is an alternate route available to the public during construction.

- **Impact of Traffic Diversions**
  As noted earlier, in order for the private partner to recoup investment and make a profit, public/private partnerships require ongoing toll increases. However, when tolls are increased significantly, a small portion of traffic will divert to other roadways, including local roads. Many roads in northeast Illinois are already congested or have not been constructed to carry traffic more appropriately handled by an expressway. Any consideration of a long-term lease should consider the likely extent and impact of traffic diversions due to increased tolls, including the type of traffic (truck vs. auto) that would divert and the roads that would receive the additional traffic (local streets, arterials, etc.).

Conclusion

The eleven issues detailed above must be reviewed as part of any toll road lease discussion. While it is likely that a lease agreement could be structured to deal with the issues, those decisions would play a large role in determining the value of the lease to a private partner.

Analysis by Credit Suisse

The public discussions that occurred in 2006 on leasing the Illinois Tollway focused quickly on the amount of money the state might realize from such a lease. The Illinois Commission on Government Forecasting and Accountability (CGFA) hired Credit Suisse (CS) to perform a financial analysis of the potential value of privatizing the tollway. The Credit Suisse study, released in August of 2006, examined various lease and sale options, estimated the revenues generated by each, and offered guidelines as to the manner in which a potential deal could be structured. (The "sale" option generated no support since it did not result in greater income to the state than the lease option and, unlike the lease option, would mean the permanent transfer of the facility from public to private ownership. Therefore, this summary will focus only on the lease option.)

Credit Suisse analyzed seven lease scenarios, based on three variables: the length of the lease; the timing and size of toll increases and estimated future traffic growth.

- Length of Lease: The lease lengths in the study varied from 25 to 75 years. The 25-year lease scenario was not financially viable.

- Timing and Size of Toll Increases: The toll increases varied from a low of 3% annually beginning in the year 2031 to a high of 50% every 20 years beginning in 2007 coupled with annual increases of 3% a year. The 3% annually beginning in 2031 was not financially viable.

- Estimated Future Traffic Growth: For all but one scenario, the study used forecasts through the year 2030 which were prepared by Wilbur Smith Associates (WSA) and included in an Illinois Tollway bond prospectus dated May 25, 2006; and for the period after 2030, the study used annual traffic growth of 1%. One scenario increased annual traffic growth at 1.5% above the Wilbur Smith projections, beginning in 2007.

Credit Suisse calculated estimated lease values using two methodologies: the Discounted Cash Flow (DCF) method and the Internal Rate of Return (IRR) method. The DCF method derives the value by computing the present value of the free cash flow using a weighted average cost of capital. (Free cash flow is the amount left over after all expenses have been paid.) Credit Suisse used a range of 6.0% to 6.9% for the weighted average cost of capital. The IRR method sets the value based on a desired rate of return for the investors.

The Credit Suisse study, released in August of 2006, examined various lease and sale options, estimated the revenues generated by each, and offered guidelines as to the manner in which a potential deal could be structured.

The following table below summarizes the Credit Suisse scenarios. Since the two valuation methodologies yielded similar ball park results, the table uses the middle of the range given for the proceeds under the Discounted Cash Flow method. Finally, the CS report did not reduce the estimated lease proceeds by the amount needed to defease outstanding Illinois Tollway bonds, although CS noted that this would have to be done and would cost around $2 billion. Therefore, the table shows net lease proceeds after paying $2 billion for bond defeasance although today's costs could be higher. (According to their 2007 Budget, the Illinois Tollway had $2.3 billion in debt outstanding at the beginning of the year, and expected to sell another $700 million in bonds during 2007.)

Summary: Illinois Tollway Lease Scenarios From Credit Suisse Report

Scenario	Required Toll Increase	Lease Term	Traffic Projections	Estimated Net Proceeds After Bond Defeasance ($ Billion)
#1.	3% annually starting 2031	75 years	Per WSA forecasts	($0.5)
#2.	3% annually starting 2007	75 years	Per WSA forecasts	$5.1
#3.	3% annually starting 2007	75 years	1.5% annually above WSA forecasts	$11.1
#4.	25% every 20 years starting 2007 plus 3% in all other years	75 years	Per WSA forecasts	$10.1
#5.	50% every 20 years starting 2007 plus 3% in all other years	75 Years	Per WSA forecasts	$18.3
#6.	50% every 20 years starting 2007 plus 3% in all other years	50 years	Per WSA forecasts	$11.1
#7.	3% annually starting 2007	25 years	Per WSA forecasts	($0.1)

While the above table shows substantial potential funding from a toll road lease, there are several factors not included which would greatly diminish the value of any lease. Also, in order to estimate the value of a lease, it is important to compare private lease scenarios to a scenario in which the toll road remained public. These TFIC concerns are discussed in the following sections of this paper.

