

Before the

**Subcommittee on Energy, Natural Resources,
and Infrastructure**

Committee on Finance

United States Senate

**Hearing on Tax and Financing Aspects of Highway
Public-Private Partnerships**

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Driving Trucking's Success

**950 North Glebe Road
Suite 210
Arlington, VA 22203**

Chairman Bingaman, Senator Bunning, and members of the Subcommittee, thank you very much for giving the American Trucking Associations¹ the opportunity to submit comments for the hearing record.

Mr. Chairman, you are to be commended for calling this hearing and for focusing attention on the federal taxation implications of highway public-private partnerships (PPPs). PPPs, and the lease of existing facilities to the private sector in particular, are relatively new financing tools in the United States. In order to judge them against other funding and financing options, it is important to gain a fuller understanding of these instruments. While federal tax law is a critical component of PPPs, there is a lack of knowledge among both public officials and the general public about how the tax code affects both the decision to enter into a PPP and how it influences the terms of an agreement between the public and private parties. It is appropriate, therefore, to shine a light on these issues in order to determine what impact, if any, the federal tax code has on public policy and project financing decisions.

We strongly believe that while private financing of highway infrastructure may play a limited role in addressing future transportation needs, certain practices may generate unintended consequences whose costs will vastly exceed their short-term economic benefits. In particular, we are very concerned about attempts by some states to carve up the most important segments of the highway system for long-term lease to the highest bidder. We believe that leasing existing highways to private interests is inconsistent with the efficient and cost-effective movement of freight, is not in the public's best interest, and represents a vision for the Nation's transportation system that is short-sighted and ill-conceived. We therefore oppose these schemes.

While privatization discussions tend to center on financing concepts and the great public benefits from concession fee revenue, what often gets lost or ignored is the impact of these deals on the users of the toll facilities and on the general public. Chief among the concerns is the impact of toll road privatization on toll rates. Demand elasticity, the art and science of determining how high rates can increase before a significant number of users will abandon the toll road, is the private operator's chief method for deciding appropriate toll rates. Private toll road operators need not be concerned about the social impacts of toll rates on low-income workers, or on the costs to businesses that depend on the highway for transporting employees, customers, goods or services. Nor do private operators care about the extent of traffic diversion to lower quality, less safe, roads. Their main concern is to maximize the toll road's profitability within the confines of the lease agreement and the law.

Supporters of privatization point out that toll rates are unlikely to increase substantially because customers will choose to simply migrate to toll-free roads. In some cases, this may be true – a reasonable toll-free alternative may be available. On most major toll roads, however the only alternative may be a two-lane road with traffic lights and a significant amount of local traffic or, in the case of a toll bridge or tunnel, no alternative at all. Complicating the situation is a standard practice of including non-compete clauses in lease agreements, which prohibit or severely restrict improvements to competing roads.

¹ The American Trucking Associations is the largest national trade association for the trucking industry. Through a federation of other trucking groups, the industry-related conferences and its 50 affiliated state trucking associations, ATA represents more than 37,000 members covering every type of motor carrier in the United States.

Privatization boosters also point to caps on toll rate increases that have been a standard part of privatization agreements. However, two major lease agreements that have been completed in the United States – the Indiana Toll Road and Chicago Skyway – have been accompanied by very large initial rate increases combined with caps on future increases that by some estimates could exceed six percent annually. Close examination of these deals reveals the extent of the problem and should serve as warnings about future privatization efforts

Indiana Toll Road

In 2006, the State of Indiana agreed to lease the Indiana Toll Road to the Macquarie-Cintra private sector consortium. In exchange for a \$3.85 billion concession fee, the firms can collect the toll revenue and agree to operate, maintain and improve the highway. Under the agreement, toll rates for a 5-axle truck increase incrementally from \$14.55 to \$32.00 in 2010 (all figures assume the truck traverses the entire length of the highway). On June 30, 2010 the lessee can increase toll rates by 8.2 percent, the rate of inflation (CPI) or the annual rate of change in national GDP per capita, compounded over the previous 4 years. Since 1960, the annual average rate of change in GDP/capita was 6.2 percent. From 2004 to 2005, the increase was 5.4 percent. Assuming a 5.5 percent annual average increase, the toll rate for a 5-axle truck may therefore rise by up to 23.9 percent, or to a rate of \$39.64 in 2010. Therefore, toll rates for a 5-axle truck may increase by about 172 percent over five years if the lessees decide to maximize toll rate increases.

