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In brief...

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FUNDING AMERICA'S INFRASTRUCTURE NEEDS: PUBLIC PRIVATE PARTNERSHIPS MAY HELP CLOSE INFRASTRUCTURE GAP

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I. INTRODUCTION

The election of a new president, one who is determined to improve the nation's infrastructure while at the same time saddled with the burden of a troubled economy, has forced a paradigm shift in the national conversation about public infrastructure projects. Each day, it seems, brings tidings of renewed economic pain, job losses, and ballooning state and federal deficits. Yet against this grim backdrop, President Obama has called for a massive new investment in American infrastructure, to stimulate the economy and to create jobs. The question for many in the business of infrastructure—contractors, engineers, architects and urban planners—is simple but significant: where will the money for this massive new investment come from?

II. A NATIONAL INFRASTRUCTURE CRISIS

The collapse of the I-35W Bridge in Minneapolis on August 1, 2008 sounded the alarm on our looming national infrastructure crisis. For years, state and local governments, industry groups, and the public have clamored for federal funds to upgrade decaying transportation infrastructure across the country. In 2003, the American Society of Civil Engineers (ASCE) determined that 27% of the nation's bridges were structurally deficient or functionally obsolete, meaning that they were "closed or restricted to light vehicles because of [their] deteriorated structural components" or "cannot safely accommodate current traffic volumes, and vehicle sizes and weights."[1] Our highways system, the primary conduit for Americans traveling to and from workplaces in every sector of the economy, is increasingly suffocated from a lack of investment: a Federal Highway Administration report determined that freight highway bottlenecks cause 243 million hours of freight delays each year, at an annual delay cost of $7.8 billion; and this figure is dwarfed by the ASCE's estimate that 4.2 billion hours of traffic delays per year cost Americans roughly $78 billion in lost productivity.[2] The federal government, for its part, has recognized the needs for significant investments. President Obama was elected, in part on a pledge to rebuild America's infrastructure, and in his first month in office has undertaken to do so.

The vanguard of the Obama Administration's massive infrastructure investment proposals is contained in the "economic stimulus" package recently passed by Congress—the American Recovery and Reinvestment Act of 2009. The Act provides approximately $120 billion in direct infrastructure spending, including $48 billion specifically for transportation infrastructure projects (such as bridges and highways).[3] According to the Administration, this massive infrastructure spending will jump-start the construction industry and generate 400,000 new jobs in American infrastructure.[4] However, the stimulus package, while large by any traditional measure, is only one step in the Administration's infrastructure agenda. In what the President calls the "the single largest new investment in our national infrastructure since the creation of the federal highway system in the 1950s,"[5] his Administration has laid out ambitious plans for infrastructure improvements that will require significantly more money than what is contained in the recently passed stimulus legislation.

III. PUBLIC-PRIVATE PARTNERSHIPS

The ASCE estimates that $1.6 trillion is needed over a five-year period to bring the nation's infrastructure to a good condition.[6] In order to meet this need, and in addition to massive governmental appropriations, the states and the federal government are likely to leverage money from the private sector to multiply the effect of federal and state infrastructure spending. Thus, one of the most immediate, and likely, vehicles for the coming infrastructure boom will be the Public-Private Partnership.

Public-Private Partnerships (PPPs) differ from traditional U.S. public procurements in several key aspects, including financing, operation, and procurement. PPPs are organizational structures by which the private sector finances, builds, rehabilitates, maintains, and/or operates specific public sector activities in exchange for a contractually specified stream of future returns. PPPs can include, for instance, private sector-financed development and operation of infrastructure, whereby a private company builds and operates infrastructure and/or provides services in exchange for commuter fees (such as toll revenue) or a significant share of the revenue stream; or, alternatively, a partnership for private sector-financed rehabilitation and operation of a hospital, prison, airport or energy facility, which is then operated by the private entity and "leased" to the appropriate

Construction *Briefings*

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Construction *Briefings* (ISSN 0162-3176) is issued monthly, 13 times a year with two issues in January; published and copyrighted 2009 by Thomson Reuters • 601 Opperman Drive, P.O. Box 64526 • St. Paul, MN 55164-0526 ■ http://www.west. thomson.com ■ For subscription information: call (800) 221–9428, or write West, Credit Ordering Processing • 620 Opperman Drive, P.O. Box 64833 • St. Paul, MN 55164-9753 ■ Periodical Postage Paid at St. Paul, MN ■ Postmaster: Send address changes to Construction Briefings • 610 Opperman Drive • P.O. Box 64526 • St. Paul, MN 55164-0526.

federal, state or local government authority for a negotiated fee.

