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# Guidance for State Implementation of ISTEA Toll Provisions in Creating Public-Private Partnerships

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Federal Highway Administration



**Message by Administrator Rodney E. Slater:  
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Financing the investment requirements of our Nation's transportation infrastructure will become both more demanding and more sophisticated throughout this decade. The nature of this challenge has been continually reinforced.

The Intermodal Surface Transportation Efficiency Act (ISTEA) passed by the Congress in 1991 recognized the challenge by expanding the eligibility criteria for funding projects and by providing opportunities for innovative financing techniques to foster investments.

President Clinton's commitment to bring the Federal budget into balance will result in greater scrutiny of funding trade-offs in future years and require new creative solutions to fund transportation's capital needs.

Vice President Gore's Report of the National Performance Review outlines steps to be taken to make government more effective and efficient. One of these steps, "Using Market Mechanisms to Solve Problems," stresses that "As we reinvent the Federal Government, we ... must rely more on market incentives and less on new programs."

The shared goal of the Federal Government and the States to finance and rebuild our Nation's transportation infrastructure can be achieved if a full spectrum of financial resources is employed. The financial tools used elsewhere in both public and private sectors of the Nation's economy must be brought to bear on transportation's needs in the next decade to expand funding opportunities. Additionally, provisions of ISTEA together with new electronic and traffic management technologies will create new financial capacity.

Consistent with this, ISTEA provides State and local governments with new options to fund and develop much needed highway and transit improvements. The legislation permits States, for the first time, to use tolls as a supplement to conventional fuels and vehicle taxes on much of the Federal-aid system. The ISTEA also permits States to develop new cost-sharing partnerships with the private sector. To date, a number of projects have been financed as public-private partnerships; a series of others are actively under construction.

In light of the need to leverage resources to meet infrastructure investment requirements, States may want to seriously examine the potential of these partnerships to expand funding available for transportation projects. Opportunities offered by private partners in highway development include innovations in financing, design, and construction.

As part of FHWA's commitment to ensure the development and availability of a menu of financing alternatives for the States to meet their surface transportation needs, this publication provides guidance on issues States should consider when developing legislation to take advantage of the expanded opportunities presented in ISTEA.

This document is one of a series of undertakings by FHWA since 1991 designed to provide technical assistance in the area of public-private partnerships. Additional materials are currently being prepared to assist interested States by documenting case histories of initiatives and experiences related to public-private partnerships that have been undertaken to date.

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# PREFACE: PURPOSE OF THIS DOCUMENT

In recent years, the growth in transportation infrastructure needs in the United States has outpaced the growth in available funding. Expanded employment of direct user charges provides one mechanism to stretch available funding. In addition, a number of States have passed laws to allow and encourage private sector participation in the development, financing, operation, and even ownership of public-use transportation facilities. Toward that same end, the 1991 Intermodal Surface Transportation Efficiency Act (ISTEA) provides new mechanisms for applying Federal-aid funding to public-private partnership projects. Because the private sector requires a financial return on its investments, toll facilities are particularly good opportunities for public-private partnership structures.

The creation of public-private toll partnerships generally requires new enabling legislation that empowers a State agency to seek, negotiate, and support public-private partnerships. The presence of enabling powers could include the ability for State transportation agencies to use the power of eminent domain in private investment projects or to blend government funds and private capital in the same project financing. Legislation must also address the barriers to public-private partnerships under current law, such as procurement procedures that do not accommodate private involvement in project development or private investment in project financing.

This document is intended to serve as a guide for States seeking to make legislative changes to create a more hospitable environment for public-private toll partnerships. Section I, Executive Summary, provides an overview of the entire document. Section II, Public-Private Partnerships in Transportation, discusses the advantages of direct user fees and private sector participation, the partnership and toll provisions of the 1991 ISTEA, and several specific models for structuring the public-private relationship. Section III, Preliminary State Action Plan, discusses specific actions that can be taken while working on developing legislation. Section IV, Components of a Model Ordinance, discusses specific areas to be addressed in enabling legislation and provides examples that may be helpful to writers of new legislation. Section V, Implementation of Public-Private Partnership Agreements, discusses the steps involved in implementation. Section VI is a Glossary of Terms for the new concepts introduced in this document. And Section VII, Summary of

State Public-Private Highway Legislation, is a compilation of existing State public-private highway legislation.

This document was prepared for the Federal Highway Administration by Price Waterhouse's Transportation and Utilities Finance Group, located in Washington, DC, under contract # DTFH61-91-C-00040. Price Waterhouse researched current and proposed legislation pertaining to the formation of public-private partnerships, and discussed potential areas of concern to legislators with a variety of transportation industry experts. Some materials included in this document also utilize previous work conducted by the Transportation and Utilities Finance Group. Neither the Federal Highway Administration nor Price Waterhouse advocate the use of the specific legislative language included in these sections, nor do they attest to the State or Federal constitutionality, compliance with existing Federal, State, or local law, or the overall legal suitability and enforceability of any of the individual provisions or the combination of provisions presented herein.



## I. EXECUTIVE SUMMARY

### A. Background

Public-private transportation partnerships have become a topic of increasing interest over the past decade. With needs outstripping limited government resources, transportation officials are looking for new mechanisms to finance badly needed infrastructure. Private sector participation in public-use projects—public-private partnerships—are one possibility for meeting these needs. Public-private partnerships vary tremendously in the degree to which the private sector assumes both financial and operating risks and responsibilities, and many structures for partnerships are being explored which allow the government considerable flexibility in developing projects.

Most successful public-private partnerships are on facilities which generate revenue for the private sector either directly (through tolling or other user fees) or indirectly (through improved access to private sector facilities). Because of this, toll facilities have been among the most common types of facilities proposed for public-private partnerships. The recent toll provisions of the 1991 Intermodal Surface Transportation Efficiency Act (ISTEA) provide an additional link between public-private partnerships and toll facilities. ISTEA allows—for the first time—the commingling of Federal-aid and private sector funds on toll facilities. In addition, ISTEA expands toll facility eligibility for Federal-aid to include new construction of toll facilities, reconstruction of current toll facilities, and conversion of currently free facilities (when those facilities are reconstructed or replaced). These provisions provide significant incentives for both States and private sector entities to carefully examine the potential benefits of public-private partnerships.

However, the provisions of ISTEA regarding public-private toll partnerships are not self-implementing. In order for States to take advantage of the expanded project eligibility and the ability to commingle Federal and private funds, they must pass enabling legislation. This document provides some broad guidelines for States looking to implement some of the public-private provisions of ISTEA.

### B. Preliminary State Action Plan

The most important step any State can take is to implement enabling legislation. However, there are

several steps a State can take while seeking enabling legislation. These include:

Develop a Detailed Toll Road Program Concept. This would address a number of issues, including the anticipated implementation timetable; the expected level of State financial, political, and legal support; the potential methods of regulating rate of return; and details of the selection process, including selection criteria. During the development of this concept, the State should take advantage of the experiences of other State officials who have already sponsored public-private or toll programs in their states. As public support is often a critical factor to the success of legislation, this is also an opportune time for development of a public involvement plan.

Draft and Propose Legislation. Based on the detailed program concept, draft legislation should be developed and proposed.

Identify Potential Projects. The State may wish to specify the projects which will be considered for public-private partnerships in order to assure coordination with State and urban planning processes.

Conduct Technical Analysis of Potential Projects. If specific projects are selected, these projects should be examined for financial feasibility. This might involve travel and ridership studies, construction and operating cost estimates, and economic impact analyses, including feasibility of financing options (bonding, equity ownership, tax revenues).

### C. Major Components of a Model Ordinance

A number of major issues should be covered in the enabling legislation for public-private toll partnerships. However, the level of detail needed in the legislation will vary. Some States may find that highly detailed legislation is too restrictive, while others may feel that such specificity is necessary to ensure that projects can be carried out or that certain public interests are protected. In either case, the following major issues should be addressed:

Legislative Findings and Framework. Most State public-private partnership legislation contains a section outlining the motivating factors for the enabling

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legislation, describing the available partnership models (i.e., build-operate-transfer (BOT), build-transfer-operate (BTO)), and discussing the types of programs and policies which are to be implemented. This section should include discussions of other relevant State and Federal legislation, including the 1991 ISTEA. Further, it should identify the governmental entity responsible for implementing and operating the programs.

Implementing ISTEA Grant and Loan Provisions. Although some of the basic loan provisions of ISTEA may be enabled through the legislative findings and framework (i.e., the ability to provide grants or loans to private sector entities), ISTEA presents other options to States as well. These include the ability to establish State Revolving Funds (SRF) for leveraging further private investment, which would be seeded with repayment of basic loans. State legislation, in pursuing these options, should discuss sources of funds for the SRF, potential uses, and terms of loans to be made by the SRF.

State-Private Agreements. Public-private agreements are the instruments by which the State enforces the public-private partnerships described in the enabling legislation. These agreements are essentially legal, financial, and accounting documents describing the mechanisms and standards by which the private party and the State will share the project responsibilities, protect their interests, limit toll rates and/or share revenues, report their activities to each other, and resolve disputes. Because the risks and financial needs vary with each project, agreements must be developed for each project. Provisions can include the authority to enter into a franchise, available State aid, services and requirements, and the rights of the franchisee to toll, operate, and develop the facility. This section may also include priorities for use of revenue, rate-of-return regulation, service requirements, and provisions for default.

Supplemental Sections. Other legislative provisions may be included depending on each State's unique situation. Some of the issues that may be addressed include: procedures for integration of public-private partnership projects into the regional, State, and local planning processes; procedures for handling unsolicited proposals, either for projects already in the long-range planning process or new projects not yet considered; procedures for handling termination or extension of the franchise agreement and determi-

nation of the agency responsible for the facility after reversion to the State. The legislation may also specify goals for social or environmental objectives to be applied to privately developed facilities.

#### **D. Implementation Issues**

The primary steps to be taken immediately following the enactment of legislation include:

Identification of a Single Agency Contact. For each project, it may be desirable to identify one specific government agency to enter into public-private agreements on behalf of the government so as to bind all other agencies within that government to the terms of the agreement. It can be counterproductive to require a private company to negotiate a public-private infrastructure agreement with several agencies at once, or to endure the threat of adverse actions by one agency after the public-private agreement is signed by another.

Development of the Final Project Selection and Negotiation Process. In order to identify and select projects for final negotiation, bid evaluation criteria and the project selection process should be clearly defined. Although this may be included in legislation, generally States leave the final project selection criteria and procedures to the responsible government agency. This allows the State greater flexibility in seeking proposals from the private sector and in choosing projects to be constructed.

Issue the Final Request for Proposals (RFP) and Select the Winning Proposals. The RFP can be formally announced through traditional State procedures. An alternative process would involve the issuing of an RFQ (Request for Qualifications), which is a process of selecting potential bidders which meet certain requirements. The purpose of this step is to insure that bidders who demonstrate they can handle the contract requirements are selected before bids are solicited. The State would then issue the final RFP only to the select group of qualified respondents. This may reduce the administrative burden of evaluating project proposals. The winning proposal is then selected based on the requirements specified in the RFP.

Negotiate Public-Private Agreement. In developing the franchise agreement, the allocation

of rights and responsibilities between the public agency governing the project and the private developer is important. Examples of these partnership-defining rights and responsibilities are: the explicit right to use design-build construction phasing, considerations which may affect the competitiveness of the private developer, compensation allowances for planning and permitting costs, reimbursement for State services, and minimum standards for facility design, safety, and maintenance levels. Another key issue to be negotiated in a public-private partnership is regulation of return to the private entity. The return on any project must meet the private sector needs without sacrificing public welfare. There are a number of issues which should be considered when negotiating rate regulation. Implementation of rate regulatory provisions, risk management provisions, and tort liability considerations should also be included in the agreement.

Final Steps. Final steps include execution of the negotiated franchise agreement for the facility and the ongoing oversight.

## **II. PUBLIC-PRIVATE PARTNERSHIPS IN TRANSPORTATION**

### **A. Introduction**

In the process of searching for new ways to finance needed infrastructure projects, States have begun to experiment with innovative financing mechanisms and private sector financial participation. The increased interest in tolling has contributed to this trend. This section explores some of the reasons for the trend and describes Federal support for tolling and public-private partnerships as provided for in the 1991 ISTEA, which allows Federal-aid funding to be applied to public-private toll projects. In addition, this section describes the major public-private partnership structures that have been used successfully in a wide variety of infrastructure projects around the world. These structures are the framework for building new partnership legislation.