Less than two years after financial close, toll rates for a 5-axle truck have increased by more than 87%, from \$14.55 to \$27.25. Toll rates on cars paying cash went up by 72%. However, the State of Indiana has been paying Macquarie-Cintra to delay toll rate increases on passenger vehicles with electronic toll tags. Therefore, the financial impact on taxpayers has been understated. The impact of Turnpike privatization on users of the highway has been significant. Over a 2-year period between September 2005 (prior to privatization) and September 2007 (14 months after privatization) revenue increased by more than 62% despite a four percent reduction in traffic.²

Toll rate increases of these magnitudes will inevitably result in diversion of traffic. The experience from toll rate increases on the Ohio Turnpike during the 1990s is instructive. When the Ohio Turnpike increased its truck toll rate to 17.6 cents/mile for 5-axle trucks, the result was massive diversion to alternate routes. The Ohio Department of Transportation found that a decade after the increase, growth in truck traffic on the turnpike was static, while truck traffic on parallel roads tripled. ODOT determined that these parallel routes had much higher accident rates. For example, U.S. 20, which saw a 267 percent increase in truck traffic, had a fatal accident rate that was 17 times higher than the Turnpike's rate. By 2010, the truck toll rate on the Indiana Toll Road is likely to be approximately 25 cents per mile, 42 percent higher than the Ohio Turnpike's toll rate at its peak. The two highways are essentially the same route, and have similar alternatives. Therefore, it is reasonable to expect a level of diversion on the Indiana Toll Road that is at least as great as was experienced in Ohio.

² Macquarie Infrastructure Group. Press Releases October 8, 2006; October 8, 2007.

There is a significant difference between the states that allows one to address these challenges effectively and forces the other to suffer the consequences. Because the Ohio Turnpike Commission is a public authority, the Governor and Secretary of Transportation were able to make changes – including lowering truck toll rates and increasing speed limits – which attracted a substantial amount of truck traffic back to the turnpike. Since control of the Indiana Toll Road has shifted from public to private hands, addressing these types of issues will not be quite as easy, and the lessees will base all changes in their operations on the potential impacts on their profitability, and not on the impacts on the public welfare.

As bad as the situation may be under the 2010 toll rates, it may even get worse. Beginning on June 30, 2011, the lessees may use the same criteria identified for annual toll increases. Assuming an average annual 5.5 percent increase in GDP/capita, the maximum potential toll rates for a 5-axle truck are:

- 5 years: \$51.81
- 10 years: \$67.71
- 20 years: \$115.56

This rate of increase will produce a toll rate that by 2016 will be equivalent to a fuel tax of approximately \$2.00 per gallon, and by 2031 will equal \$4.42 per gallon.

It has been suggested that these massive toll rate escalations are unrealistic because, as has been demonstrated on other facilities, including the Ohio Turnpike, raising the toll rate too high forces significant traffic off the highway. However, the lessee will set a toll rate to a level that maximizes profitability, not traffic. In fact, when the Ohio Turnpike lowered its toll rates, the highway experienced an income loss, despite significant traffic increases. Private sector operators have little or no interest in and no responsibility for what happens off the toll road. In fact, if Indiana wants to upgrade alternative routes to Interstate Highway quality standards to address traffic problems caused by diverted toll road traffic, the state will have to compensate the toll road operators for loss of revenue. This creates a perfect scenario for the lessee: a portion of the revenue lost due to diversion of traffic as a result of high tolls will simply come back as compensation from the state, and the lessee profits additionally by avoiding maintenance and expansion costs that it would otherwise have borne had that traffic not diverted. The combination of construction costs and compensation to the lessee could, over the course of a 75 year lease, easily exceed the state's concession fee plus earned interest.