The purpose of PPPs is to more efficiently (and economically) deliver a needed project or service that would otherwise have been provided by the government through traditional public sector procurement. Because PPP projects are funded in part through private capital, they provide a means of delivering public services at lower "up front" cost to the government. Particularly in the case of costly infrastructure projects, sharing financing burdens with private entities can significantly reduce budget constraints. At the same time, private entities often benefit from generous performance incentives as a reward for their increased risk.

The system differs from traditional notions of "privatization" or "outsourcing," whereby a government entity actually transfers responsibility for, and title to, an asset to the private sector.[7] In a Public-Private Partnership, either the public entity or the private entity may own the underlying asset. In the case of a hospital, for instance, a private entity may finance and build the facility with the intent to operate it and "lease" it back to the local municipality. On the other hand, in the case of an airport, a city of municipality might "lease" the airport to a private entity to operate, for an annual fee, while retaining ultimate ownership of the asset.

In the case of infrastructure projects, PPP agreements can be multi-faceted, with several competing interests. Whereas public construction projects are typically awarded pursuant to longstanding and well-understood competitive bidding regimes, PPPs often are designed to foster innovation, are geared towards specific performance metrics. This means that under some circumstances, it may in fact be more advantageous to the public entity to engage in a PPP with more open-ended specifications, designed to maximize the private entity's ability to deliver the required end-asset with greater creativity and efficiency. According to the Federal Highway Administration:

> Low bid construction contracts for projects with significant technology and systems may not accommodate risks of new approaches. For such projects, many states and agencies have found that special approaches (often requiring legislation) may be necessary. In particular, procurements for more complex projects where the private partner is providing multiple services may involve trade-offs that may require direct discussion and negotiation. Alternative procurement methods include quality-based awards in which the owner establishes a benchmark for comparing the services and qualifications of potential private sector partners in order to identify the bidder that can provide the public partner with the best overall value for services sought. For example, for a project that involves the installation of electronic toll collection equipment, the owner may want to include performance standards for reliability and speed of installation, and offer the bidders the opportunity to share in the increased revenue from accelerated installation and reliable operation.[8]

PPPs are changing how the states and the federal government think about funding transportation infrastructure projects. Long a staple of public procurement in the United Kingdom and elsewhere abroad, PPPs are increasingly favored in the United States, as dwindling budgets make partial private financing an attractive option. Moreover, as increasing numbers of states and municipalities engage in PPPs to build and operate critical infrastructure, both public and private entities can more accurately assess the potential benefits of PPP arrangements. Large transportation infrastructure projects across the country are using PPPs to maximize transportation resources and increase efficiency within the transportation sector:

- In January 2005, the Skyway Concession Company, LLC assumed control of the Chicago Skyway, a major toll road formerly operated by the City Department of Streets and Sanitation.[9] In exchange for $1.83 billion, Skyway Concession contracted to operated and maintain the road (with rights to toll revenues) under a 99-year lease.

- In 2007, the Missouri DOT selected Missouri Bridge Partners to replace or rehabilitate 802 bridges in Missouri in the next five years, under a Design-Build-Finance-Maintain agreement including an availability payment funding mechanism that is tied to technical and performance targets.[10]

- In 2008, the state of Virginia commenced work under a $2 billion PPP agreement with Fluor Corp. and the Australian company Transurban to add a 14-mile, four-lane high-occupancy-toll stretch to the Capital Beltway. Tolls will be based on demand, and will change throughout the day according to real-time traffic conditions to manage congestion.[11]

- In October 2008, the City of Chicago entered into a $2.5 billion long-term lease agreement with Midway Investment and Development Company, a private investment group, which will operate and maintain Midway Airport for a term of 99 years.[12]

The concept of building and operating infrastructure through the use of PPPs has become increasingly common. Presently, 23 states have enacted enabling legislation permitting the government to build transportation infrastructure using PPPs.[13] Several states have taken unique approaches towards PPPs, with some states operating tentative pilot programs, while others have enacted broad enabling statutes permitting them even to accept unsolicited proposals for transportation infrastructure projects.[14] Each of these states, however, has shown a commitment to explore PPPs as one option in trying to upgrade and maintain transportation infrastructure. Thus, while the contours of PPP projects will be defined by the individual state regulations, and will mirror the risks and costs assumed by the public and private entities, it is likely that PPPs will continue to become an increasingly popular vehicle for undertaking large infrastructure projects.