### **B. Background on the Shift to User Fees and Public-Private Partnerships**

Steady increases in demand for new or improved infrastructure have raised the popularity of user fees for all types of infrastructure, including tolls, as well as new financing mechanisms involving private investment. In fact, public-private partnerships and toll financing are often closely linked, as private investment may require a corresponding revenue stream to repay the investment. Furthermore, there are a number of reasons other than a gap between demand and available public funding that make toll financing and public-private partnerships attractive options for transportation projects. These other benefits are discussed in the following sections.

#### **1. Public-Private Partnerships**

##### **a. Overview**

The long history of private development of railroads, seaports, canals, and tollways in the United States is evidence that private involvement in transportation infrastructure is neither a minor nor a recent phenomenon in the United States. Indeed, although American *public-use* transportation facilities have come to be overwhelmingly government-owned, the United States still has a higher portion of its total transportation and non-transportation infrastructure in private hands than any other industrialized nation in the world. For these reasons, private ownership of infrastructure and related public-

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private partnerships is part of the process by which America has been and will continue to be built.

Public-private partnerships differ from both the privatization of public services (i.e., sale of public services to private firms) and the sale of existing government-owned enterprises to private firms. In service contracting, the government is usually in complete control of the service provided and bears nearly all of the operating and financial risk in the project. The private contractor bears only modest risks and receives commensurate rewards. The sale of government-owned enterprises usually involves a wholesale transfer of property, people, risks, and responsibilities to the private sector. Public-private partnerships, on the other hand, are intended to share the planning, financing, and even the management burden in a way that improves the efficiency and level of service to the users of a project beyond what either partner could provide alone.

#### **b. Benefits of Public-Private Partnerships**

The key to the success of public-private development is taking advantage of the complementary strengths of the respective partners. The private partner contributes its willingness to finance large-scale projects based on the potential return on investment. The tools for seeking this return are investor capital, bank financing, and increased efficiency and cost-effectiveness from profit-driven procurement, design, construction, and operations. The public sector provides a system planning perspective and criteria for quality of service and safety. It can help obtain right-of-way, permits, and even some of the supporting financing. The public presumably benefits from this “efficient” sharing of responsibilities. Thus, the use of public-private partnerships for toll road development provides benefits to both the private and public sectors. The private sector benefits from the opportunity for (but not the guarantee of) profits, and the public sector benefits from potential access to the facility sooner than under traditional public development. Additional potential joint or individual sector benefits include the following:

- The private sector identifying markets and acting as a financial catalyst. Private sector firms can explore new and untested markets and initiate transportation projects where the government has not identified the need for specific transportation projects, as well as in cases where it has. In both cases, the private partner can

be a highly motivated catalyst for providing new funds for major projects that cannot be initiated and completed quickly through the planning, permitting, land acquisition, financing, and construction phases due to funding constraints imposed by formula-based allocation of limited State revenues. Private sector project development also introduces efficient opportunities for value capture and joint commercial development, and may be more likely to take advantage of innovative pricing, marketing, and service strategies.

- Efficiency and speed. Because the financial success of private sector toll projects is driven by demand for the facility, there are significant incentives for the private entity to respond quickly to apparent demand. In addition, private developers interested in maximizing net revenues and minimizing costs may seek significant time and cost savings through innovative methods of highway development. Governments often must employ rigid procurement procedures designed to provide equitable access to all potential contractors and to protect the public interest, not all of which necessarily contribute to the timeliness of a project. The private development approach, on the other hand, may increase quality and cut red tape and the time to build through more direct contracting of services. Finally, private sector manpower and expertise can also supplement public sector manpower, thus reducing public overhead.
- Innovation in design and construction. Private sector participation in transportation projects places a premium on life-cycle cost reduction via innovations in design and construction methods and the installation of efficient operating technologies such as Electronic Traffic and Toll Management (ETTM) and Intelligent Vehicle Highway Systems (IVHS).

As noted earlier, the most important benefit of public-private partnerships is the efficient sharing of the responsibilities, risks, and rewards according to the respective strengths of each party. In a purely public sector infrastructure project, the Federal, State, or



local government assumes all responsibility for compliance with regulations and bears all financial risk. In a purely private infrastructure project, the firm takes upon itself the same risks and responsibilities. In many cases, however, the private sector would be unwilling to enter into high-risk projects without some support from the government such as obtaining right-of-way, project credit support, or protection from frivolous torts, legislative changes, or competition from parallel facilities that could harm the financial viability of the project. For their part, State governments are generally unwilling to permit private construction and operation of public-use transportation facilities without retaining some influence over safety, quality of service, and user fee rates. Public-private partnership structures offer a variety of arrangements which take these considerations into account, thus allowing the public and private sectors to share in the responsibilities, risks, and returns of infrastructure investment.

**c. A Brief History of Public-Private Partnerships**

Private sector involvement has been growing in all areas of infrastructure, from water supply to corrections facilities, but transportation may be particularly well suited to private participation. Toll roads and toll bridges, airports, rail systems, and some transit facilities can often generate enough revenue from user fees and neighboring commercial development to attract private capital. Moreover, even in projects which cannot cover their costs with user charges, a private sector partner may be a contributor of revenue or a joint development partner to enhance access to commercial enterprises. The move to public-private partnerships is being driven by four public works megatrends of the last quarter of the century:

1. The percentage of the nation's Gross National Product that is devoted to spending on public works spending has declined by nearly 50 percent between 1975 and 1990.
2. The Federal share of the Nation's total spending on transportation infrastructure has declined by a similar percentage over that time.
3. Taxpayer resistance to general tax increases at all levels of government has had a powerful effect on spending. At the

same time, competition for government funds from areas such as health care services, education, and corrections has increased.

4. Citizens increasingly prefer direct "at-the-door" user charges over other forms of public works financing and support user fee increases as an alternative to general tax increases; since 1984, the portion of transportation infrastructure financed by user fees has grown from roughly one-quarter to over one-third.

The trend toward user charges as a financing mechanism led the U.S. Congress in 1987 to create an extensive pilot program for Federally assisted toll roads and, in 1990, to allow local airports to charge a per-passenger fee. Such policy changes favoring direct user charges are opening new opportunities for public-private partnerships, because wherever a transportation project can collect user fees or attract commercial development, a public-private partnership can be created.

The Intermodal Surface Transportation Efficiency Act of 1991 introduced the option of private participation in Federal-aid toll projects, including roads (except Interstate), bridges, and tunnels. Public-private partnerships can now be formed to reconstruct and toll existing Federal-aid roads, bridges, or tunnels, or to develop new toll projects. In many respects, this legislation is one of the more important events in the history of public-private relationships. However, the legislation cannot stand on its own. New State legislation that parallels and implements the public-private toll provisions of ISTEA is needed in order to allow partnerships to form.

**d. Recent State Public-Private Partnership Laws**

State transportation officials are not bound by ISTEA to support public-private partnerships. Indeed, they also have the choice of continuing with traditional project development or working exclusively with public toll road authorities. However, those States that wish to foster public-private partnerships in transportation, with or without the help of Federal-aid funds, will need legislation empowering a public agency to seek, assist, and direct public-private projects. Only a few States have passed legislation to allow the blending of public and private funds in a transportation project, the accelerated

procurement of transportation systems, and the use of State powers on behalf of privately developed projects.

In the Virginia Highway Corporation Act of 1988, the first modern public-private legislation was passed. In 1989, an act passed the California legislature setting up a program to implement public-private partnerships, and more recently California has begun to explore the use of ISTEA in such areas as project credit enhancement and State revolving loan funds. In 1991, Arizona passed a private toll road law and received several proposals. As of the fall of 1993, one of the California projects and the Virginia project have been financed and begun construction. Massachusetts focused on the creation of intermodal public authorities through the merger of existing transportation agencies, with the new agency empowered to make use of ISTEA toll provisions on existing as well as new facilities. By the fall of 1993, several more States, including Florida, Minnesota, Missouri, Texas, and Washington have passed new laws authorizing the private development of public-private toll facilities. The Minnesota and Washington legislation were designed to take advantage of the ISTEA provisions.

## 2. The Direct User Fee Approach

The shift towards increasing use of public-private partnerships has been accompanied by increasing

public support for user fees, especially tolls. User fees can be defined as the amount charged directly to the facilities' users.

### a. Benefits of Direct User Fees

Direct user fees are increasingly accepted because charges are directed to the actual consumers of particular public services (thus forgoing cross-subsidies by non-users). Because the financial success of toll projects depends upon the degree to which citizens endorse the product, project sponsors have a strong interest in choosing needed projects, charging acceptable fees, and providing quality services in order to guarantee a return on their investment.

### b. History of User Fees and Tolls

Tolling is not a new concept in the United States. In the late 1700s and early 1800s, several toll facilities, including roads, bridges, and some canals and other types of improvements, were authorized by the States and developed by private citizens. It is estimated that between 10,000 and 20,000 miles of toll roads were in operation in the United States by the 1830s. This was the major method by which any transportation improvements were made during that time in history. A few similar projects still exist, primarily at river crossings in low-traffic areas.

By the end of the 19th century, it was apparent that

Activities on Federal-aid Facilities Eligible for Toll Financing and Public-Private Partnerships	FEDERAL-AID SHARE			
	Interstate		Non-Interstate	
	Highways	Bridges/ Tunnels	Highways	Bridges/ Tunnels
Initial construction of toll highways, bridges, tunnels, and approaches to these facilities	NA	NA	50%	80%
Reconstruction of toll highways, bridges, tunnels, or approaches	50%	80%	50%	80%
Resurfacing, restoring, and rehabilitating of toll highways, bridges, tunnels, or approaches	50%			
Reconstruction or replacement of free (non-Interstate) highway or toll-free bridges or tunnels on or off the Interstate together with conversion to toll facilities	NA	80%	50%	80%
Preliminary feasibility studies of the aforementioned toll construction activities	50%			

the nation's road transportation system was in need of significant improvements and that ad hoc private development was unlikely to yield the type of comprehensive network needed to help economic growth. After a series of small funding initiatives, a national highway policy was codified in the Federal Highway Acts of 1916 and 1921. Tolls were prohibited on roads built with the new Federal aid. Although little toll road construction occurred around this time, private toll bridges flourished. In 1928, the national Congress franchised 75 private toll bridges over interstate waters and State legislatures franchised many more.

Toll road construction saw tremendous growth in the U.S. in the 1940s, with Pennsylvania, New York, New Jersey, and Maine beginning to build toll turnpike projects. The construction of these turnpikes demonstrated that the public was willing to pay user fees for the use of modern highways.

Passage of the Federal Highway Act in the 1950s, which originally established the Interstate System, led to a sharp decline in toll road construction. Using Federal funds generated by a 4-cent-per-gallon gas tax and increased excise taxes on motor vehicles and parts, the Act authorized construction of 41,000 miles of new Interstate roads, with 90 percent of the funds coming from the national government. With the exception of approximately 2,000 miles of expressways newly incorporated into the Interstate System, tolls were expressly prohibited on the system. This legislation provided the framework for most major highway development in the United States until the end of the 1970s.

The 1980s were a period of renewed interest in toll facilities. The cost of simply maintaining the existing system of highways began to overtake the funds available from traditional sources and left few resources for adding new capacity. Faced with limited Federal aid for non-Interstate construction, the States asked Congress to provide matching funds to construct toll roads.

In addition to public toll facilities, governments in the 1980s were increasingly interested in private investment in public-use infrastructure. In Europe, private ownership of public-use infrastructure was already a common practice. With the collapse of socialism and the shift to market economies, developing countries began to follow the European practice of first seeking proposals from private companies before embarking on a government-funded

transportation project. By the mid-1980s, American policymakers also began to consider the merits of private investment in infrastructure, especially highways, since toll financing, whether for publicly or privately operated highways, offered more capacity without drawing upon scarce gas tax revenues.

By 1987, the State-level interest in tolling encouraged Congress to pass legislation to authorize a "pilot program" under which up to 35 percent Federal aid would be available to construct toll roads in nine interested States: California, Colorado, Delaware, Florida, Georgia, Pennsylvania, South Carolina, Texas, and West Virginia. Building on the 1987 legislation, the ISTEA extended the toll program to all 50 States and increased the maximum Federal share from 35 to 50 percent. In addition, States could elect to use Federal funds to pay up to 50 percent of the costs of building or expanding a non-Interstate toll facility, including those with private sector participation. Because of the new legislation and renewed interest in toll road construction, it is estimated that by 1992 over 1,300 miles of new toll facilities were being planned or were under construction in the U.S.

