

ACEC CONFERENCE ON THE BUILT ENVIRONMENT

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As Part of a Panel on Public-Private Partnerships

In Texas, our experiments with “public-private partnerships” in transportation began in 2003, when the Legislature passed a major transportation package that authorized comprehensive development agreements (CDAs).

Like the term “public-private partnerships,” the term CDA is so broad as to be almost meaningless. It is used to describe a variety of project approaches, from simple design-build to design-build-operate-maintain-finance-transfer and long-term concessions.

My remarks will focus on concessions and, within that, on concessions for new projects rather than asset sales such as the Chicago Skyway deal.

A number of potential concessions are in play in Texas. These mostly fall in three categories: (1) new greenfield intercity connectors such as the Trans Texas Corridor projects; (2) new greenfield projects within metropolitan areas; or (3) capacity expansions within metropolitan areas.

The engineering community in Texas is participating in these projects, but generally with more skepticism than enthusiasm. On the planning side, the general attitude is that these projects probably will never get built, but if the DOT is going to spend \$200 million studying them, I’m going to get in line. For those participating on the developer side, it is fair to say that the transactional costs have been very high. The legislation authorizing CDAs is highly discretionary and essentially allows the DOT to make whatever rules it wants, within very broad parameters.

The result has been a complicated, costly process characterized by the end result being a constantly moving target, abuses of intellectual property, and not just risk-sharing but risk avoidance on the part of the owner. There is some hope that this process will improve over time, but it is not clear that it will.

In general, it is probably fair to say that the contractors share this view of the process as well.

In addition, most of the firms that have been working with concessionaires have concluded that ultimately they have a “flea market” approach to engineering. As a business model, this does not appear to be one that highly values engineering judgment.

However, I’m sure it will not surprise you to know that the success or failure of concessions in the public policy arena will not be determined by how they affect engineers. Instead, we have to talk about whether concessions are good transportation policy.

At the start of this discussion it is important to distinguish between arguments over concessions and arguments about tolling. Both of these debates are going on in Texas, and while we may be skeptical of concessions, like all organizations interested in transportation we know that we have to expand the number of toll projects – and we support that. The real debate is not about whether to expand tolling but about the merits and demerits of pursuing needed toll projects through concessions as opposed to using public toll authorities.

First, it should make you nervous that there is an extremely high correlation between concession proponents and no-new-tax proponents. Too many people are talking about concessions in order to avoid talking about the motor fuel tax. Many have structured a hyperbolic argument that the motor fuel tax no longer works as a transportation finance mechanism, as if we will all be driving hydrogen cars by 2010.

The visionary transportation, including some in Texas, are talking about how to implement mileage-based fees and how think about transportation as a utility, but clearly these changes are a long way off. So while the motor fuel tax and other user fees certainly have their economic inefficiencies, we will be using the gasoline-powered internal combustion engine for transportation in this country for many, many years. We do not need to let people get away with talking about concessions as if they could supplant public investment.

Too often, the proponents of concessions imply, without really saying it, that concession investments and upfront concession fees represent new money for transportation – money that is almost free money.

But in reality the only new money in these projects is toll revenue paid by the users, which is generated whether the project is built by a concessionaire or a public toll authority. A concession fee is nothing more than the net present value of some future positive cash flow that has been created by extending the term of a deal from the 25-30 years customary in a public transaction to 50-100 years common in concessions. It is, in effect, the financial engineering of the revenue stream. More to the point, it is a new way of borrowing.

To give credit where credit is due, there is something new and different here. Whereas for several decades in this country we have been developing ways to borrow from our children in order to support our lifestyle (think Social Security and permanent national deficits), in 100-year concessions we have now discovered a way to borrow from our grandchildren.

One of the things about this new way of borrowing that is often ignored in the public debate is that it is replete with a whole set of trade-offs, mostly relating to a loss of public control over transportation planning and decision-making. Let me touch on a few.

The first major trade-off is covenants not to compete. A concessionaire is going to be looking at protection for his concession and his investment – i.e, protection against the free alternative that moves traffic away from his concession. While this is understandable, these agreements clearly involve a public body surrendering – or at least compromising – its long-term ability to respond to changing transportation realities.

A second trade-off is the loss of system benefits – or a limit on the ability to run a regional toll system as a system, using the positive net income of one aspect of the system to expand the system or serve other transportation needs. In the Houston/Harris County area, in Dallas-Fort Worth, and in San Antonio, high-revenue projects are being cherry-picked for concessions even when they are within the geographic area of a successful regional toll agency.

In Texas, these agencies are very successful, with a project delivery record that surpasses that of the DOT. Since they are local and regionally controlled agencies developing local and regionally controlled projects, they also can more effectively counter anti-toll crusaders. Yet we are undercutting these regional agencies in what amounts to a power struggle and undermining their ability to develop regional systems.

Finally, another trade-off is the loss of control over toll rates. One of the arguments for concessions is that a private operator can operate them with higher economic efficiency – that is, extract higher tolls since they are not subject to political pressures. That's certainly not all bad, but it naïve not to realize that control of toll rates is a legitimate issue for local and regional political leaders.

In the August 21 issue of Engineering News Record, one transportation planner stated that this is all “a balancing act like no other.” The author noted that “the contract must allow the developer to make fair rates of return yet contain provisions that control toll structure and maintain policy flexibility for the public owner.” And the typical answer of DOTs is that we can look out over 100 years and accomplish this. “We have anticipated this issue.” “We can answer that.” “That will be dealt with in the contract.”

Unfortunately, WE ARE NOT THAT SMART. Think of it in these terms: Making deals 75 years in the future is equivalent to us living in 2006 under an agreement that the DOT negotiated in 1935! Is it possible that a transportation planner in 1935 could have anticipated all the changes that would occur in a transportation corridor and essentially ceded control over it while preserving what is best for the public? Unlikely. And is there any reason to expect that the pace of change will slow down between 2006 and the end of the century from what it has been over the past 75 years? Not a chance.

In the end, the concession approach has less to do with transportation than with what Warren Buffett (critically and disparagingly) called the “financialization of the American economy” – we don't make things anymore, we finance them.

In our view, we need to think long and hard about the trade-offs involved in concessions.