Finally, the projected toll rates far exceed what is necessary to raise sufficient money for the operation, maintenance and improvement of the Indiana Toll Road. This means that toll road users will be forced to subsidize other state functions and enrich toll road investors, with little benefit to themselves.

Chicago Skyway

Effective 2005, the City of Chicago agreed to a concession agreement in which Macquarie-Cintra would take control of the Chicago Skyway for 99 years in exchange for \$1.8 billion. Concession revenue is to be used primarily to pay off City debt.

Macquarie-Cintra used similar toll escalation caps for both the Indiana Toll Road and Skyway deals. However, the availability of free alternatives may hold rates down. On the other hand, because the Chicago area is already very congested, an acceptable loss of traffic to the owners of the Skyway due to toll rate increases may have a negative impact on the mobility of the alternative routes. Again, however, profit, not regional mobility or the larger public interest, is the lessee's main concern. Therefore, by giving up control of this asset, the city has also given up the ability to incorporate it into a broader transportation strategy.

Toll rates will increase by 150 percent over the first 12 years of the lease and then are capped at about 6 percent per year (based on historical GDP/capita). Most Skyway users are Indiana residents, so there is little political impact from these increases and little recourse for users of the toll road other than to vote with their wallets and use an alternative route if possible. The toll increases are essentially a commuter tax, with the lessees and the city, not the payers of the tax, enjoying the benefits of the revenue.

Beyond the concerns over toll rates, there are also questions about whether private toll road operators will act in the public's best interest. It is impossible to predict changing circumstances over the life of a lease, which tend to be long-term – up to 99 years in duration. Many of the facilities under consideration for private takeover are among the most critical links in our freight and military logistics chains. They are also important commuter and tourist arteries. Will the private operators act in the public interest, even if it cuts into their bottom line? Given that their responsibility is to their shareholders, this is unlikely. When other corporations act in a manner that is not perceived to be in the public's best interest, the free market tends to correct their behavior. In a situation where the corporation essentially has a monopoly, these market forces do not exist. When the free market fails, government must often step in to protect the public. ATA believes that when it comes to the long-term lease of critical highway infrastructure, it is necessary and appropriate for the federal government to take action to protect the public interest and to establish interstate commerce protections, as required of the federal government by the Constitution.

We also believe that if too much reliance is placed on the private sector for financing highways, the criteria for project selection will shift from larger public benefits such as congestion mitigation, safety and reduction of emissions, to an evaluation of the project's ability to pay for itself and to subsidize unrelated government functions.

Among the most problematic features of these lease agreements is the long-term nature of the contracts. The Indiana and Chicago contracts will keep these highways in private sector hands for 75 and 99 years, respectively. The length of these deals is due in large measure to the federal depreciation benefits received by the private party, which can be substantial. It is common among supporters of PPPs to suggest that the federal government should “just get out of the way” when it comes to these transactions, particularly when a federal-aid highway is not involved. However, this implies no federal interest or liability. Certainly, the large federal subsidies that are involved in depreciation of the assets give the federal government adequate reason to be a party to the negotiations. Indeed, by giving the private party tax ownership of the facility, and thus the right to claim a federal depreciation benefit – as was the case in the Indiana

and Chicago transactions – the public partner has intentionally brought the federal government into the transaction. Furthermore, these lease agreements may have significant implications for interstate commerce and national defense if they involve major freight routes or carry military traffic. It is therefore necessary and appropriate for the federal government to assert itself into these negotiations, either through changes in law that have implications for multiple transactions, or on a case-by-case basis.

ATA believes that the Finance Committee should, at a minimum, address the impact of federal tax law on the length of leases and take steps to ensure that the tax code does not dictate term lengths through depreciation benefits. Such long leases affect highway agencies' ability to make long-term planning decisions. They also burden generations of motorists with high toll rates from which they may never benefit. This was especially evident in the Chicago Skyway lease. The concession revenue was used primarily to pay off city debt. By any measure, saddling citizens with a 99-year financial liability in return for one-time debt-relief is a questionable policy and financial decision.

Mr. Chairman, ATA looks forward to working with you and other members of the Finance Committee to ensure that federal tax policy as it relates to highway PPPs do not unintentionally produce poor public policy. Thank you for the opportunity to submit comments.