### C. The New Toll Provisions of ISTEA

The Intermodal Surface Transportation and Efficiency Act of 1991 makes significant amendments to Title 23, United States Code (Title 23) provisions governing highway transportation. Among these changes are new provisions which allow loans made by a State for toll project financing (public or private) to be reimbursed from the State's apportionment of Federal-aid highway funds.

ISTEA did not change the basic Federal-aid highway mechanism. Specifically, Federal aid is available to *reimburse* States for expenditures they have made on eligible projects. ISTEA expanded *types of expenditures* that are eligible for reimbursement (i.e., loans are considered an eligible State expenditure, with the loan itself rather than what the loan was used to purchase being eligible for Federal-aid reimbursement), the *types of projects* that are eligible (i.e., a variety of new toll facilities, reconstruction of toll facilities, and reconstruction with toll conversion projects), and the *identity* of the facility owners (privately owned and joint public-private projects are now eligible in addition to State-owned projects).

Nor did ISTEA change the *form* of the Federal aid.

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It is still an apportionment to the State, and may be contributed to the eligible project to pay for eligible expenses. If Federal-aid loans are used on an eligible project, loan repayments remain with the State, although they must still be spent on any types of projects eligible under Title 23. However, aside from this requirement, once Federal-aid funds have been used to reimburse the State, the Federal identity of these funds has been extinguished. Among other things, the loan repayments might be reloaned or used for improvements to highway and transit projects.

### **1. Expanded Project Eligibility**

Under ISTEA, the eligibility of toll projects for Federal-aid funding has expanded significantly to include: construction of new toll facilities (except highways on the Interstate system); reconstruction, resurfacing, restoration, and rehabilitation of existing toll facilities; and reconstruction or replacement of currently free facilities and conversion of the facilities to toll facilities (except for Interstate highways). Federal-aid funding for these projects may be commingled with revenue bond proceeds backed by tolls and/or with private capital. In addition, the revenue bond proceeds and/or private capital can be counted as the State's matching share. Finally, the tolls do not have to be removed upon recovery of construction costs. Under ISTEA, tolling may continue after recovery of these costs and revenues applied to operations and maintenance, debt service, reasonable returns on private investment, and other eligible purposes authorized under Title 23.

The table below summarizes eligible projects and their respective Federal-aid share.

### **2. Public-Private Partnerships**

Because ISTEA allows commingling of Federal, State, and private sector funds, and sharing of responsibilities between public and private sectors, the new law paves the way for significantly increased use of public-private partnerships as a highway development tool. The emerging collection of potential private partners includes investor, construction, management, and technology companies. Under contracts, leases, and public utility-type franchise agreements, these entities may design, finance, construct, and operate new highway facilities or participate in the repair and expansion of existing facilities.

### **3. Loans Under ISTEA Section 1012(a)**

ISTEA also allows Federal-aid funding to be recycled, since the funds can be either loaned or granted to a toll project. If the funds are loaned, the repayments (including interest) are made to the sponsoring State, where they remain to be used for other transportation projects. The funds are not returned to the Federal Government. These repayments can then be used to fund other transportation projects eligible under Title 23 free of the Federal requirements that originally accompanied the Federal-aid funds.

### **4. State Revolving Funds**

While ISTEA does *not* explicitly mention the creation of State revolving loan funds (SRFs) for toll projects, such funds may be a natural extension of the basic ISTEA project loan. State revolving loan funds have been utilized for many years, usually as a mechanism for supporting local economic development. The basic mechanism involves three steps:

1. The State provides an initial grant or loan to the revolving loan fund agency.
2. The agency lends the money and receives loan repayments.
3. The agency uses the loan repayments to make new loans.

The process continues through limitless loan-and-repay cycles. If the agency makes a profit on its loans (i.e., lends the money at an interest rate that is more than sufficient to cover bad loans and keep up with inflation), then the size of the loan fund will grow over time.

The Clean Water Act of 1987 authorized the use of Federal wastewater treatment construction grants to act as seed money for State-level revolving loan funds to finance local wastewater treatment plants. The implementing agencies typically lend out money to local governments at interest rates that are less than what the local government would have to pay had it gotten the loan on its own, if it could have obtained the financing at all. The idea was to stretch the available Federal aid as far as possible and to create a new financing vehicle for environmental protection. A similar principle could be applied to State revolving loan funds for toll projects.

## 5. State Matching Requirements

The State matching requirement of eligible project costs can be met in several ways, including a State appropriation, proceeds from revenue bonds (secured by the project or other sources) or general obligation bonds, and private capital, whether in the form of equity or debt secured by the toll project.

## 6. Private Project Eligibility Requirements

In order to establish a public-private partnership which is eligible for Federal-aid funding under ISTEA, a contractual agreement must be negotiated between the State and the private entity proposing to develop the facility. This agreement may include the roles of the respective parties, allocation of responsibilities, and financial arrangements. ISTEA specifies only that the private developer/operator/investor is limited to a reasonable return on the invested capital. Through the agreement, the State exercises its responsibilities for compliance with all of the applicable statutory requirements under Federal law, such as environmental compliance. Other terms of the contract are entirely up to the State and private entity. There are no specific eligibility requirements for private sector partners under ISTEA; however, States may wish to specify particular requirements in enabling legislation.

## 7. Reconstruction Opportunities

Reconstruction of currently free Federal-aid facilities is also eligible for ISTEA funding. Currently free facilities, including Federal-aid highways, bridges, tunnels, and approaches to these facilities, may be converted to tolls to help cover the portion of the reconstruction not funded by Federal aid. Conversion of a free Federal-aid facility to a toll facility must be part of a major reconstruction activity. Examples of reconstruction include addition of new lanes to increase capacity, replacement or reconstruction of existing lanes, or introduction of controlled access coupled with construction of interchanges. The reconstruction can be done by the highway agency or as part of a public-private partnership arrangement. The highway agency (or the private company operating under an agreement with the highway agency) may then collect tolls on the facility to recover the reconstruction investment.

## D. Models for Structuring the Public-Private Relationship

Public-private toll road development involves the collaboration of a public sponsor and a private partner to finance, construct, and operate a new road or improvements to an existing road. For each project, the structure of the public-private partnership will depend on which party (or parties) is responsible for:

- obtaining and supporting financing for the project;
- directing and funding the design, planning, and construction of the project;
- holding legal ownership of the project; and
- operating the facility and collecting toll revenues.

Because private toll roads are public-use projects, the State or local government may often regulate safety, quality of service, toll rates, and/or profits on these facilities. This section discusses some of the principal models used in public-private toll road development. Traditional public toll authorities are discussed briefly in the following section.

It is important to note that ISTEA does not specify particular models for the public-private relationship. However, all of the models discussed below can be accommodated within ISTEA's requirements so long as all Federal Highway Administration implementation guidelines are met and the projects are supported by appropriate State public-private partnership legislation. The models are listed in order of declining private involvement and increasing public involvement.

**Build-Own-Operate (BOO)**—A private consortium finances and builds a facility, and then owns, operates, and collects revenues on the facility for an unlimited time. For example, the Ambassador Bridge on the United States-Canada border is privately owned and operated. This bridge and a nearby tunnel, which is partially owned by the same private firm, serve most of the cross-border traffic from Detroit, Michigan, to Windsor, Ontario, at a toll rate of approximately one dollar per car.

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**Build-Operate-Transfer (BOT)**—A private consortium receives a concession to finance, build, own, and operate a facility for a limited time period (usually 20 to 40 years), after which the facility is transferred to the sponsoring government free of charge. The eventual transfer of the facility to the government makes the BOT model appealing to many government officials. BOT is becoming one of the most common models for private financing of transportation infrastructure around the world.

**Build-Transfer-Operate (BTO)**—A private consortium finances and builds a facility, but transfers ownership to the government immediately after construction is completed. The private consortium then leases the facility from the government, operates it, and collects revenues for a limited franchise period (usually 20 to 40 years), after which all rights to the facility are transferred to the government. Even though the government may “own” the facility from the first day of operations, full financial responsibility usually remains with the private firm and is not transferred to the government.

The BTO model may be preferable to the BOT model when some form of government ownership of the facility is an advantage. For example, the California toll road demonstration projects employ the BTO model in order to ensure government control over the projects and to limit the tort liability of the private consortia.

**Buy-Build-Operate (BBO)**—A private consortium buys an existing facility from the government, expands or repairs it, and then operates and collects revenues (usually tolls) on the facility on a permanent basis.

**Lease-Develop-Operate (LDO)**—A private consortium leases an existing facility, expands or repairs it, and then operates and collects revenues on the facility for the duration of the lease. Ownership is continuously held by the government, but the private partner is allowed and encouraged to invest in the facility, to recover its investment through payments and fees, and to pay royalties or share profits with the government owner.

**Temporary Privatization**—A private firm takes over operation and maintenance of an existing non-toll facility, expands or repairs it, and operates it as a toll facility until the firm collects enough revenue to recover the cost of the expansion/repair, including a reasonable return on capital, or until its temporary

franchise expires. Title is continuously held by the government. Unlike the LDO model, the expiration of the lease is usually tied to the final recovery of the capital investment cost, and the rights of the private partner (the lessee) are more limited.

**Wraparound Addition**—An existing government-owned core facility is expanded by a private firm, which then holds title to the addition only. However, the private firm operates the entire facility, including the original government-owned facility. Both parties have an ownership stake in the final facility and, in most cases, the financing or grants in the core government-owned facility do not have to be repaid.

Although this list does not describe all of the possible variations for structuring a public-private project, it does encompass most projects in which the private sector would bear a high degree of financial and operating responsibility. The first three models have generally been employed for new facility development, while the last four models listed are more appropriate for the expansion or repair of existing facilities. These last four models may represent the real future of public-private partnerships for tollways in America, since there is a much greater need for the repair or expansion of existing infrastructure than there is for the construction of entirely new facilities. Moreover, investing in such reconstruction may be viewed as less speculative than investing in all-new facilities. The traffic on an existing facility, whether it is already tolled or not, provides valuable assurance to private developers/investors that there is at least a basic level of demand upon which to build future traffic growth and to recover the cost of the repairs or expansion. Finally, recovery of investment in an existing project may be quicker than in a new facility for a number of reasons, including the shorter project time line. This shorter time horizon is usually more appealing to both investors and the government partner.

These models are more than abstract lessons in structuring public-private relationships; they are the framework around which the components of a model ordinance are ordered. Moreover, several models from public alternatives to privatization options can be included in the same legislation, and doing so would probably make it easier to tailor public-private partnerships to the varied transportation needs of the State. For example, Arizona’s private toll road legislation includes provisions for both the Build-Operate-Transfer model (first used in Virginia’s legislation) and the Build-Transfer-Operate

model (first used in California's legislation), thereby stimulating project proposals that would not have been made with just one model. ISTEA expanded the traditional public toll authority provisions to allow private sector options as well.

The new public-private toll provisions of ISTEA make it attractive to include even more models in State legislation. For example, the Lease-Develop-Operate and Temporary Privatization models are particularly well suited to the ISTEA provisions allowing the use of tolling on reconstructed facilities, while the loan and grant provisions for new facilities are well suited to the Build-Own-Operate, Build-Operate-Transfer, and Build-Transfer-Operate models. As State-level ordinances are developed, each of these models must be tailored to the institutional, legislative, and constitutional environment of each State. It is then left to the State implementing agency to tailor the projects to the models authorized by the legislature.

#### **E. Traditional Public Toll Authority**

Although the traditional public toll authority does not incorporate private sector participation in the ways that the models described above do, it nonetheless provides an alternative structure for tollways. This section discusses a number of variations of the traditional public toll authority, and provides examples of each.

City or County Government: Some local toll road and bridge financial and ownership aspects are completely controlled by a local government. Local taxes and bond revenue may be set aside for specific toll projects as the need arises, and the toll revenues are disbursed as the local government sees fit. An example of this is the City of El Paso and the El Paso International Toll Bridge.

Local Commissions or Authorities: Other toll entities are created by State statute and act like independent State commissions. They are completely financially independent of the local government, although they may be directed by a board of commissioners appointed by the government or may actually be a division of the local government. These authorities have ultimate financial responsibility for all commitments entered into and completely fund their own projects. Examples are the Burlington County (NJ) Bridge Commission and the Harris County (TX) Toll Road Authority.

Dependent State Authorities: In essence, this type of authority acts as a financial extension of the State department of transportation. The authority is responsible for all debt issued, but transfers the bond revenues and the operation of the toll system to the State under a lease agreement. The lease payments received from the State are then applied to service the debt. An example of this model is the Kentucky Turnpike Authority.

