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US policy on PPPs: jury still out

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Despite the widespread conviction that transport infrastructure in America is badly in need of repair and expansion and the acknowledged inadequacy of available public funding, private investment in heretofore publicly funded transport facilities remains politically controversial. The pace of further activity may well be constrained by an unfriendly statutory framework and an abiding scepticism among many politicians about whether PPPs are beneficial in the long term. Given the important federal and state legislation that will be enacted over the next few years, stakeholders must provide legislators with a more accurate understanding of the ways in which PPPs are not only consistent with, but can enhance, the public interest.

Highways

The US Highway Trust Fund (HTF), heavily dependent on an 18.4-cents-per-gallon tax on gasoline, is currently the source of nearly half of all US investment in highways and transit and is intended to generate approximately US$40bn a year in matching funds for the benefit of the 50 state governments that do the actual contracting. It would have shown a deficit for the first time in history in 2008 but for an emergency infusion of US$8bn from general tax receipts in mid-September.[1]

The HTF's revenue shortfall is attributable in part to developments that would be celebrated as good news in any country that did not link the quality of its transport infrastructure to a tax on fossil fuel: (i) increasingly efficient autos and trucks on American roads and (ii) an unprecedented reduction in vehicle miles travelled. The first factor is the product of national laws and regulations compelling manufacturers to produce more fuel-efficient vehicles; the second is attributable to the recent doubling in the price of fuel – now as volatile in its economics as in its chemistry – and a predictably depressed demand curve.[2]

Facing a first-ever shortfall in Highway Trust Fund revenues and persuaded that congestion can be addressed successfully only if road use is priced more effectively, the US Department of Transportation (DOT) has launched a major campaign to encourage the increased use of tolls and other user fees throughout the system. Understanding that economic pricing also creates opportunities for private investors and thus has the potential to unlock hundreds of billions of dollars in private investment capital, DOT also has become a staunch supporter of PPPs.

In these circumstances, the way would appear to be clear for a significant acceleration in US-based PPP activity. Indeed, federal surface transportation legislation over the past decade and a half has included programmes apparently designed to encourage innovative approaches to the financing, construction, and management of highway facilities. DOT and its Federal Highway Administration have developed additional programmes through administrative means to focus communities on new and more effective ways of delivering improvements and addressing congestion.[3] All of this is encouraging, and it has led many commentators to assume that transport-related PPPs in the US will henceforth enjoy steady, certain growth. It is a premature conclusion.

The opportunities actually available are seriously constrained by restrictions built into the programmes themselves, by severely limited funding, and by an abiding scepticism among many politicians at all levels of government – federal, state, and local – regarding whether PPPs are consistent with the public interest. When viewed through the prism of America's current needs, these programmes look more like a tentative toe in the water than the game-changing policy transformation that is so urgently needed.

In US highway legislation, the fundamental statutory rule for decades has been that any highway facility that has been built with federal financial assistance "shall be free from tolls of all kinds."[4] Fortunately, another provision now exempts from this prohibition all highways, bridges, and tunnels other than those on the 'Interstate' system of major highways – thus allowing widespread federal participation in the construction of tolled facilities and the conversion of free facilities to tolling. Moreover, the provision expressly contemplates placing such facilities under private management through PPPs.[5]

If a state plans to convert to a toll facility a previously free highway originally constructed with Federal-aid funds, however, it must commit that all toll revenues will be first used for debt service, a 'reasonable return' on private investment, and operation and maintenance. Importantly, any toll revenues received in excess of those needed for these enumerated purposes may be diverted away from the facility only if they are used on other highway-related activities.[6]

The tolling of existing free Interstate segments is also permitted now, but only pursuant to a number of strictly limited pilot programmes. The Interstate Reconstruction and Rehabilitation Pilot Programme, created a decade ago,[7] permits up to three pilot projects; only one opportunity remains available. Another is the Value Pricing Pilot Programme, originally authorised in 1991.[8] Only one opening remains available of the 15 originally contemplated. The Interstate System Construction Toll Pilot Programme, established in 2005,[9] provided three opportunities, of which two remain available. And finally, the tolling of heretofore free Interstate segments is also permitted under the Express Lanes Demonstration Programme.[10] Some 15 projects are authorised and most remain available.[11]

Airports

Airport privatisation, widely practiced the world over, is extremely difficult in the US. The only avenue is an Airport Privatisation Pilot Programme enacted in 1996.[12] The programme allows the privatisation of up to five airports, one of which must be a general aviation airport and not more than one of which may be a large hub airport.[13] The list of statutory requirements that must be met in order to obtain approval has proven daunting, not the least of which is a requirement that at least 65% of the airport's air carriers (by number of carriers and by landed weight) must approve the airport sponsor's use of sale or lease revenue for non-airport purposes. Also, unless approved by 65% of air carriers at the airport, the private operator may not increase air carrier rates and charges at a rate that exceeds the consumer price index.

