GAO Questions Wisdom of Public Private Partnerships

Government Accountability Office testimony warns of need to better assess the true cost of privately operated toll roads.

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The Government Accountability Office last week questioned the wisdom of using public-private partnerships to build and maintain toll roads. GAO's Director of Physical Infrastructure issues, Jay Etta Z. Hecker, summarized the congressional watchdog agency's work in testimony before a US Senate Finance subcommittee hearing on Thursday that focused on the cost to the public of privately operated toll road leasing arrangements.

Broadly speaking, these arrangements allow private companies to lease existing roads in return for the ability to collect toll revenue for a fixed term that can last up to 99 years. In some cases, these companies will offer local politicians billions of dollars in up-front cash payments for leasing rights. The private company would then be responsible for maintaining the road. In other cases, the private company would build and own entirely new roads, delivering significant new highway capacity to the public in return for significant profit potential.

While acknowledging potential public benefits of private participation in these deals, Hecker said that GAO's extensive study of this funding approach identified a number of fundamental problems.

"There is no 'free' money in public-private partnerships," GAO's report stated. "They are potentially more costly to the public and it is likely that tolls on a privately operated highway will increase to a greater extent than they would on a publicly operated toll road. There is also the risk of tolls being set that exceed the costs of the facility, including a reasonable rate of return, should a private concessionaire gain market power because of the lack of viable travel alternatives."

In 2006, two key highways in Illinois and Indiana were handed to Cintra-Macquarie, a consortium of Spanish and Australian toll road operators. The Chicago Skyway was leased for 99 years in return for a $1.8 billion payment and the Indiana Toll Road for 75 years for $3.8 billion. State officials found the ability to spend these windfalls on current needs, but GAO questioned whether future generations may regret this decision.

"Using a highway public-private partnership to extract value from an existing facility also raises issues about the use of those proceeds and whether future users might potentially pay higher tolls to support current benefits," the report stated. "In some instances, up-front payments have been used for immediate needs, and it remains to be seen whether these uses provide long-term benefits to future generations who will potentially be paying progressively higher toll rates to the private sector throughout the length of a concession agreement."

GAO found that a significant portion of the up-front payment derives from the tax-exempt status of the bonds issued and depreciation deductions that, in effect, shift millions from the federal treasury to the state's coffers. GAO calculated that the annual taxation cost of $1.2 billion in tax-exempt bonds issued for Virginia's Pocahontas Parkway, South Carolina's Southern Connector and Nevada's Las Vegas Monorail was as much as $35 million a year. South Carolina and Virginia also lose up to $3 million a year in state tax revenue.

Beyond the accounting illusion created by the up-front payment, GAO identified a distinct lack of willingness of state governments to perform honest cost-benefit analysis of projects before agreeing to undertake them. For example, no "public interest" study was done before state and local politicians signed off on the Chicago Skyway and Indiana Toll Road deals. GAO reported that Oregon's experience shows that this could be a mistake. That state's department of transportation hired a consultant to assess the added cost involved in a proposed public-private partnership model to build a new highway. The analysis found the costs "were not justifiable given the limited value of risk transfer in the project."

GAO suggested the US Department of Transportation might be to blame for the rush to embrace tolling regardless of the cost to the public.

"Despite the need for careful analysis, the approach at the federal level has not been fully balanced, as DOT has done much to promote the benefits, but comparatively little to either assist states and localities weigh potential costs and trade-offs, nor to assess how potentially important national interests might be protected in highway public-private partnerships," GAO concluded.

A full copy of the report is available in a 205k PDF file at the source link below.

Source: Highway Public-Private Partnerships (Government Accountability Office, 7/24/2008)