Independent State Authorities or Commissions: Many State commissions and authorities are autonomous in financial responsibilities such as fixing toll rates and charges as well as repayment of debt, but subject to some degree of political control as the governor appoints members of the board and the authority's debt issuance may or may not be subject to review by a State finance board. No funding is received from the State, and ultimate payment of debt is the sole obligation of the authority. Examples of these State commissions are the Oklahoma and Kansas Turnpike Authorities.





### III. PRELIMINARY STATE ACTION PLAN

To implement a public-private toll partnership program most States must enact enabling legislation. In recognition of the considerable time that may be required to enact new legislation, States can benefit by adopting a preliminary action plan which includes steps that can be taken prior to and immediately following enactment of enabling legislation. This section will describe the kinds of issues that should be addressed, and proposes a series of steps to implement an action plan. States should consider this only as a guide, and not hesitate to use another approach that fits their individual situation best. However, the following example may be helpful in considering such an action plan.

#### A. Develop a Detailed Toll Road Program Concept

A detailed program concept should address the following issues:

- Type of program to implement. The State should first determine how it wishes to structure its toll road program: private concessions only, public toll authorities only, or a combination of the two approaches. It may also wish to define a Statewide system of toll facilities or consider initiating the toll concession program as a pilot program. This would provide the State with experience in managing a new form of project development while minimizing the risk and cost to the State. Even under legislation that allows full implementation of a public-private partnership program, it would be wise to limit the number of initial projects to gain experience with the techniques before full implementation.
- State financial support. States may wish to provide direct financial support to toll road concession programs to help stimulate private sector interest in the concept. The State should seek to minimize the financial exposure that results from such support. Possible support mechanisms include: Federal-aid participation, direct loans, loan guarantees, establishment of a State Revolving Loan Fund (RLF), supplemental State-established entities such as special assessment districts, and ear-

marking revenues from the project into an escrow account for project financial backing.

- State political and legal support. States may need to provide assurances to private partners that would reduce political and legal risks. The State can provide this support by considering measures to limit the tort liability of the private partners, ensuring that investors are entitled to fair compensation in the event of a State expropriation, and establishing a process by which investors could seek a judgment and collect damages on a timely basis in the event of a State contract default.
- Toll regulation. One of the most important areas of risk for investors is toll regulation, or the risk that the State will not allow sufficient toll rate increases to provide investors with a reasonable return on investment. One way to reduce this risk is to design the toll rate regulatory mechanism such that maximum toll rates or returns are set and adjusted according to a predetermined formula and rate increase opportunities are frequent, fair, and fully automatic.
- Review of existing laws and procedures. The State should thoroughly review the requirements of the existing laws in order to identify potential barriers to a concession program, including: police powers, procurement regulations, and economic regulations, among other barriers. Special provisions for implementation of a toll road program may be necessary to attract private developers and financial institutions willing to absorb the risk of building and operating toll road projects. Also, consideration must be given to providing for appropriate integration of privately conceived and developed projects within the State and local legal framework, especially with existing planning and environmental processes.
- Project selection. The selection of the route and design for a tollway concession project can be handled many ways. For example, a private entity could be allowed to identify the route location as

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well as design, build, and operate the facility. Or, the State may wish to identify the route within a selected corridor or system and obtain environmental clearances, and then put the project's final design, construction, and operation out to bid. Many other possible selection procedures could be developed that fit into this spectrum. In any case, a well-designed and implemented concession program would maximize the communication between public and private partners in selecting routes and project designs.

- **Bid selection criteria.** It is important for the State to establish clear criteria for selecting proposals in order to communicate the State's objectives to the private proposers and allow them to compete fairly and openly for the concessions. If the State is concerned that too many bids without serious merit may be received, it may be desirable to hold a two-stage acquisition process. One method of doing this is to issue a Request for Qualifications (RFQ) during the first stage to determine which private entities or consortiums have sufficient engineering and financial resources needed to carry out a franchise. In the second stage, the State would issue a Request for Proposals (RFP) to the qualifying firms.
- **Public involvement.** Broad public support is essential for successful program implementation. The State should have an organized plan for involving the public, particularly highway users, throughout the process of developing the toll road program and subsequent projects.
- **Outside advice.** It is often useful for the State to seek advice on developing a public-private toll road program from State officials who have already sponsored toll road programs in their own States and independent financial and engineering advisors with experience in public-private partnerships. These parties can help the State avoid problems that have occurred in other toll concession programs and enhance the attractiveness of the program to private investors.

## **B. Develop/Revise Proposed Implementing Legislation**

Assuming that a State has carried out an analysis to provide a detailed program concept that meets its program needs, it could proceed to develop proposed implementing legislation that takes into account the issues outlined above.

Proposed public-private partnership legislation may also be introduced into the State legislature by other parties. Some of these sources include private developers or large engineering firms attempting to forward single facilities of interest to them, financial interests attempting to forward programs with features that increase investment in highway facilities, and legal interests specializing in innovative finance deals. All of these interests may see an opportunity to create investments that will provide a financial return to them and their investors.

These investments could increase the financial resources that can be placed into highway facilities that are critically needed in many States.

## **C. Identify Potential Projects**

In anticipation of passage of enabling legislation and in order to begin early coordination with Statewide and urban planning processes, the State may wish to begin preliminary selection of specific systems, corridors, or routes for improvement under a public-private partnership program. Once the legislation is passed, the scope of the program can be established based on the preliminary information developed during this phase. Alternatively, the State may wish to allow the private partners to select, or assist in selecting, the specific routes for concession. This would depend on the model adopted in the enabling legislation.

## **D. Conduct Technical Analyses of Potential Projects**

To encourage private participation in the projects, the State must have a clearly defined basis for evaluating any proposals submitted by the private partners. Technical guidelines should cover, as a minimum, requirements for:

- ridership surveys and traffic projections under varying toll rate assumptions;
- construction and operating cost estimates;

- economic impact analysis;
- financial feasibility analysis; and
- public opinion surveys.

Preliminary guidelines could be developed and refined before the legislation is passed. This would facilitate implementation of the program should it gain legislative support. Once State laws permit development of public-private roads and bridges, the State should conduct technical analyses of potential systems, corridors, or projects in order to determine that the projects are financially feasible and in conformance with State and local transportation plans and improvement programs. These analyses could be conducted by the State, although it may be reasonable for the State to obtain some of the information and analyses from the private partners.

**E. Develop a Request for Qualifications (RFQ) and/or Request for Proposals (RFP)**

An RFQ/RFP can be developed in the following stages:

- Based on the detailed program concept and proposed implementing legislation, develop a preliminary RFQ/RFP. The RFQ/RFP should contain detailed instructions for private firms to submit proposals to the State to operate a toll road concession.
- Once legislation is passed, the State may wish to circulate a preliminary RFQ/RFP to State officials that have sponsored toll road programs in other States, and/or independent advisors with experience in public-private partnership projects, and the public for comment.
- The State may also benefit by seeking additional input, possibly by holding a conference open to all interested parties to discuss the preliminary RFQ/RFP.
- Develop final RFQ/RFP.



#### IV. COMPONENTS OF A MODEL ORDINANCE

This section outlines topics commonly addressed in State enabling legislation for public-private partnerships. The level of detail needed in the legislation will vary: some States may find that highly detailed legislation is too restrictive, while others may feel that such specificity is necessary to ensure that projects can be carried out or that certain public interests are protected. For the most part, brief and relatively non-specific legislation usually requires a highly motivated and entrepreneurial-oriented implementation unit in the agency, as well as the cooperation of other State agencies that may have jurisdiction during project implementation. For such an agency, detailed legislation may be burdensome and may interfere with the creation of the very partnerships the law was intended to foster. However, more detailed legislation may be required to overcome the barriers created by other State laws and agencies and to assure legislators that the public interest is being protected.

In the following sections, each topic is discussed in some detail, and, where available, excerpts from existing or draft State legislation are presented as examples of what other States have done or are considering. It is very important to note that the provisions below are excerpts used as examples of legislative options being explored by some States, and are not offered as a unified model ordinance.

##### A. Legislative Findings and Framework

Most State public-private partnership legislation contains a discussion of the legislature's findings regarding transportation infrastructure and public-private partnerships. These sections outline motivating factors for enabling legislation, and discuss the types of programs and policies which are to be implemented. Included in these sections are discussions of other relevant legislation at a State or Federal level, including the 1991 Intermodal Surface Transportation Efficiency Act. In general, this section will also discuss the governmental entity to be responsible for implementing and operating the programs, as well as the partnership models available for doing so.

##### 1. Legislative Declarations

State legislation often begins with an introductory section that includes a declaration of purpose and a

discussion of the compelling reasons for enacting the bill. This introductory section helps clarify the State's goals and can provide overarching principles for guiding the implementing agency and potential toll road developers. California took this approach in the opening sections of its Assembly Bill 680 passed in 1989:

*The Legislature hereby finds and declares all the following:*

*(a) It is essential for the economic well-being of the State and the maintenance of a high quality of life that the people of the State of California have an efficient transportation system.*

*(b) Public sources of revenues to provide an efficient transportation system have not kept pace with California's growing transportation needs, and alternative funding sources should be developed to augment or supplement available public sources of revenue.*

*(c) One important alternative is privately funded Build-Operate-Transfer (BOT) projects whereby private entities obtain exclusive development agreements to build, with private funds, all or a portion of public transportation projects for citizens of California. California Assembly Bill 680, Section 1*

The declaration of purpose may include specific discussion of State needs and objectives for the legislation, as in the California Assembly bill cited above, as well as a broad statement of support for public-private partnerships. Note that California's declaration specifies a particular model for the public-private relationship. Alternatively, the legislation can specify multiple models (e.g., BOO, BTO, LDO, etc.) or leave that decision to the implementing agency and private toll road developers.

##### 2. Reference to ISTEA Toll Provisions

States may wish to include in enabling legislation a reference to the 1991 Intermodal Surface Transportation Efficiency Act and its relevant tolling and public-private partnership provisions, particularly if the State wishes to make Federal aid a substantial part of its support for the projects. The following proposed legislation for Arizona addresses the ISTEA provisions:

*3. Apply for, receive, and accept, from any Federal agency or any other governmental body, grants for or in aid of the design, construction, reconstruction, resurfacing, restoring, rehabilitation, replace-*

ment, maintenance or operation of toll and non-toll highways, bridges and tunnels, or study of the feasibility of such activities, and enter into any contracts with the granting body, or any other governmental body and with private entities as may be required to qualify for such grant. The Department may transfer or lend the proceeds of any such grant, or utilize such proceeds available for credit enhancement, to public agencies or private entities, on terms and conditions complying with applicable Federal and State law and otherwise acceptable to the Department. Arizona Chapter 26, revisions as proposed by HNTB, Section 28-3203

### **3. Identification and Empowerment of Implementing Agency**

#### **a. Institutional Framework**

In most States, the current institutional framework for transportation planning is not conducive to public-private partnerships. Many States use legislation to identify and empower a specific agency responsible for project implementation, as in the following language from Arizona and Florida:

#### ***Powers of the Board***

##### ***A. The board shall:***

- 1. Review and approve or deny the application provided by section 28-3062.***
- 2. Supervise and control the operator in the performance of its duties under this article and this title.***
- 3. Correct any abuse in the performance of the operators' public duties.***

***B. The board may require from the operator a report describing the nature of its contractual and other relationships with individuals or entities contracting with the operator for significant financial, construction or maintenance services. The board shall review the report and other materials as it deems necessary to determine improper or excessive costs.***

***C. The board shall approve a transportation facility constructed or operated pursuant to this article only if a reasonable alternative route exists. Such a transportation facility shall:***

- 1. Accommodate the same type of motor vehicles as the existing alternative facility.***
- 2. Provide a route that is at least as direct as the existing alternative facility.***

Arizona Chapter 26, Section 28-3064

***Prerequisites for construction, operation, extension, or enlargement of a private toll roadway.—***

***(1) A person may not construct or operate a private toll roadway unless the Florida Transportation Commission has issued a certificate authorizing such construction or operation. A person may not extend or enlarge a private toll roadway for which a certificate has been issued unless the commission issues a certificate authorizing such extension or enlargement.*** Florida House Bill 175, Section 3

Under the current institutional framework, promising partnership projects are often overlooked or subordinated. Participation in the planning process by private infrastructure developers or joint venture partners is generally limited to routine citizen hearings and public comment period. Moreover, there is usually no office within a transportation agency to which private developers can turn with their proposals or problems. Changing this framework is important for States seeking to attract private investment.