Not surprisingly, only one airport has been privatised under the programme thus far – Stewart Airport in Newburgh, NY – and that airport has since been returned to public ownership. A number of other applications have been submitted but were subsequently withdrawn or terminated. At this writing, the most important pilot privatisation thus far – at Chicago's Midway Airport, the first large hub to seek approval – is at the bidding stage. Investors will be watching carefully for lessons learned. If Midway is successfully privatised, however, it will not be possible to apply those lessons to any other large US hub privatisation without an act of Congress expanding the programme.

To be sure, pilot programmes are a time-honoured means by which legislators test new ideas, and perhaps it is reasonable to hope that we will see a mainstreaming of these first modest experiments in forthcoming legislation. Recent experience, however, furnishes little cause for optimism.

First, it has not been easy to focus Congressional attention on the critical challenges the US is experiencing in transportation. The current surface transportation enabling legislation, SAFETEA-LU,[14] was passed two years after the due date, requiring a dozen extensions of the predecessor act. New legislation enabling the federal government's aviation programmes is already one year late and will likely remain undone for many more months, if not years. SAFETEA-LU will expire on September 30, 2009, by which time the new President and new Congress will have been in office for a mere eight months. It is difficult to imagine how, with so many competing priorities, it will be possible by the end of September to draft, discuss, and enact the kind of surface transport legislation that America needs right now. Further extensions therefore seem highly likely.

Support of Congress?

Timing aside, a more important question is whether there will be sufficient support in Congress and state legislatures for the policy transformation that is required if the US transport system is to drive national economic growth and not impede it. PPPs need to emerge from the pilot programme laboratory as a core element in America's transport investment strategy.

Thus far, signals coming from the leadership of the most important Congressional committees have reflected serious reservations about the long-term implications of PPPs. Fewer than half the states have enabling legislation allowing them to enter into public-private transactions.[15] Texas last year – despite its much heralded, multi-modal Trans-Texas Corridor – enacted a two-year moratorium on new PPP activity. The New York State Legislature refused to support New York City Mayor Michael Bloomberg's proposal to establish a cordon pricing programme to reduce traffic gridlock in Manhattan. Other examples abound.

Congress and state legislatures cannot be expected to take up these questions in a fresh and creative way without a major educational effort by knowledgeable stakeholders. Legislators need to be convinced that the public's long-term interest in cost-effective system performance will not be compromised by the private sector's supposed focus on near-term returns. The myriad ways in which properly structured PPPs are not only consistent with the public interest, but actually enhance it, need to be described clearly.

Public policy has never been the exclusive province of the public sector. The investment banking community has an important responsibility to explain these approaches more cogently, more frequently, and in terms that are comprehensible to the public at large.

Notes:

[1] The Department of Transportation has been warning of the likely deficit since February 2006.

[2] Escalating construction costs and accelerated spending have put further pressure on HTF balances.

[3] DOT and the Federal Highway Administration have assembled a highly useful collection of materials on PPPs and posted them online. See, for example, www.fhwa.dot.gov/ppp, and ops.fhwa.dot.gov/tolling_pricing.

[4] 23 U.S.C §301.

[5] This and other programmes to encourage tolling have been discussed previously in these pages. See, e.g., R. J. Gibbons and M. P. McGuigan, "US PPPs: The Trend Continues," Transportation Finance Review 2006/07, p. 30.

[6] 23 U.S.C. §129(a)(3).

[7] Transportation Equity Act for the 21st Century (TEA-21), Pub. L. 105-178; 112 Stat. 107 (1997), §1216(b).

[8] Intermodal Surface Transportation Efficiency Act (ISTEA), Pub. L. 102-240; 105 Stat. 1914 (1991), § 1012(b), as amended by TEA-21 (1997), §1216(a) and the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU), Pub. L. 109-59; 119 Stat. 1144 (2005), § 1604(a).

[9] SAFETEA-LU, fn. 6, §1604(c).

[10] SAFETEA-LU, fn. 6, §1604(b).

[11] Applications must be submitted by May 31, 2009.

[12] Federal Aviation Authorisation Act of 1996, §149, Pub. L. No: 104-264, 110 Stat. 3212 (1996); codified in 49 U.S.C. § 47134.

[13] A "large hub airport" is defined as one that accommodates more than 1% of total passenger boardings. 49 U.S.C. § 47102(10).

[14] See fn. 8.

[15] The Federal Highway Administration website (www.fhwa.dot.gov/ppp/legislation.htm) reports that 23 states have enacted legislation authorising participation in public-private partnerships.

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