Critical Factors Affecting Lease Value

There are several major variables which can cause significant changes, both up and down, in the dollar value of a tollway lease. These variables include: future toll increases, length of the lease, establishment of an endowment or stabilization fund to cushion toll increases, required future construction, weighted average cost of capital used in the financial analysis, and non-compete provisions. Each of these variables is discussed in this section.

Additionally, the Credit Suisse report only quantified possible lease proceeds as a single upfront payment. However, rather than a single payment, the payments could be structured to be made through the life of the lease in order to support ongoing transportation improvements. This section also analyzes the "annual payment" option.

Guaranteed toll increases are a required element of any concession agreement if payment is to be made by a private partner to the state.

Toll Increases

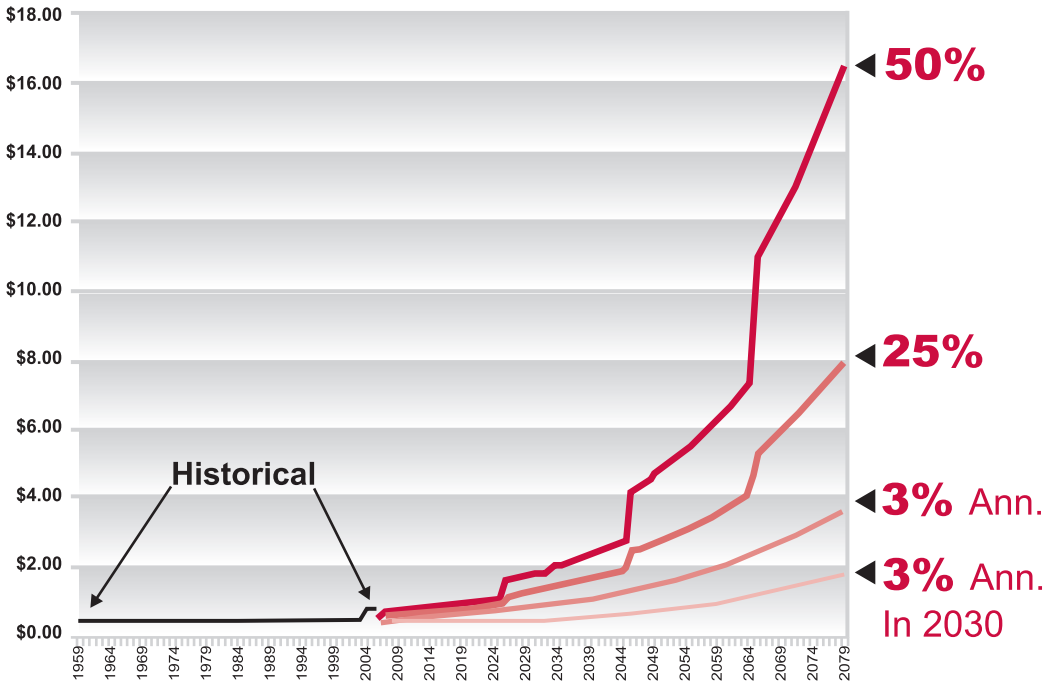
Guaranteed toll increases are a required element of any concession agreement if payment is to be made by a private partner to the state. As noted earlier, Credit Suisse used four different toll regimes to estimate the value of a tollway lease. These four were:

- Scenario #1 - Annual increases of 3%, starting in 2031
- Scenario #2 - Annual increases of 3%, starting in 2007
- Scenario #4 - 25% increase every 20 years, starting in 2007; 3% increase in all other years
- Scenario #5 - 50% increase every 20 years, starting in 2007; 3% increase in all other years

(Scenarios #3 & #7 used the same toll regime as #2, but #3 had more aggressive traffic growth and #7 had a much shorter lease. Scenario #6 used the same toll regime as #5, but with a shorter lease.)

The graph on the next page shows historic toll rates plus the rates under each of the four toll increase regimes. As the graph illustrates, historic rates have been relatively flat, and the toll increase regimes would be a significant departure from past practice. In the case of the most aggressive regime — 50% increase every 20 years plus 3% in other years — the tolls would rise from the current $0.40 for I-Pass users to more than $16.00 by 2079.