The creation of an office within the transportation agency to coordinate and support public-private partnerships can foster a new kind of thinking within the agency, be a source of educational research and grantee support, and provide a liaison with the private sector encouraging new projects and more productive public-private dialogue. This office may be more effective if placed within the budget and policy-making apparatus of the transportation agency and given some authority over those activities. It also can be used as the government's agent in negotiating public-private agreements or to support negotiations managed by another department or agency.

#### **b. The Proposal Solicitation and Negotiation Process**

In addition to the implementation provisions noted above, it may also be helpful, if not essential, to include provisions that create a new or improved conduit for soliciting, receiving, evaluating, and negotiating partnership proposals. Most State procurement decisions are made on a fee-for-service basis, in which the contract is awarded to the contractor with the lowest price, provided that detailed service or product specifications are satisfied. The private contractor takes little or no risk in the procurement. However, a public-private toll partnership, in which the private partner is taking most or all of the financial risk, is not well suited for this procurement environment.

California approached this problem by having lengthy and relatively informal meetings with poten-

tial private developers before the formal Request for Proposals was issued. More formal discussions took place after the submission of proposals and before the negotiation process began. As a result of these outreach efforts, the project selection and negotiation process went relatively smoothly, since many of the potential obstacles—including ground rules for the negotiations, critical issues to be addressed, and possible points of contention between the developers and the State—had been ironed out in advance. In essence, the State adopted a “user-friendly” process outside of its normal procurement process that took into account the special needs of both the developers and the State.

#### **4. Powers to Provide Grants, Loans, and Other Aid to Private Entities**

The basic philosophical notion that best drives legislation creating a new procurement process is that public-private toll partnerships are public-purpose projects in which the private partner is an important participant. Therefore, many of the actions which might be inappropriate or unavailable for purely private purpose projects—the acquisition of right-of-way for a private party, the incorporation of existing government-owned facilities into a private project, or the blending of public and private funds in a single project—may be a necessary and appropriate part of a toll partnership process. Many of these issues should be addressed in the type of enabling legislation discussed in this document. Others may have to be addressed by amendments to other State laws or changes in transportation agency policy.

Many States do not have legislation enabling public agencies to award grants or loans to private entities for the private development of transportation infrastructure. However, recently, such obligations of Federal-aid funds were specifically authorized by ISTEA. Although many States give their State transportation agencies wide latitude in the use of Federal-aid funds, it may be necessary to detail the additional authority through State legislation. The following language, allowing such financial support and other forms of government participation in a partnership project, has been proposed for the State of Arizona:

*In addition to the agreements of the type described in Chapter 26, the department may enter into agreements, on such financial and other terms as the department may deem to be in the public interest, with private entities for the private development*

*and operation of toll transportation facilities and for private participation in public toll highways financed pursuant to this chapter. Subject to the determination being made in the final sentence hereof, such agreements may provide for one or more of the following:*

- a. Sale or lease to the private entity by the Department of undeveloped real property to be utilized in connection with the private toll facility.*
- b. Sale or lease to the private entity by the Department of an existing State highway to be utilized in connection with the private toll facility.*
- c. Lending to a private entity the proceeds of bonds issued pursuant to this chapter, to be utilized by the private entity to finance the construction of a private toll facility.*
- d. Imposition of tolls on currently existing State highways, and making toll revenues available for the financing of privately constructed toll facilities.*
- e. Engaging private entities to operate and/or maintain toll highways constructed by the Department pursuant to this chapter.* Arizona Chapter 26, revisions as proposed by HNTB, Section 28-3202

Issues to be examined for such grants include:

- whether the requirements of Federal anti-trust law should be applied to State exclusivity;
- the characteristics of State public-private partnership statutes, e.g., treatment of a possible requirement that there be a “public alternative to the proposed toll road”;
- the nature of permissible State exceptions to “grant of exclusivity” to a private party;
- the ability to grant a “zone of no new or currently unplanned competition” around a privately developed toll facility;
- the nature of State obligations to compensate private developers for franchise infringement;
- interface with necessary exercise of State and local police powers;
- interface with ISTEA contract requirements; and
- the ability to impose State-developed constraints on local governments and the MPO planning process.

#### **5. Allowable Models for the Public-Private Relationship**

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Legislation may either leave joint venture options open for negotiation on a project-by-project basis, or specify the allowable models prior to project initiation. The following language defines a particular joint venture model, in this case the Build-Transfer-Operate model:

*An agreement with a private entity entered into pursuant to this section shall provide for all of the following:*

- 1. State ownership of the transportation facility constructed by a private entity.*
  - 2. Lease of the transportation facility to the private entity for a period mutually agreeable to the Department and the private entity.*
  - 3. Reversion to this State of the transportation facility constructed by the private entity after the expiration of the lease at no expense to the State, as consideration for the lease granted by the State.*
- Arizona Chapter 26, Section 28-3051, Part C

The various models that might be incorporated into the legislation include: Build-Own-Operate (BOO); Build-Operate-Transfer (BOT); Build-Transfer-Operate (BTO); Buy-Build-Operate (BBO); Lease-Develop-Operate (LDO); Temporary Privatization; and Wraparound Addition. These models are discussed in greater detail in Section II of this document.

## **B. Implementing the Grant and Loan Provisions of ISTEPA**

### **1. The Basic Project Loan**

Federal-aid funds remain an apportionment to the state, which may then loan the funds to eligible projects for eligible expenses under Title 23. Provided that the legislative framework has allowed the State to make loans and grants to private sector entities, no further legislation is required to allow the State to make a basic project loan.

### **2. Creation of a State Revolving Loan Fund**

#### **a. The Basic SRF Mechanism**

State-level enabling legislation is probably required for the establishment of such SRFs. A State must first establish the fund itself and create an appropriate oversight mechanism to ensure that the fund is properly managed, is properly funded, and does not make inappropriate loans (e.g., loans that have little

prospect of being repaid). The following draft legislative provision, which was proposed in Arizona, addresses the establishment of revolving loan funds:

#### ***Revolving Loan Fund***

*(a) In general. There is hereby established a Revolving Loan Fund. The Fund shall be maintained and administered by the Board in accordance with the provisions of this subtitle and such rules as the Board may from time to time prescribe. The Fund shall be available in perpetuity for the purpose of providing financial assistance in accordance with the provisions of this Section. Subject to the provisions of any applicable bond resolution governing the investment of bond proceeds deposited in the Fund, the Fund shall be invested and reinvested in the same manner as other State funds. Any investment earnings shall be retained to the credit of the Fund.*

Arizona Chapter 26, revisions as proposed by HNTB, Section 28-3205

This enabling legislation may address the following issues:

- **Creation of the SRF.** Legislation establishing the SRF may state the purpose of the SRF (i.e., what types of loans it is intended to provide) and describe in broad terms the manner in which the funds in the SRF are to be invested. This legislation may also address uses of interest received on SRF funds and specify allowable reinvestment of these interest payments or application to other State uses.
  - **Administration of the SRF.** Legislation may specify the body which is to be responsible for maintenance and administration of the SRF. SRFs may be operated under a currently existing board. Description of oversight and review mechanisms may or may not be included in this legislation.
- b. Leveraging the SRF with Bond Proceeds**

Note that the Arizona language refers to the management of bond proceeds. This suggests that the author of the proposed provision anticipated that the fund might be “leveraged”, i.e., that the fund would borrow money from bond buyers and reloan the pro-



ceeds to eligible projects. The bond buyers would then be repaid with the loan repayments from the projects. If the State initially placed \$10 million in the revolving fund and the fund borrowed an additional \$30 million, then the State can be said to have leveraged its investment by three to one, making it possible to finance many more projects than could have been financed with only the initial \$10 million.

Using the same example, the \$10 million could be kept in the SRF as a reserve against bad loans. Such a reserve would make it more attractive for potential bond buyers to lend their money to the SRF, since there would be at least some money to repay them if some of the toll projects fell short of *their* repayment obligations.

FHWA rules require that the use of Federal-aid highway funds be tied to specific projects, eliminating them for use as a reserve for a pool of project loans. However, Federal-aid highway funds can be used to make direct project loans (as in Section II above) to the individual projects financed by the pool. This would free non-Federal-aid revenues in the pool for use as leverage for projects funded only through the SRF. Revolving loan funds often attract higher levels of private sector investment than individual projects, since the variety of different projects in the fund diversify risk.

It is important to note that almost all of the leveraged State revolving loan funds (e.g., wastewater treatment funds) currently in existence are leveraged with tax-exempt bonds issued by the State. The interest on these bonds may be exempt from Federal income tax, allowing the bonds to be issued at a lower interest rate than bonds issued by private companies. However, current Federal tax law greatly restricts the use of tax-exempt bonds for “private” purposes; i.e., the government cannot easily reloan the money it borrows to private firms or to projects in which there is a high private ownership content. Therefore, if the SRF intends to make loans to private and public-private toll projects, it may have to issue only taxable bonds or carefully manage its loans such that the proceeds of tax-exempt bond issues are not reloaned in a way that violates the Federal tax code.

#### c. Sources of SRF Funds

States may wish to include a description or list of potential and intended sources for initial SRF funding in the legislation. The following proposed lan-

guage for Arizona outlines the various sources of SRF funds:

***(b) Deposits in Fund. There shall be deposited in the Fund:***

***(1) Federal grants and awards or other federal assistance received by the State and eligible for deposit therein under applicable Federal law;***

***(2) State funds appropriated for deposit to the Fund;***

***(3) Payments received from any public or private agency in repayment of a loan previously made from the Fund or pursuant to 23 USC 129(a)(7) or successor legislation;***

***(4) Net proceeds of bonds issued by the Board which have been designated for deposit in the Fund;***

***(5) Interest or other income earned on the investment of moneys in the Fund; and***

***(6) Any additional moneys made available to the Fund from any sources, public or private, for the purposes for which the Fund has been established.***

Arizona Chapter 26, revisions as proposed by HNTB

#### d. Uses of SRF Funds

If a State creates an SRF, it will also want to address potential uses for the funds and project eligibility in the legislation. A legislative provision proposed for Arizona includes the following language to specify the uses of SRF loans:

***(c) Purposes. Amounts in the Fund may be used only:***

***(1) To make loans for the construction, reconstruction, resurfacing, restoring, rehabilitation or replacement of public or private toll transportation facilities within the State, or the study of the feasibility thereof.***

***(2) To guarantee, or purchase insurance for, bonds, notes, or other evidences of obligation issued by the developer of a public or private toll facility for the purpose of financing all or a portion of the cost of such toll facility, if such action would improve credit market access or reduce interest rates;***

***(3) To earn interest on Fund accounts; and***

***(4) For the reasonable costs of administering the Fund.***

Arizona Chapter 26, revisions as proposed by HNTB

Potential uses might include construction loans,

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long-term project loans, or contingent loans (e.g., guarantees or letters of credit) to provide reserves in case a project does not generate enough revenue to service the loan. Again, such contingencies must be provided with State funds. Federal-aid highway funds cannot currently be used for such contingencies.

SRF resources may be used as grants or loans for feasibility and planning studies, which may then be converted to a long-term project loan upon completion of the feasibility study and initiation of the project. However, because Federal laws (Title 23, NEPA) require that all environmental requirements be met before a Federal-aid highway loan can be made, such studies would have to be covered with State funds.

### 3. Loan Agreement Terms

Although loan agreement terms may be negotiated on a project-by-project basis, inclusion of basic loan terms and conditions in legislation may expedite project applications and approval. The following proposed legislation for California outlines the loan agreement terms for loans made from a proposed California's State Transportation Revolving Fund.

***Loans made from the State Transportation Revolving Fund shall bear interest at the average rate of interest earned by the State Pooled money investment Fund over the preceding twelve months. Loans repayment shall begin no later than 5 years from the date that the facility is opened to toll traffic and shall be completed by no later than 30 years from the time the loan was obligated. The amount loaned may be subordinated to other debt financing for the facility other than loan from any other public agency. The Department may charge reasonable origination fees for any loan made pursuant to this article.*** Draft wording for amendment to Section 1720 of California State Labor Code

States should consider the following points for inclusion in legislation:

- **Term of the loan.** The term of the loan includes the maximum time to beginning of repayment and the maximum time to initial payments on the loan. ISTEA requires loan repayments to begin within five years after the project is completed and under traffic.

- **Interest rate of the loan.** ISTEA requires that loans bear interest at the average rate the State's pooled investment funds earned in the 52 weeks preceding the start of repayment.
- **Subordination of the loan.** State loans eligible for Federal-aid reimbursement must be subordinate to all other project debt except loans made by the State or other public agencies.
- **Other fees.** Legislation may specify other fees (origination fees, processing fees, etc.) associated with loans made under the SRF.

