Transportation for Illinois Coalition
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PUBLIC/PRIVATE PARTNERSHIPS
POLICY ISSUES

Overview

Financing future transportation improvements in Illinois poses ever greater challenges. For that reason, the public/private partnership concept should be carefully reviewed to determine if such arrangements are feasible. The TFIC Issue Paper identifies an initial series of issues that must be addressed by the legislative and executive branches of Illinois State government, as well as by the public at large, as part of this review process.

Legislation has been proposed that would allow the Illinois Department of Transportation (IDOT), the Illinois State Toll Highway Authority (ISTHA), the Regional Transportation Authority (RTA) and its service boards (CTA, Metra and Pace) to enter into public/private partnerships, including partnerships for the construction of new infrastructure projects and for the lease of new and existing infrastructure assets. In the case of Illinois highways, two types of partnerships are frequently mentioned: (1) the leasing of all or part of the existing toll road system; and (2) the construction and leasing of new toll road extensions, such as the OíHare Western Bypass.

Under the first scenario, in exchange for payments from a private partner, ISTHA would enter into a long-term concession or lease arrangement giving the private entity the right to operate a toll road, raise and collect the tolls, and keep any profits from the operation. This is what the city of Chicago did with the Chicago Skyway. Under the second scenario, IDOT and ISTHA would partner with a private entity, which would finance and construct a new toll road. In exchange for this financial commitment, the private partner would enter into a long-term lease giving it the right to operate the road, to raise and collect tolls on it, and to keep the profits from the new road.

While such partnerships have the potential for benefiting the transportation system by providing up-front cash for transportation improvements and/or enabling quicker construction of needed toll road extensions, the partnerships are complex arrangements that have long-term policy implications. TFIC has identified fifteen specific public policy issues that we believe should be considered. Each of these issues is discussed below. It should be noted that the decisions on these issues would impact the amount of money that private partners are willing to invest.

The Transportation for Illinois Coalition is recognized as the authority on and unifying voice for transportation needs in Illinois. Given this leadership role on transportation issues, TFIC is a necessary part of any serious discussion of this issue and stands ready to fully participate in the public discussion of the concerns identified. Until the issues outlined below have been fully and openly addressed in authorizing legislation, TFIC is unable to take a position on public/private partnership legislation in the Illinois General Assembly.

Policy Issues

1. Continued ability to finance new additions to the expressway system in the future.

One of the traditional virtues of Illinoisí tollway system is the ability to use the success of completed segments to help build new segments. Originally the Tri-State had to pay for itself. All extensions after that were 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 and now I-355 in Will County. Carving off a piece of the system for a private partner could make this option much more difficult to use in the future. Leasing the entire system to a private partner would likely eliminate the ability for ìcross-subsidizingî new segments. Potential needed future expressways that could be hindered over the next few years include the Ill 53 extension in Lake County, the Elgin-OíHare/OíHare Bypass and extension of the Prairie Parkway north of I-88. How can this flexibility be preserved with a private partner?

2. Use of revenues generated by public/private partnerships.

Public/private partnerships have the potential to generate significant sums ó $1.8 billion in the case of the Skyway and $3.8 billion in the case of the Indiana Toll Road. In Indiana these moneys are to be used for highway purposes, while in Chicago they are not. Illinoisí toll roads were paid for by the users and it seems appropriate that any funds generated for the public sector through a privatization arrangement should be used for the benefit of the highway users. Should this principle be reflected in the proposed legislation?

A related question deals with whether the public is best served by a onetime payment of benefits or by payments stretched over many years. With a onetime 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 benefit. How can/should funding for future needs be included in public/private arrangements?

3. Requirement for future subsidies from IDOTís highway program rather than using the toll highway system to finance new private partner roads.

There are few if any roads to be built in Illinois that can completely pay for themselves through tolls. A public/private partnership to construct toll road extensions will require a public subsidy. But, ISTHA is prohibited by its bond covenants from providing money to uses other than maintenance, operation and expansion of the ISTHA system. Therefore, IDOT would probably have to provide the subsidy, which in the past had come from toll increases on the existing toll system. This could be a major future drain on state highway programs.