Credit Suisse Toll Rate Assumptions



The revenues generated by these guaranteed toll increase scenarios are quite large. The following table, using estimates made by TFIC, shows how substantial these revenues could be in the future.

Estimated Toll Revenues ($ Billion)

Scenario	Status Quo	#1.	#2.	#4.	#5.
Required Toll Increase	None	3% Annual Starting 2031	3% Annual Starting 2007	25% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual
Toll Revenues in 2030	$1.0	$1.0	$1.8	$2.4	$3.2
Toll Revenues in 2050	$1.2	$2.1	$3.9	$6.2	$9.6

To put these revenue numbers in perspective, the state's largest riverboat casino revenue generator is Elgin with revenues of $407 million annually.

Length of Lease

As noted earlier, leases in public/private partnership arrangements can be very long — 99 years for the Chicago Skyway and 75 years for the Indiana Toll Road. When lease terms are shortened, the value of the lease to the private sector, and hence the lease payment to the public sector, go down. This is illustrated in the following table.

Lease Value at 20% Toll Increase Every 20 Yrs. Plus 3% Annual

Lease Term	Est. Net Proceeds After Bond Defeasance ($ Billion)
75 Years*	18.3
50 Years*	11.1
25 Years**	3.6

**Credit Suisse Estimate*
***TFIC Estimate*

Establishment of an Endowment Fund to Cushion Toll Increases

It has been suggested that the guaranteed toll increases could be mitigated for a period of time by taking part of the proceeds and depositing them into a fund to pay the private partner annually for revenues lost due to a toll freeze. Deferring toll increases could make legislative passage of a toll road lease politically easier. However, there are several disadvantages:

- The cost of establishing an endowment/toll stabilization fund reduces proceeds from the concession agreement.
- Fund investments may not achieve targets increasing the state's risk since the private partner must be reimbursed an agreed amount.
- When the toll freeze ended, a large toll increase would be necessary to bring tolls up to guaranteed levels.

The following table shows the fund size necessary for a 10-year toll freeze assuming a 5.2% earnings rate for the endowment fund.

Endowment/Toll Stabilization Fund 10-Year Freeze ($ Billion)

Scenario	#2	#4	#5
Required Toll Increase	3% Annual Starting 2007	25% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual
Required Fund Size	$0.7*	$1.7*	$3.2**
2017 Required Toll Increase	38%*	68%*	102%*

**TFIC Estimate*
***Credit Suisse Estimate*

It should be noted that, in lieu of an endowment fund, the private partner could simply reduce the upfront lease payment to the state, based on deferring any toll increases for a chosen period of time.

Future Construction Requirements

Credit Suisse made the following assumptions on capital spending for improvements to the Tollway to be required by the concession agreement:

- Completion of the Tollway's current $5.3 billion Congestion-Relief Program (CRP)
- Annual maintenance of $175 million through 2011, $200 million through 2020, 3% annual growth thereafter.

The annual maintenance assumptions are reasonable. However, no provision is included in the estimates for needed pavement/bridge reconstruction or for additional lanes and new interchanges in future years after completion of the current CRP. Nor did they assume construction of any new additions to the system such as the most recent IL 355 extension down to I-80.

While this is not an issue for the 25-year lease term analysis, it is a major shortcoming for the 50 and 75-year lease analysis. Credit Suisse noted the need for a CRP-sized program **after 45 years** for lease terms of over 85 years, but CS only analyzed shorter lease terms. Thus, the CS analysis did not include any funding for additional major capital needs beyond those in the current Congestion-Relief Program. The following capital assumptions should be added if the Tollway is to continue to be a vital part of the northeastern Illinois transportation network into the future.

Additional Capital Expenses Needed Over Credit Suisse Report (2006 $ Billion)

	Lease Term: 50 Years	Lease Term: 75 Years
Existing System Capacity Expansion	$1.0; Year 25	$1.0; Year 25
New System Extensions	$1.5; Years 15 & 30	$1.5; Years 15, 30 & 65
O'Hare Western Access	$2.0; Year 10	$2.0; Year 10
CRP Magnitude Program	$0	$5.3; Year 50

Inclusion of these amounts will reduce the proceeds to the state. TFIC does not have the financial models used by Credit Suisse and can only estimate the present value of these additional expenses.