### C. State-Private Agreements

Public-private agreements are the instruments by which the State enforces the public-private relationships described in their enabling legislation. These agreements are essentially legal, financial, and accounting documents, describing the mechanisms and standards by which the private party and the State will share the project responsibilities, protect each other's interests, limit toll rates and/or share revenues, report their activities to each other, and resolve their disputes. Because the risks and financial needs vary with each project, the agreements themselves must also be crafted for each project.

#### 1. Authority to Enter Into Franchise Agreements

Explicit enabling legislation may be essential for a toll concession program because of the substantial political risks faced by investors in a project. The following language from California and Illinois explicitly defines the authority of the implementing transportation agency to enter into franchise agreements, thus defining the legal and political risks to the public and private partners:

***(a) The department may solicit proposals and enter into agreements with private entities, or consortia thereof, for the construction by, and lease to, private entities of four transportation demonstration projects, at least one of which shall be in northern California and one in southern California.***

***(b) For the purpose of facilitating those projects, the agreements may include provisions for the lease of rights-of-way in, and airspace over or***

*under, State highways, for the granting of necessary easements, and for the issuance of permits or other authorizations to enable the private entity to construct transportation facilities supplemental to existing State-owned transportation facilities. Facilities constructed by a private entity pursuant to this section shall, at all times, be owned by the State. The agreement shall provide for the lease of those facilities to the private entity for terms up to 35 years. In consideration therefore, the agreement shall provide for complete reversion of the privately constructed facility to the State at the expiration of the lease at no charge to the State.* California Streets and Highways Code, Section 143.

*The Authority shall have the power:*

*(g) To acquire, or to enter into long-term contracts to acquire, privately constructed roadways, or portions or parts thereof, pursuant to Article II of this Act. Upon acquisition, such roadways, or portions or parts thereof, may become a part of the system of toll highways, operated, owned and controlled pursuant to Article I of this Act.* Proposed Illinois Act I, Section 100-8

Although State or local governments may have the authority to grant a concession under existing law, it may be that investors or other private parties will be unwilling to participate in a concession project without explicit legal authorization for the agency with which they intend to negotiate. Enabling legislation provides this authorization and indicates a commitment on behalf of the State to support the concession process.

The advantage of detailed authorization language is that it helps avoid confusion over the full powers of the implementing agency. However, detailed legislation can sometimes be the vehicle for hidden barriers to projects, restricting the government's flexibility in structuring the concession program and limiting the ability of the implementing agency to resolve issues that might arise during the public-private contract negotiations.

A government's authority to enter into franchise agreements can be more clearly defined by incorporation of descriptions of allowable activities. This is important to clarify which types of projects are authorized by the law. Examples include:

- sale or lease to the private entity by the public partner of undeveloped real property to be utilized in connection with the

private toll facility;

- sale or lease to the private entity by the public partner of an existing State highway to be utilized in connection with the private toll facility;
- lending to a private entity the proceeds of bonds issued to be utilized by the private entity to finance the construction of a private toll facility;
- imposition of tolls on currently untolled existing State highways, and making toll revenues available for the financing of privately constructed toll facilities;
- engaging private entities to operate and/or maintain toll highways constructed by the public partner.

## 2. Available State Aid, Services, and Requirements

It is especially important for governments to provide adequate assurances to private consortia with respect to political and legal risks because of the governments' unique control over these risks. Likewise, the State may want to outline its responsibilities and require some guarantees (the "strings attached" to the granting of franchise rights to the private sector) from the developers. The following language has been proposed for a private toll road law in Minnesota:

*(b) A development agreement may permit the private operator to assemble funds from any available source, including federal, State, and local grants, bond proceeds, contributions, and pledges and to incorporate an existing road or highway, a bridge, and approach structures, and related improvements into the toll facility. The Private operator shall pay the road authority the fair market value of any property incorporated into the facility or shall adjust toll charges to the public to reflect the value of the incorporated property.*

*(e) A development agreement may include authorization by the road authority to the private operator to exercise powers possessed by the road authority with respect to similar facilities.* Proposed Minnesota Private Operator Legislation, State Code 1620, February 20, 1992, Subdivision 4

Three important provisions which may be consid-

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ered in granting franchise rights are listed below:

- **Assumption of damages.** The concessionaire may assume responsibility for damages to the State or a third party resulting from the concession. However, although it is reasonable for the private consortium to bear some tort liability, the government should consider limiting the tort liability, possibly by retaining ownership of the facility and leasing it to the private consortium.
- **Right to reclaim facility.** The State may want to establish its right to reclaim a concession facility on compelling public interest grounds, with compensation to the private partner, in the cases of inadequate quality of service, unauthorized toll rate increases, or force majeure.
- **Recourse in case of default.** The State may want to establish a streamlined process (e.g., arbitration or formula) by which one party could seek a judgment and collect damages on a timely basis in the event of a default on the agreement by the other party.

There are a wide variety of other potential provisions governing State aid, services provided by the State, and private responsibilities in dealing with the State. A few of those provisions are addressed below:

**a. Exercise of State Powers on Behalf of the Private Developer**

Legislation may clarify the power of the State government to exercise sovereign power in intergovernmental disputes (e.g., disputes with or among local governments or State agencies) that interfere with the State's overall objectives for the project. Most private transportation infrastructure projects must look to the State government for approval and protection from intergovernmental disputes. Local government land-use permits or zoning exceptions are particularly threatening hurdles for private toll projects.

This is not to argue that State governments should routinely attempt to override local policymakers or their own State requirements in infrastructure devel-

opment, but only that the State may wish to ensure that the level of assistance given to private infrastructure developers is roughly equal to the power exercised by the State in its own dealings with local zoning laws and permitting procedures for highway developments.

**b. Escrow of Sales Tax Receipts**

The State may wish to provide for temporary escrow of sales tax receipts on the construction supplies used in a privately developed transportation project to be used as limited State credit support for the project. In many States, government-developed transportation projects are exempt from State sales taxes on their supplies and equipment, while privately developed projects are not similarly exempt. One way for a government to provide *contingent* financial support to a private project without risking existing funds is to place the sales tax receipts in an escrow account, which would be held only for a certain number of years and would only be used if project revenues fell short of debt service needs. After the escrow period expires, the funds (assuming they were not used) would be returned to the State treasury along with accrued interest.

**c. Special Transportation Taxing Districts**

If allowed by State law, local governments can create special transportation financing districts to capture part of the economic activity growth created by the addition of a new transportation link. Special assessment districts, tax increment financing districts, impact fee districts, and other highly specific revenue-raising techniques are increasingly being used to finance transportation improvements. The fees or taxes are usually assessed on a per-square-foot basis, although some are applied to increases in assessed property values. Most of these techniques rely on revenues collected from existing commercial development to achieve a stable revenue stream, or at least a combination of existing development and new development. The revenue streams are often used to support bond offerings.

The logic of special financing districts is simple: property owners that directly benefit from a new transportation project should be called upon to help pay for it. In fact, many special districts (such as the Route 28 project in Northern Virginia) are created at the request of business and property owners who want improvements to the roads that serve them.

**d. Government Credit Support**

It may be desirable for enabling legislation to identify at least some conditions under which limited government support could be used to back up private financing for privately developed projects. Credit support means that if a project fails to financially support itself, then another entity will step in to help pay the creditors. Government-developed projects have multiple layers of credit support available to them—concluding with taxpayers—and so can obtain low-cost financing. Privately developed projects face the same risks but lack such credit support options, and therefore may have to pay higher interest.

Transportation infrastructure, whether governmental or privately-developed, is a public-purpose project. Lending partial credit support allows governments to help provide much-needed infrastructure without bearing the full cost and risk of developing the facility itself. Such credit support should be granted for a privately-developed project on a project-by-project basis, perhaps in return for a share of the profits. In many infrastructure projects, this credit support takes the form of a letter of credit (basically, financial insurance), a deeply subordinated loan, or contingency funds held in escrow until the project is financially secure.

**e. Local Government Financial Support**

The private toll road laws of California and Arizona prohibit the use of State funds on behalf of private toll road projects, but they are not specific with regard to local government funds. Indeed, at least one of the projects authorized in California plans to use a subordinated loan from the local government in its financing structure, a prospect which both the developer and local government describe as a positive action on behalf of needed public-use highway. Because local governments derive their authority from the State, the State is usually able to prevent or support such local aid as it chooses.

**f. Tax-Exempt and Taxable Financing**

The State may wish to provide for the commingling of tax-exempt and taxable debt to finance the project in the enabling legislation. The ability to use tax-exempt debt may significantly enhance the project's ability to secure financing and add to the feasibility

and attraction of public-private partnerships.

The commingling of tax-exempt and taxable financing may be accomplished most easily by obtaining an allocation of the State's volume cap on private-purpose tax-exempt debt (Federal tax law tightly limits the total amount of tax-exempt debt in a State that any level of government may reloan to private firms). Alternatively, this may be accomplished by separating the ownership of a toll facility's individual parts.

**g. Eminent Domain**

In the enabling legislation, the State may want to grant the sponsoring government agency the right to take right-of-way and buffer land on behalf of the private partner. Private developers usually have only the power of persuasion and money to convince landowners to proffer the land needed for a project; they also may be able to convince landowners and developers that adjacent land will significantly increase in value, and may consequently be able to obtain the land as a donation or at reduced cost. Federal and State governments are generally required to pay fair market value for all land acquired.

While the Toll Road Corporation of Virginia was able to negotiate options to acquire most of its right-of-way for the Dulles Toll Road Extension using these methods, it found it necessary to gain the cooperation of Loudon County to use its power of eminent domain for some parcels. As government has discovered, a fair market offer for the land is often not enough. Private infrastructure developers will usually need the government's help, including the power of eminent domain. However, it is often worthwhile to pursue possibilities for donations or sales of land at reduced cost before taking this step. Once acquired, the land can be held by the government and leased or (depending upon State law) sold to the private partner. California's Assembly Bill 680 authorized such public acquisition on behalf of the privately developed toll roads.

Many investor-owned electric, water, and gas utilities have been granted direct use of the power of eminent domain by their State charter, and do not need a government agency to act on its behalf. However, because each privately developed transportation project is unique and self-financing, most existing State transportation partnership laws require a government agency to act on behalf of the private partner when acquiring land by eminent domain.

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### 3. Rights of the Franchisee to Toll, Operate, and Develop

States may want to define specifically in enabling legislation the rights of the franchisee to toll, operate, and develop a facility, and establish requirements for monitoring the franchise. Alternatively, these issues may be resolved on a project-by-project basis. Arizona used the following language in its draft legislation to outline these rights:

#### *Powers and Duties of the Operator*

##### *A. The operator may:*

- 1. Operate the roadway and charge tolls for the use of the roadway to receive reimbursement of costs and a reasonable return on investment.*
- 2. Subject to applicable permit requirements, cross any right-of-way if the crossing does not unreasonably interfere with the use of the right-of-way.*
- 3. Classify traffic on the roadway according to reasonable categories for the assessment of tolls.*
- 4. With the consent of the department, adopt and enforce reasonable rules including rules:
  - (a) Prescribing maximum and minimum speeds that conform to Department and State practices.*
  - (b) Excluding vehicles or cargoes or materials from the use of the roadway if exclusion of such vehicles, cargoes or materials by this State or a local authority is authorized by the laws of the State.*
  - (c) Establishing high occupancy vehicle lanes for use during all or any part of a day and limiting the use of these lanes to certain traffic.* Arizona Chapter 26, Section 28-3065*

In the following provision, legislation proposed in Illinois is even more explicit and expansive with regard to the powers (including State powers) granted to the operator, in part because of the similarity of the Investor Owned Tollroad Company to electric utilities, which have the same powers as the State in Illinois.