The case study on the Elgin-OíHare/OíHare Bypass, prepared by Business Leaders for Transportation, indicates that private financing could generate $905 million towards construction of this project, and that another $300 million in public subsidy would be required (over and above the $140 million in federal funding authorized last summer). The study assumes that $139 million of the $300 million would come from ISTHA. But, as noted above, ISTHA would be unable to provide any funding because it would not benefit ISTHAís system. The source for the full $300 million in public subsidy would likely be IDOTís state highway program. Using IDOTís current estimate of 10% annual construction cost increases over the next two years, the state highway program subsidy for this project could easily be more than $600 million - assuming that $905 million is possible to be raised by a private partner from facility tolls.

The public policy question here is whether subsidies for future toll road extensions in northeastern Illinois should continue to be financed by system wide toll increases or from the state highway program.

4. Ability to manage the transportation network as a system.

It is difficult enough today 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. How can a private partner be integrated into the system?

A private operator will manage the system to maximize returns to shareholders/investors, not to maximize the public interest. A good example of this is the Skyway repair that is being done at the same time as the Dan Ryan reconstruction. There is no incentive for a private owner to want to schedule work so there is an alternate route available during construction. That would only cause the private owner to lose profits. How can good system traffic management for future construction be included?

5. Potential higher costs to the highway user.

There are several factors that could result in higher costs to the highway user:

- One of the biggest risks for a new toll facility is the potential for delay in starting up and reaching full traffic volume. With no existing revenues to support financing during this time, the investors and bondholders will likely require a risk premium and additional reserves to pay debt service during start-up. This adds costs compared to a financing using bonds secured by a system, which has a long track record.

- Private facilities must generate a return on equity to investors that the Tollway does not, which can increase tolls for the user.

- A private partner will find it difficult to operate a single segment at less cost than a public agency. First of all, it is not as cost efficient to independently maintain one segment of road as it is to add that segment to a much larger system. Additionally, the legislation requires the private operator to abide by many requirements that can increase costs.

In order to protect the public, partnership agreements generally will index future toll increases to an index like the 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 pace the CPI.

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 can that be accomplished within the framework of a public/private partnership?

6. Maintaining current Tollway financial strength.

The OíHare Western Bypass is one of the regionís most needed facilities because it will reduce congestion at the current entrance to OíHare by providing access to a new western entrance and allowing traffic on the Tri-State and Northwest Tollways alternate methods not only to get to OíHare but for through traffic to get around OíHare. If operated by an entity other than ISTHA, the Bypass will divert existing traffic (and revenues) from the ISTHA system, thereby reducing the Tollwayís ability to repair and expand its system both now and in the future. However, it is unclear whether traffic growth on the Tri-State would offset traffic diverted by the Bypass. Also, this revenue diversion could be avoided by the Tollway tolling the entrance/exit ramps to the Bypass, but that would lessen the usefulness of the facility and make it less attractive to the private sector. How can ISTHA be protected from future revenue stream losses?

7. Maintaining flexibility to raise additional transportation resources.

Illinois has a strong record of support for periodic transportation funding increases. (See Attachment for history of funding increases and listing of major projects completed or funded in past 25 years.) However, promises of additional money without raising public 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. Taking the pressure off of officials to increase funding to implement a ìheadlinerî project makes it more difficult to put a package together that meets all of the stateís transportation needs such as rural widening/resurfacing and bridges, public transportation, and interstate reconstruction. To pass initiatives in the General Assembly, all parts of the state must benefit from the program. Cherry picking key projects by the private sector could hurt IDOT and ISTHA in future efforts to raise user fees to make improvements system wide and to keep the existing system in good condition.

How can private partnerships be structured to enhance future public initiatives or to be part of an overall transportation funding strategy?

8. Potential inconsistency between privately controlled design-build and the public interest.

Use of design-build on urban expressways could have potential negative impacts on urban neighborhoods. Ability to implement context sensitive designs may clash with maximizing profit to private partners. The private sectorís goal will be to make the facility as attractive as possible to the motorist at the lowest possible cost to the private investor. There is no incentive for the private sector to protect adjacent residents and businesses or mitigate their concerns. How can the public be assured that its concerns will be considered and mitigated in the design process?

9. Consideration of <u>public</u> financing options which could offer the ability for additional improvements while protecting the public interest.

Currently the Tollway enjoys a fairly high bond rating which reflects a high ratio of revenues to debt. Private owners are willing to accept much lower debt ratings to maximize the amount of construction. If ISTHA were willing to accept a lower bond rating, it could significantly increase its construction at current toll levels. Higher debt levels and leverage (and lower bond ratings) can be consistent with good management, optimal operation and accomplishing important public projects. How do these public options compare to private options?