Present Value Additional Construction Expenses ($ Billion)

	Lease Term: 50 Years	Lease Term: 75 Years
Existing System Capacity Expansion	$0.4	$0.4
New System Extensions	$1.5	$1.7
O'Hare Western Access	$1.4	$1.4
CRP Magnitude Program	0	$1.0
Total	$3.3	$4.5

Weighted Average Cost of Capital (WACC)

Under the Discounted Cash Flow method used by Credit Suisse, the estimated proceeds to the state are very sensitive to the interest rate assumptions used for the Weighted Average Cost of Capital (WACC). Because of this, Credit Suisse expressed their findings as a range, using a WACC from 6.0% to 6.9%. The table below shows this range. As the table illustrates, a change of **less than one percent** in the WACC can alter the estimated proceeds by **billions of dollars**. (The information presented in this paper uses the middle of that range – 6.45%.)

Range of Estimated Gross Proceeds WACC from 6.0% to 6.9% ($ Billion)

WACC	Scenario #1	Scenario #2	Scenario #4	Scenario #5
6.0%	$1.9	$8.4	$14.2	$23.9
6.9%	$1.0	$5.8	$10.0	$16.8

Non-Compete Provisions

Credit Suisse believes that a non-compete provision will likely have to be included to achieve the estimated proceeds in their report. Failure to include a non-compete provision would substantially lower the value of the concession. The Skyway agreement does not contain such a provision, but the Indiana Toll Road agreement does. The Indiana agreement defines a competing highway as:

> *"Competing Highway" means any newly-constructed Comparable Highway which is built by or on behalf of the State during the Term and at least twenty (20) continuous miles of which is within ten (10) miles of the Toll Road. In addition, the existing US 20 shall be considered a "Competing Highway" if, on or before the fifty-fifth (55th) anniversary of the Closing Date, it is expanded or improved by or on behalf of the State so that it becomes a Comparable Highway and at least twenty (20) continuous miles of such highway (all of which is Comparable Highway and none of which was Comparable Highway on the Effective Date) is within ten (10) miles of the Toll Road. The existing US 20 shall not be considered a "Competing Highway" notwithstanding any future improvement and/or expansion to make it a Comparable Highway so long as the improvement or expansion which makes it otherwise a Competing Highway is not completed prior to the fifty-fifth (55th) anniversary of the Closing Date.*

A comparable highway is defined as:

> *"Comparable Highway" means a divided four or more lane controlled access interstate quality highway with interchanges, interstate quality bridges or combination or portion thereof.*

Further, the agreement stipulates that the state must reimburse the private partner if a comparable, competing highway is constructed:

(e) ...The opening of a Competing Highway shall constitute a Compensation Event with respect to which Concession Compensation shall be payable on or before March 15 in an amount equal to the actual decrease in net income suffered by the Concessionaire during the preceding calendar year as a sole and direct result of the Competing Highway.

It is unknown what type of non-compete provision might be included in a proposed Illinois Tollway lease. However, the inclusion of a non-compete provision is likely necessary to achieve significant proceeds for the state.

What is known is that there are many locations throughout northeastern Illinois where future improvements on routes near the Tollway will be required over the next 50 to 75 years. Preserving state and local power to make these improvements will be critical to maintaining a good transportation system for the future. A few examples of these needed improvements are:

O'Hare Western Bypass
Elgin-O'Hare completion
Illinois 53 corridor in Lake County
Illinois 59 corridor
Illiana corridor
Metra Star line

Summary of Critical Factors

Following is a table which summarizes the critical factors discussed in this section.

	Scenario #2	Scenario #4	Scenario #5	Scenario #6
Key Variables Included in CS Report				
Required Toll Increase	3% Annual Starting 2007	25% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual
Lease Term	75 Yrs.	75 Yrs.	75 Yrs.	50 Yrs.
Est. Lease Proceeds (after bond defeasance)	$5.1 Billion	$10.1 Billion	$18.3 Billion	$11.1 Billion
Est. Cost of Variables Not In CS Report				
10-Yr. Toll Freeze Endowment	$0.7 Billion	$1.7 Billion	$3.2 Billion	$3.2 Billion
Present Value of Add'l Construction Needed	$4.5 Billion	$4.5 Billion	$4.5 Billion	$3.3 Billion
Est. Net Lease Proceeds	($0.1 Billion)	$3.9 Billion	$10.6 Billion	$4.6 Billion
Other Variables				
0.45% Change in WACC	+/-$1.3 Billion	+/-$2.1 Billion	+/-$3.6 Billion	+/-$1.7 Billion
Acceptable Non-Compete Provision	?	?	?	?