*Powers and Duties of Investor Owned Tollroad Company. (A) The Investor Owned Tollroad Company shall have the authority to operate the roadway, bridge, or railway and charge tolls or fees for the use thereof, and may pledge its assets, other than right-of-way, and any revenue net of operational expenses realized from tolls charged for the use of the project in order to secure repayment of any obligations incurred for the construction, alteration or operation of such a project. In no event shall the Investor Owned Tollroad Company*

*have the right to pledge, or cause lien to be created upon, project right-of-way. The debts or obligations of the Investor Owned Tollroad Company shall be limited to an amount not to exceed the cost of construction plus an amount for issuance costs and other financing expenses, a reasonable amount for reserve funds, and a reasonable return on its investment. The State or Authority shall not be morally obligated for, and shall not obligate its full faith and credit on, any financing of the Investor Owned Tollroad Company and any debt, bonds or other financing documents shall include a statement that said obligation is not guaranteed by the Authority and is not guaranteed by the full faith and credit of the State, and assumption of operation of the project shall not obligate the State or Authority, morally or otherwise, to pay any obligation of the Investor Owned Tollroad Company whether secured or otherwise. Subject to applicable permit requirements, the Investor Owned Tollroad Company shall have the authority to cross any canal or navigable watercourse so long as the crossing does not unreasonably interfere with navigation and use of the waterway. In operating the project, the Investor Owned Tollroad Company may:*

- 1. Classify traffic according to reasonable categories for assessment of tolls;*
- 2. Set tolls sufficient to satisfy the debt service incurred for the construction of the project subject to review and approval of the Authority as provided in Section 101-10(B)1;*
- 3. Make and enforce reasonable regulations, including regulations:
  - a. which set maximum and minimum speeds after review and approval by the Authority;*
  - b. which exclude undesirable vehicles or cargoes or materials from the use of the roadway;*
  - c. which establish express lanes for use during all or any part of a day and limit the use of such lanes to certain traffic;*
  - d. which determine points of access;*
  - e. which determine truck/trailer multiples;*
  - f. which determine truck weight stations;**
- 4. Acquire by purchase, grant or otherwise, and take title to, any existing public roadways, highways, toll highways, or bridges of this State, subject to the approval of the Authority and Department as provided in Section 101-7 of this Article; and*
- 5. Engage in any business other than that of an Investor Owned Tollroad Company, including the right to acquire real estate and the incidents of*

*ownership thereof in any form or personal property by private purchase, gift, or otherwise, and to sell, grant options or convey the same subject to this Article and as otherwise provided by law. With the exception of right-of-way as defined herein, the acquisition or sale of real estate or the incidents of ownership thereof under this paragraph, shall not be subject to Authority regulation.* Illinois Article 2, Section 101-10

**a. Tolling**

Most States do not have laws in place to enforce collection of tolls for public-private projects. But, because the financial feasibility of the project may be jeopardized if such authority is not explicit, States may wish to provide for this. In addition, new methods for cost-effective enforcement and tolling, such as video-based citations and Automatic Vehicle Identification, may be vulnerable to legal challenge unless the State specifically authorizes their usage in the enabling legislation.

When explicitly allowing the franchisee to collect tolls, States may also want to allow innovative tolling mechanisms such as peak-hour pricing. States could then permit private operators to vary toll rates by time of day in order to decrease congestion. Higher tolls during peak hour serve to discourage rush hour traffic, decrease congestion, maintenance costs, and air pollution.

**b. Operation and Expansion**

States may also wish to allow the private operator to determine, with the approval of the State Department of Transportation, what types of vehicles and cargoes will be permitted to use the road, bridge, or tunnel. Urban, congestion-relieving private toll roads may not need to build bridges able to carry tractor-trailers, for example, and could reduce their construction costs considerably if they were not required to do so. Most States also allow private toll road operators to vary tolls based on vehicle classifications.

The enabling legislation should also provide ground rules for the potential extension, modification, and widening of the private toll road after initial construction of the facility. If a private operator wants to extend the toll road to serve developing communities, repeating the whole franchising process may be cumbersome and inefficient. However, great care must be taken to assure there are no conflicts with

State procurement codes. In the event that traffic exceeds projected levels (necessitating road widening or the addition of new on- and off-ramps), provisions should already be in place to expedite the necessary modifications. Project-specific procedures or restrictions to handle these issues could be incorporated into the franchise agreement.

**4. Priorities for Use of Revenue**

The State may want the legislation to establish priorities for the use of the toll revenues generated under franchises, and potential uses for excess revenues. For example, Arizona requires that revenues be used (1) to maintain and operate the road, (2) to pay off the operator's debt, and (3) any excess to be deposited in a highway reserve fund.

***B. The operator shall:***

***1. Pledge any revenue net of operational expenses realized from tolls charged for the use of the roadway in order to secure repayment of any obligations incurred for the construction, enlargement or operation of the roadway.*** Arizona Chapter 26, Section 28-3065

***Disposition of excess toll revenues***

***On at least an annual basis the director shall credit all toll revenues authorized by section 28-3066 in excess of a reasonable rate of return on investment as prescribed in the written agreement pursuant to this article to the highway user revenue fund established by section 28-1598 of this title.*** Arizona Chapter 26, Section 28-3074

Private infrastructure operators are often required to pledge first lien on their toll revenues to an operations and maintenance fund. After this reserve is fully funded, toll revenues pay the debt incurred by the private operator. Revenues in excess of debt repayments but not in excess of the rate of return limit (if returns are limited) are the profits of the private toll road operator. Excess revenues beyond the limit allowed the private operator are often pledged to the State Highway Fund.

**5. Rate of Return and Toll Rate Regulation**

Economic regulation is designed to mitigate the problems associated with monopolies of public-use infrastructure. Electric and water utilities are examples of facilities for which the government grants a monopoly to a single company, but regulates the

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prices and/or profits. Too stringent limitation on rates of return or user charges may make it difficult to attract adequate investment to the project. Too lenient regulation can lead to abuses and public acceptance problems.

Because there are often competing roads and alternative modes of transportation nearby, toll roads rarely have the same degree of regional monopoly as electric or water utilities and are therefore usually regulated differently. Moreover, even if a toll road were to have complete monopoly power over local transportation, it might be such a high-risk project that any regulation would render it unfinanceable. Therefore, economic regulation of toll roads should be approached carefully and with strong attention paid to the needs of financial markets, the project risks, and the competition from existing and planned facilities.

Among the States that have passed private toll road legislation, Virginia chose to use its existing public utility commission as the regulator. However, many private developers and transportation officials believe that transportation projects are sufficiently unique that only the State DOT or Highway Commission is in a position to judge the project's finances. Moreover, well-crafted franchise agreements which include a negotiated limit or formula for toll rates or rates of return could obviate the need for continuous financial oversight of the type used for power utilities.

The following Florida legislation outlines the governing power of the State over operator toll rates:

***The department may approve or disapprove the toll rates charged by an operator. The department shall approve the initial rates if it determines that they are reasonable for the use of the private toll roadway, that they are not likely to unreasonably discourage the use of the private toll roadway, and that they do not exceed the pareto-optimum toll rate established by a traffic and revenue study performed by a traffic and revenue consultant with an established reputation in the bond markets. Upon application by an operator or upon its own initiative, the department may adjust the toll rates charged by an operator, subject to the provisions of this subsection.*** Florida House Bill 175, Section 6

In implementing Assembly Bill 680, Caltrans felt that it was preferable to control rates of return on investment rather than toll rates because

developer/operators would need the flexibility to set rates. So long as the developer/operator controls toll rates, the project is less likely to lose money if the traffic does not materialize. Moreover, Caltrans anticipated that the developer/operators would use their rate flexibility to encourage car pooling, use congestion pricing, and/or reduce off-peak-hour pricing. Incentives for doing so were written into the franchise agreements.

If the control of toll rates is left to the government, then the private developers may seek assurances that the rate adjustments can be made automatically and without undue political influences or protracted and adversarial hearings.

## **6. Duration of the Public-Private Agreement**

The feasibility of a project requires that the duration of the public-private agreement be long enough to allow the developer/operator to achieve the target rate of return on investment. The useful life of transportation infrastructure projects is measured in decades, and so is the term of financing. Typically, a toll road project will require 20 to 40 years to achieve its targeted return on investment. For that reason, California's Assembly Bill 680 legislation provides for up to 35 years of private operation before the facility is turned back over to the State. In Virginia, the Toll Road Corporation of Virginia would be allowed operate the Dulles Toll Road Extension for up to 40 years. ISTEA allows a total of 30 years to repay loans obligated with Federal-aid highway funds.

## **7. Quality of Facilities/Service Requirements**

Legislation should include some discussion of the required quality of facilities and service requirements during the period of the franchise. The following Arizona legislation provides for the monitoring and inspection of the toll facilities by the State throughout the life of the roadway project:

***If the Board approves the project, project design and connections of the roadway, the Department shall enter into an agreement with the applicant providing that the Department, on a reimbursable basis, shall:***

***1. Review the plans and specifications for the roadway and approve them if they conform to State practices.***



**2. Inspect and approve construction of the roadway if it conforms to the plans and specifications and State construction and engineering standards.**

**3. Throughout the life of the roadway project, monitor the maintenance practices of the operator and take action as appropriate to ensure the performance of maintenance obligations.**

**4. Perform other necessary services that the private entity is unable to perform, including project development and environmental impact statements.** Arizona Chapter 26, Section 28-3066 B

In the course of the construction and operation of public-private toll facilities, State standards for the quality of the facilities and services are usually applied. In addition, public policy goals for the State may include addressing the conditions of the roads, traffic congestion, air quality, and the use of high-occupancy vehicle restrictions. Although most States currently do not have standards for the operation of privatized toll facilities, effective standards should be developed and passed through to the private sector, and public policy goals regarding quality and performance incentives should also be included as objectives or at least referenced in the law.

Although the private infrastructure project must provide quality service or else it may not attract paying customers, the sponsoring government may want the developer/operator to achieve social objectives beyond customer service, such as more carpooling and lower accident rates. In order to encourage the pursuit of such objectives, the sponsoring agency can be empowered to negotiate financial incentive provisions in the franchise agreements. For example, the California toll road agreements give developer/operators the opportunity to earn more money if they increase vehicle occupancy rates or have fewer accidents per vehicle/mile. Toward that end, one of the project developers plans to allow carpools and buses to drive free, while others are considering building park-and-ride lots (where drivers of single-occupant vehicles park their cars and take buses) at some interchanges.

## **8. Provisions for Default and Agreement Modification**

Legislation should include specific provisions in case of default or the need to modify a franchise agreement sometime during its life. An example of Arizona legislation concerning default follows:

### **Default**

**A. If there is a material and continuing default in the performance of the operator's construction or operation duties or if the operator fails to comply with the terms of its agreement with the department, the board, after a hearing in which the applicant or operator has notice and an opportunity to participate, may take the following actions that the department may participate in or initiate:**

**1. Revoke the authority for the roadway.**

**2. Declare a default in the construction or operation in the roadway.**

**3. Make or cause to be made the appropriate claims under any completion or performance bond.**

**4. Take other action determined appropriate by the board under the circumstances.**

**B. If the authority is revoked pursuant to the appropriate claims under subsection A, the applicant or operator does not have the authority to construct and operate the roadway, and:**

**1. The department may construct and operate the roadway.**

**2. The department may take steps that are in the public interest including completion of construction of or additions to the roadway, closing the roadway or an intermediate step.**

**3. The operator shall grant to the department all of its rights, title and interest in the assets of the corporation.** Arizona Chapter 26, Section 28-3071

Florida addressed the default issue in slightly different language:

**Default.—If an operator commits a material and continuous violation of, or fails to comply with, the terms of its contract with the department, the commission may revoke the operator's certificate, declare a default in the construction or operation of the private toll roadway, and make or cause to be made claims under any completion or performance bonds or may take other appropriate action. Prior to revoking an operator's certificate, the commission shall provide the operator notice and an opportunity to be heard. Upon revocation of a certificate, the operator to whom it was issued ceases to have the authority to construct or operate the project that is the subject of the certificate. The department may close the project, or otherwise dispose of the project in a manner that the department determines is in the public interest. The operator shall, at the discretion of the department, grant the department without cost all its rights, title, and interest in the project, real property acquired as rights-of-way for the project, and facilities of the**

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*project.* Florida House Bill 175, Section 14

There are a number of issues of which States should be aware when drafting legislative provisions covering these circumstances:

**a. Operator Default**

The State should ensure that the State DOT has the right to develop the road in the event that the private operator fails to do so. The implementing legislation may require that, in the event of default by the private operator prior to opening the toll road, the right to develop the toll road reverts to the State. In these cases, the private operator is generally allowed a reasonable period of time to construct the road, and provisions for reimbursement for the work already completed by the private operator, if any, can be included in the franchise agreement.

The enabling legislation should limit the government's right to take over a privately developed facility to events involving serious default on the public-private agreement on key items affecting the public interest and the completion of the full franchise term. Unlimited authority to take a private facility may be too threatening to investors in private transportation projects, even if they might be promised compensation. The reason for this fear is that after taking the risk of investing in the project, they might see only a return of their principal and little or no return on their investment, and so may refuse to invest in the first place.