10. Flexibility to modify or terminate agreement.

Privatization concepts look at very long lease times (75 to 99 years). 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, the partnership agreement would likely 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 tolls increases were perceived as ìtoo high,î 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 Torontoís case, the matter has been 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.

How can the legislation minimize this risk and address the need for flexibility to respond to changing political considerations?

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 - let alone 70 or 80 years away. How can the flexibility be maintained to address unforeseen future transportation needs?

11. The right of the public to know what is being placed in contracts with private partners.

While public agencies are supposed to be transparent, private businesses strive to be opaque to protect proprietary information and maintain competitive advantages. The public/private partnership legislation under consideration in Missouri requires contract details to be a ìclosed recordî until after the agreement between the state and private operator is executed. Illinois has a history of public involvement in transportation planning and funding. How can the legislation provide the proper mix of sunshine to protect the public and secrecy to protect the private partnerís proprietary and competitive interests?

12. Impact of non-compete provisions.

Inclusion of ìnon-competeî provisions will increase the amount a private partner will be willing to pay for a long-term lease since their 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 the private partner, a non-compete provision could prohibit state, local and transit agencies from making future improvements in or near the corridor. Should the legislation restrict the use of such provisions?

13. Conversion of free roads to toll roads.

The current proposed legislation permits turning existing freeways into toll roads. Should this power be granted?

14. 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. Should there be some oversight or approval process required for public/private partnership commitments? How much administrative discretion should be granted?

15. Compliance with state statutes regarding labor provisions, environmental impacts, work force diversity, and competitive bidding procedures

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 range from ensuring minority participation in public works projects to provisions that ensure community participation in the design of a transportation facility. Some of the statutory and regulatory requirements include the following:

- Disadvantaged Business Enterprise Law
- Prevailing wage law
- State procurement code requirements, including competitive bidding for construction
- Qualification-based Selection Act for hiring engineering and design firms
- Context sensitive design requirements

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

Attachment: Transportation Funding Increases

Governor Thompson raised the gas tax and license fees in 1983, initiated the Build Illinois Program in 1985, raised tolls to construct the North-South Tollway in DuPage in the mid-eighties, and raised the gas tax again in 1989. Governor Ryan raised license fees in 1999 to fund the Illinois First Program, increasing resources for state and local roads by more than $4 billion. Governor Blagojevich raised tolls in 2005 to fund the $5 billion Open Road Tolling program and numerous expansions to the Tollway including the North-South extension in Will County. Only during the eight Edgar years were there no increases in state funding for transportation and this was due to Illinois receiving the largest increase in the nation (50%+ increase) in federal highway funds with ISTEA in 1992. A major infusion of public infrastructure funding has occurred every four or five years for the past 25 years.

Many new expressways or expressway expansions have been either completed in the last 25 years, are now under construction, or are funded in current multi-year programs with traditional public financing. Here are 20 examples:

Elgin OíHare expressway west of I-290 ***(Completed)***
North-South Tollway in DuPage County ***(Completed)***
I-355 from I-55 to I-80 ***(Under construction)***
Tri-State add lanes to the entire length ***(Portions under construction, completed and funded)***
Northwest Tollway add lanes from the Kennedy to west of Elgin ***(Funded)***
Add lanes to Reagan Tollway from I-290 to Ill 59 ***(Portions completed, under construction and funded)***
I-290/Ill 53 add lanes in Western Cook County ***(Completed)***
I-39 from Rockford to Bloomington ***(Completed)***
I-80 add lanes from the Tri-State to Indiana ***(Under construction)***
I-155 from Lincoln to Peoria ***(Completed)***
I-72 from Springfield to Quincy ***(Completed)***
Ill 29 from Springfield to Taylorville ***(Portions completed and under construction)***
US 51 south of Decatur ***(Portions completed and under construction)***
US 67 in Morgan County ***(Portions completed and under construction)***
I-270 in St. Clair County ***(Completed)***
Alton Bypass ***(Under construction)***
Ill 13 in Saline County ***(Completed)***
US 45 in Saline County ***(Under construction)***
US 34 in Henderson County ***(Portions completed and funded)***
Ill 336 from Quincy to Macomb ***(Portions completed and under construction)***