Structure of Lease Payments

The Credit Suisse analysis estimated the lease proceeds as a single upfront payment. However, another option would be to apply the net proceeds to a Transportation Capital Trust Fund which could provide funding annually for transportation programs throughout the term of the lease as opposed to spending all of the proceeds in a short period of time.

Advantages of this approach include:

- The additional funding would not run out until the lease expired, at which time the revenues from the asset would again be available to the state - to return to its role as operator or to lease it again.
- The lease proceeds would not be depleted in a five or ten-year period, leaving decades where tolls were increased but motorists received no transportation benefits.
- Stretching the proceeds over the term of the lease would avoid committing the state to either a substantial tax increase or large transportation capital program reduction when the proceeds were depleted.

Disadvantages include:

- There would be no big short-term program.
- Steady annual payments would be eroded significantly over the years by inflation.

The following table estimates the new transportation funds available annually if all the net proceeds were dedicated to a Transportation Trust Fund for the full life of the lease or for a period of 10 years. The table assumes the trust fund would earn 5.2%.

Potential Lease Payouts Stretched Over Time

	Scenario #2	Scenario #4	Scenario #5	Scenario #6
Required Toll Increase	3% Annual Starting 2007	25% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual
Lease Term	75 Yrs.	75 Yrs.	75 Yrs.	50 Yrs.
Net Proceeds*	($0.1 Billion)	$3.9 Billion	$10.6 Billion	$4.6 Billion
Payout Over Life of Lease Est. Annual Amount	n/a	$0.2 Billion	$0.55 Billion	$0.26 Billion
Payout Over 10 Yrs. Est. Annual Amount	n/a	$0.51 Billion	$1.36 Billion	$0.60 Billion

*Net proceeds after defeasing bonds, funding needed additional construction identified in this section, and setting up 10-year toll freeze endowment fund.

Comparison: Public Option Vs. Privatization

Rather than lease the Tollway to a private partner, the Tollway board could raise tolls in a manner identical to a private partner. The additional toll revenue could be used to support new bonds, with the proceeds of the bonds dedicated to additional transportation improvements.

To analyze such an option, the following assumptions were used:

- Same operating and capital expenditures as those used by Credit Suisse for a private partner
- ISTHA's Congestion-Relief Program (CRP) paid for with current toll revenues
- No toll freeze or additional expansion costs over Credit Suisse assumptions
- Revenue growth used to support new bonds for capital improvements
- 1.3 coverage ratio for new debt service
- 25-year term for new bonds

The following table compares the tollway lease scenarios to a public option. As the table illustrates, the public option yields as much as $97 billion (net present value) for additional capital spending. Thus, if the toll increase regime required for private lease options were implemented by public sector, much more funding would be available for capital improvements.

Keeping the Tollway Public: Additional Tollway Capital Spending 2007-2081

	Scenario #2	Scenario #4	Scenario #5
Toll Increase	3% Annual	25% Every 20 Yrs. Plus 3% Annual	50% Every 20 Yrs. Plus 3% Annual
Private Option: Est. Lease Proceeds (after bond defeasance)	$5.1 Billion	$10.1 Billion	$18.3 Billion
Public Option: New Tollway Bonds (net present value)	$23.4 Billion	$52.3 Billion	$97.2 Billion

It is highly unlikely that the Tollway board would adopt the same aggressive toll increase schedule as a private partner would require. Typically, toll road increases are proposed when needed to fund specific capital improvements and are adopted only after public scrutiny. This contrasts sharply with the private partner toll increase model of annual increases for 50 or 75 years, including sizeable increases every 20 years, with no public scrutiny and with no linkage to toll road improvements.

The Illinois Tollway's most recent toll increase, effective in 2005, was adopted only after public hearings; was relatively modest; and is funding a $5.3 billion major reconstruction and expansion of the system, including the $730 million I-355 extension. Thus, it should be possible to generate the funds for needed transportation improvements, through the public option, with smaller toll increases.

Conclusion

Stretching for 274 miles and serving around 8 billion vehicles miles of travel a year, the Illinois Tollway is an invaluable asset to the state and particularly to the people of northeast Illinois. It is critical that nothing be done to jeopardize this vital component of Illinois' transportation network.