IV. PROPOSED NATIONAL INFRASTRUCTURE BANK

Another facet of the Obama Administration's vision for long-term investment in state, local and national infrastructure is a proposal to create a National Infrastructure Reinvestment Bank. Specifically, the President has proposed setting aside $60 billion over 10 years to fund the bank, which would use this money to finance critical infrastructure projects – including highways, bridges, roads, ports, air, and train systems.[15] According to the President, this investment would lay the foundation to finance nearly $500 billion in new infrastructure projects.[16]

The President's call mirrors bipartisan proposals in Congress as well. In the 110th Congress, both the U.S. Senate and the U.S. House of Representatives considered legislation to create such a National Infrastructure Reinvestment Bank.[17] Under those proposals, which are bound to resurface in the 111th Congress with support from the Administration, the Bank would consider state and local infrastructure projects seeking a minimum federal investment of $75 million—and finance the projects with direct subsidies, direct loan guarantees, long-term tax-credit general purpose bonds, and long-term tax-credit infrastructure project specific bonds.[18] The National Infrastructure Reinvestment Bank would provide another vehicle to substantially increase access to capital for large-scale infrastructure projects, from which states, municipalities, and, it is likely, PPPs, would ultimately benefit.

V. TRANSPORTATION REAUTHORIZATION

Although the Administration's plans for a National Infrastructure Reinvestment Bank are yet to be finalized, a more immediate undertaking will be the Transportation Re-Authorization bill, which authorizes Federal surface transportation programs for highways, highway safety, and transit. The current authorization, which provided approximately $244 billion in such funding for 2005-2009, must be re-authorized this fall, and it is likely that the Administration will use the Transportation Re-Authorization to continue to expand its investment in American infrastructure.[19]

While the Transportation Re-Authorization bill provides the Administration with another opportunity to implement its infrastructure agenda, it is clear that public money alone will not suffice. Once again, it is likely that the Administration will seek to maximize federal appropriations by leveraging its investment to encourage increased private investment in infrastructure. At his Senate confirmation hearing, incoming Secretary of Transportation Ray LaHood put the issue plainly: "We are going to reauthorize the transportation bill this year and there is not going to be enough money to do all the things that all of us want to do and I think we do have to think outside the box."[20] Among the "outside-the-box" measures proposed by the Secretary was the use of Public-Private partnerships for transportation infrastructure projects.[21] Efforts by the Administration and Secretary LaHood to engage Public-Private Partnerships are also likely to find support in Congress. Delivering the keynote address at the June 2008 American Public Transportation Association Rail Conference, Speaker of the House Nancy Pelosi made it clear that PPPs are key to improving national infrastructure:

> Private investment is playing an increasingly larger role in public infrastructure. Innovative public-private partnerships are appearing around the country, bringing much-needed capital to the table. It is important to ensure that the public interest is well-served in public-private partnerships, since they are here to stay and likely grow in importance.[22]

Based on the Administration's desire to undertake Eisenhower-scale infrastructure improvements, Secretary LaHood's disposition toward PPPs, and Congressional support for leveraging federal dollars to maximize the public benefits of transportation appropriations, it is likely that PPPs will play a key role in the upcoming Transportation Re-Authorization.

VI. CONCLUSION

The recently-passed American Recovery and Reinvestment Act of 2009 demonstrates the Obama Administration's commitment to make a significant investment in American infrastructure. Even as it makes this substantial down payment, however, the Administration is seeking additional means of generating investment in transportation infrastructure. The proposed National Infrastructure Reinvestment Bank and the upcoming Transportation Re-Authorization represent critical components of the Administration's agenda, as well as a substantial potential source of federal funds to encourage and invest in transportation infrastructure projects. Public-Private Partnerships, already recognized in 23 states, are also likely to receive increased attention as vehicles for maximizing the effect of this massive federal investment as it is channeled through the states to upgrade and operate critical infrastructure.

For additional information regarding critical issues in American infrastructure, and the emergence of Public-Private Partnerships, please visit the following:

- The Official Blog of the U.S. Secretary of Transportation: http://fastlane.dot.gov/
- The Federal Highway Administration's State-by-State analysis of Public-Private Partnership enabling statutes: http://www.fhwa.dot.gov/PPP/tools_state_legis_statues.htm
- The National Council for Public Private Partnerships at: http://www.ncppp.org/

- The American Society of Civil Engineers, Report Card for America's Infrastructure: http://www.asce.org/reportcard/2005/index.cfm

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