TFIC believes that privatization of the Illinois Tollway would present many public policy challenges, would provide only a limited short-term funding fix, and would not generate as much funding for future capital needs as continued public sector control. Factors that led to this conclusion are:

- Many tough policy issues complicate any private lease option for the toll road, including how to finance future improvements currently cross-subsidized by existing toll revenues, the size of toll increases, the length of the lease, required non-compete provisions, employee rights, and other issues. Decisions on these issues would likely begin to limit the value of the toll road to a private partner, and could also limit the full potential of the toll road to function as an integrated, coordinated component of northeastern Illinois' transit/highway network.
- Based on the toll road study commissioned by Illinois' Commission on Government Forecasting and Accountability (CGFA), a successful toll road lease would require a long lease term (50 to 75 years) and an annual toll increase schedule dramatically different from Illinois' history of infrequent and small increases.
- The CGFA study did not make any provision for funding future major toll road improvements (beyond those underway today), such as reconstruction and additional lanes on the existing system as well as toll road extensions. Providing funding for these improvements would significantly reduce lease proceeds.
- Allowing the existing tollway board to implement fare increases like those required to attract a private partner would actually result in more funding for capital improvements than would a toll road lease. Or, the existing tollway board could provide transportation improvement funds as needed by adopting more modest fare increases than a private lease would require.

While leasing toll roads to a private partner may work in some locations, for the Illinois Tollway it is the wrong option — creating numerous policy challenges, likely to be costly to consumers and likely to be less efficient than keeping the toll road publicly operated.

Transportation for Illinois Coalition Members

The Transportation for Illinois Coalition is a diverse group of statewide and regional business, organized labor, industry, governmental and not-for-profit organizations that has joined together in a united and focused effort to support a strong transportation alliance for Illinois. The coalition takes a comprehensive approach and seeks to speak with one voice for all of Illinois regarding transportation funding needs at both the state and federal levels. The coalition believes that transportation is critical to the economy of Illinois. This comprehensive approach involves all modes of transportation, including rail, air, water, highways and mass transit.

STEERING COMMITTEE

Statewide Organizations

American Concrete Pavement Asso. – IL Chapter, Inc.
American Council of Engineering Cos. of Illinois
Associated General Contractors of Illinois
Illinois AFL-CIO
Illinois Asphalt Pavement Association
Illinois Association of Aggregate Producers
Illinois Association of County Engineers
Illinois Chamber of Commerce
Illinois Municipal League
Illinois Road & Transportation Builders Association
Illinois State Branch of Operating Engineers
Precast/Prestressed Producers of IL & WI
Underground Contractors Association
United Transportation Union

PARTICIPATING MEMBERS

336 Coalition
AAA – Chicago Motor Club
American Society of Civil Engineers - IL Section
Associated Equipment Distributors
DuPage County – Dept. of Economic Dev. & Planning
Greater Peoria Contractors & Suppliers Assn
Growth Association of Southwestern IL
Illinois Concrete Pipe Association
Illinois Construction Industry Committee
Illinois Professional Land Surveyors
Illinois Public Transportation Association
Illinois Society of Professional Engineers
Illinois Valley Contractors Association
Mid-West Truckers Association
Structural Engineers Association of Illinois
Township Officials of Illinois

STEERING COMMITTEE

Local/Regional Organizations

Chamber of Commerce for Decatur & Macon County
Champaign County Chamber of Commerce/
Champaign Alliance
Champaign-Urbana Mass Transit District
Chicago Metropolis 2020
Chicago Southland Economic Development Corp.
Chicago Transit Authority
Chicago & Vicinity District Council of Iron Workers
Corridor 67, Inc.
Egyptian Contractors Association
Elgin Area Chamber of Commerce
Greater Springfield Chamber of Commerce
Heartland Partnership
Kane County
Lake County Division of Transportation
Lake County Transportation Alliance
Metra
MetroLINK
Naperville Area Chamber of Commerce
Quincy Area Chamber of Commerce
Regional Transportation Authority (RTA)
Rockford Winnebago County Better Roads Assn.
Route 51 Coalition
Southern Illinois Construction Adv. Program

SUPPORTING MEMBERS

Builders Assn. of Greater Chicago
Chicago Federation of Labor (AFL-CIO)
Chicago Southland Chamber of Commerce
Chicagoland Chamber of Commerce
Greater Aurora Chamber of Commerce
Highway 34 Coalition
Illinois Automobile Dealers Association
Illinois Highway Users Association
Illinois Petroleum Council
Illinois Public Airports Association
Illinois Quad City Chamber of Commerce
Jacksonville Area Chamber of Commerce
Leadership Council of SW Illinois
Macomb Area Chamber (MACCDDC)
McLean County Chamber
Metropolitan Planning Council
Mid-Central Illinois Regional Council of Carpenters
Northwestern Illinois Contractors Association
Southwestern IL Bldg. & Constr. Trades Council