Causes for potential takeover should be negotiated in advance and included in the public-private agreement. Failure to live up to the terms of the agreement may constitute default under the agreement, but not all types of private-partner default should be dealt with by government takeover; fines or other penalties can also be used. Further, the government most likely would take over the facility only after adequate time and opportunity have been given to rectifying the reasons for default. Moreover, even in default, the developer may be entitled to some compensation for its investment in the facility. Finally, the project lender's rights may need to be protected in a manner similar to the protection provided for government-sponsored projects, such as giving the lender (limited) time and opportunity to select another operator or otherwise rectify the situation where a private operator defaults.

Most States provide that, in the case of full default

by the private operator, the State takes title to the road, or gives the lenders a certain period of time to remedy the reasons for default. Puerto Rico's BOT San Jose Lagoon Bridge guarantees the private operator a 12.5% return on equity if the private operator goes into default.

**b. Guarantees to the Private Operator**

Enabling legislation may specify the scope of guarantees to the private operator. The State could offer guarantees to private investors in toll road projects in order to enhance the attractiveness of specific projects or of the program as a whole. The guarantees, if any, should be explicitly described in the implementing legislation. A clear mandate from the legislature will prevent confusion and ensure that all private operators are provided the same guarantees.

Two of the most common guarantees offered to private developers of transportation infrastructure are debt repayment guarantees and traffic guarantees. Debt repayment guarantees would obligate the State to assume all or part of the debt of the private operator in the event of default or to provide subordinated loans for a specific period of time up to a pre-set amount. However, some debt repayment guarantees could decrease the incentive of private operators to operate the facility profitably. Traffic guarantees sometimes allow the private operator to extend the length of the concession period or to sell the road to the State if traffic levels are below projections.

**D. Supplemental Sections**

Other legislative provisions which may be included vary from State to State. Some general provisions are discussed below.

**1. Inclusion of Private Projects in the State System or Planning Process**

The relationship of public-private projects to existing State systems and procedures must be defined in order to fully realize the opportunities presented by public-private partnerships and ISTEA. Enabling legislation must provide for the integration of public-private partnerships into the regional, State, or local Transportation Improvement Programs (TIPs) of Metropolitan Planning Organizations (MPOs), State DOTs, or local municipalities. Along with the enabling legislation, in order to successfully include

private projects in the State system and planning decisions, a number of principles and guidelines must be established, principally affecting permitting and approval processes.

- Both the public and private partners must recognize that there are several Federal, State, and local agencies involved in the planning process, which sometimes have conflicting guidelines, interpretations, and requirements.
- A common understanding of timing and deadlines must be reached. Private partners often push for faster schedules (to allow more time for them to recover their return on investment). Private firms do not face the same procurement requirements that public agencies face, and may look to design-build strategies to further speed up the process and spread risk. However, a partnership cannot allow speed to be pursued at the expense of the public interest. Recognition of these different incentives on the part of the public and private partners within a legislative framework can help facilitate a successful partnership.
- Effective coordination between public sector transportation planners or other public agencies and private firms can help to achieve non-transportation provisions in a timely manner such as Federal and State clean air and employment requirements.

By coordinating the private sector development process and the State and urbanized area planning processes and transportation improvement plans, the public will benefit from the most cost-effective means of achieving their transportation needs. Some of the specific concerns which public-private partnership enabling legislation could address to enhance this coordination include:

- how to handle unsolicited private proposals either for projects already identified in the long range plan or TIP, or for projects not previously included in these documents;
- how the offer of private financing will affect the prioritization of and levels of

public support for a project already included in the plan or TIP;

- how a private proposal will be evaluated and ranked in relation to existing plans and improvement programs if it did not appear on the programs previously;
- how the inclusion of a private proposal will mitigate or eliminate the need for another proposal already in the plan; and
- how compliance with environmental requirements, including the Clean Air Act Amendments, will be performed.

In an era of severe budget constraints, it would be beneficial if transportation agencies would routinely consider (using input from potential private partners) whether a private firm could provide a transportation project without or with minimal taxpayer funds.

## 2. Agency Powers Following Termination of Agreement

Implementing legislation should set conditions under which the franchise agreements terminate and under which they may be extended. It also should determine which agency will be responsible for the facility should it revert to the State. The following Arizona legislation outlines steps for the termination of the franchise and the acquisition of the facility by the board.

*Termination of certificate; dedication of assets*  
*Within ninety days of the completion and closing of the original permanent financing, the operator shall provide full details of the financing, including the terms of all bonds, to the board and shall certify the date on which all debt will be retired. The board may require the operator to provide copies of any relevant documents and shall review the financing and determine the date on which all bonds or other debt constituting the original permanent financing will be retired. After establishing this date, the board shall enter the order terminating the operator's authority on a date prescribed in the written agreement with the private entity. At the request of the operator or the department or on its own initiative, the board may revise its order to modify the date for termination of the certificate of authority to account for any refinancing of the original permanent financing if the refinancing or*

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***modification is in the public interest or any refinancing for the purpose of expansion or early retirement of the debt. When the authority terminates, the authority and duties of the operator under this chapter cease, and the highway assets and improvements of the operator shall be dedicated to the department for highway purposes.***

Arizona Chapter 26, Section 28-3073

At the termination of the franchise period, the private facilities would usually revert to the State. The franchise agreement should describe the specific facility and the price (usually zero) that the State will pay for the private facility.

## V. IMPLEMENTATION OF THE PUBLIC-PRIVATE PARTNERSHIP AGREEMENT

Once enabling legislation is in place, States should define an implementation process. This would include identification and empowerment of the agency which will be the primary contact for the private entity, defining a project identification and selection framework, and defining a process to negotiate specific details of each agreement, such as rate of return, risk sharing, financing provisions, and any non-compete agreements.

### A. Identification and Empowerment of a Single Agency Contact

If the enabling legislation does not specifically identify and empower an agency which will be the primary contact point for the private sector entities, then this is likely to be the first step in implementation.

For each project, one specific government agency should be empowered to enter into public-private agreements on behalf of the government so as to bind all other agencies within that government to the terms of the agreement. It is impractical to require a private company to negotiate a public-private infrastructure agreement with several agencies at once, or to endure the threat of adverse actions by one agency after the public-private agreement is signed by another. For this reason, the California legislature chose the California Department of Transportation to negotiate the Assembly Bill 680 agreements. An Assistant Director served as the State's chief negotiator. The final agreement was approved by the Director of Transportation.

It is much more practical and efficient to delegate approval to the responsible agency head. Requiring additional approval steps after the private developer has invested funds in planning and design of a facility, such as a second *legislative* approval of a project or approval of a signatory independent from the negotiating agency, significantly discourages proposals. In both California and Virginia, authority to approve final plans (aside from the issuance of permits and licenses) is vested in the negotiating agency, acting on behalf of the Governor.

### B. Finalize Bid Evaluation Criteria

In order to effectively identify and select projects which will move into the negotiation stage, bid eval-

uation criteria must be established and the project selection process should be clearly defined. Although this may be included in legislation, generally States leave project selection processes to the implementation phase. This allows them greater flexibility in choosing specific projects or asking for proposals from the private sector.

#### 1. Project Selection

Selection of the route and tollway design for a concession project may be the responsibility of the government or the private partner. Unless there is a specific project that the government wants constructed, it may be preferable to allow the private partner to propose what it believes to be a financially feasible project.

Because its responsibilities for building infrastructure are not focused on projects which can cover their costs from user fees and neighboring development, the government is not always in the best position to identify *financially* feasible private projects, i.e., projects that consumers are willing to pay for directly through tolls. On the other hand, a private firm's interest in a project is influenced by its perception of unmet consumer demand; that is, the developer may be willing to take the risk, often a sizeable one, that people will use the project, and that they will express their demand by paying at the door (and, sometimes, in nearby commercial development).

If the private partner is allowed to select a project, the government could include route and design selection criteria in the bidding documents. These criteria could specify the approximate length, location, type of facility, requirements for an alternative route, and other government preferences. It should be noted that the private sector generally avoids projects which have not been cleared environmentally—a high risk of environmental mitigation requirements tends to discourage private investors. This may be factored into government preferences as well.

One effective means of promoting interaction between the private and public sectors is to hold a bidding conference prior to the formal solicitation for proposals. For example, the Arizona Department of Transportation invited prospective private partners to a meeting prior to issuing a Request for Proposals in order to gauge the level of interest in the projects, receive input from potential private part-

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ners on the content of the bidding documents, and encourage cooperation of the private parties in generating project ideas and pooling complimentary skills. According to public and private officials who participated in the conference, the Arizona bidding conference was highly successful at achieving these objectives.

## 2. Bid Selection Criteria

It is important for the State to establish clear criteria for selecting proposals in order to communicate the State's objectives to the private proposers and allow them to compete fairly and openly for the concessions. As a prerequisite, all winning proposals should:

- involve qualified firms with sufficient resources to implement a project;
- include construction cost, operating cost, and traffic and revenue estimates that are reasonable and consistent;
- propose a financial plan that is realistic and achievable even in the event that variations occur in the underlying assumptions;
- include a minimum private equity investment in the financial plan in order to preserve the private partner's incentive to perform efficiently and profitably. (It may result that with a low private equity commitment, private participants may be more interested in construction contracts and government financial guarantees than developing a viable toll road).

All proposals that meet these requirements must then be evaluated with respect to additional criteria in order to select a winning proposal. Examples of potential project selection criteria are as follows:

- Best Project. If the private partners are allowed to select the concession projects, the State could choose the project that best met its selection criteria. Maximum toll rates, or maximum rate of return, and the concession term could then be negotiated with the private partner. The California AB680 projects use a maximum rate of return approach, and the Arizona demonstration program allows either a

maximum rate or return or a variation of maximum toll rates.

- Shortest Term. The State could set a maximum rate of return and select the proposals with the shortest concession term. This approach is attractive because it minimizes the time before the facility is transferred to the State, and the higher required rate of return (due to the shorter term) improves the ability of the project to attract medium-term debt financing.

The disadvantage is that the higher toll rates which would result would be less acceptable to users. In addition, an objective of the State may be for the private consortium to take responsibility for maintaining the roads. A shorter term would transfer this responsibility to the State at an earlier date.

- Lowest Base Toll Rates. The State could set a concession term length and select the proposals with the lowest base toll rate. This approach minimizes the rates charged to the users, although the term may be longer than under the shortest term option. However, this approach may discourage private firms due to inflexibility in increasing the toll when required to meet debt service and operating requirements plus a reasonable rate of return.
- Highest Upfront Payment. The State could set the concession term length and the maximum toll rates, and select proposals based on the highest upfront payment offered to the State for the right to the concession.

This approach could generate upfront cash for the State for use on other road projects. However, an upfront payment would require a longer concession term and/or higher toll rates than without a payment. The upfront payment could also increase the financial risks of the project because it would constitute an additional cost that would have to be financed. In addition, it is worth noting that the project could generate substantial real estate, sales, and income tax revenues for the State even without an upfront payment.

There are numerous other criteria that can be considered when selecting proposals. For example, the time until the beginning of operation could be considered in order to accelerate opening of the toll road. Two recent examples of evaluation criteria are listed in the Arizona Department of Transportation Office of Privatization Final Request for Qualifications/Proposals for Contract Number 92-23, and the Request for Qualifications for Toll Revenue Transportation Projects from the California Department of Transportation Office of Privatization. Arizona's criteria are summarized below:

- Team Composition—Qualifications to Perform Projects Proposed. This criterion relates to the Primary Proposer, the Project Manager, Key Staff, and other members of the proposing team. The basic question is: How well does the team's qualifications, experience, and time allocation relate to the specific project proposed. (15 points)
- Capability and Capacity to Deliver and Finance Project Proposed. This criterion relates to a proposer's capabilities regarding the project(s). (35 points)
- Applicability of Privatization Program as Defined in Title 28 Chapter 26, ARS 28-3051-28-3074, and Any Other State or Federal Standards and Statutes to Proposed Project. This criterion relates to the basic or preliminary understanding of the project as related to Title 28, Chapter 26, ARS 28-3051-3074, and any other applicable State standards or statutes. (10 points)
- Commitment to Schedule. This criterion relates to the proposer's external reputation and internal capability to meet the scheduled completion date. (10 points)
- Contribution to State's Needs. These criteria relate to the importance and utility of a prospective project in meeting the transportation needs of Arizona. (30 points)
- Commitment to Perform the Work in the State of Arizona (incentive). This criterion relates to making a commitment to

perform the work required by the project in the State of Arizona. Scoring will be accomplished by applying the percent of commitment to perform the work in the State of Arizona to the maximum points available. (5 points)

- Commitment to a Disadvantaged Business Enterprise Program (incentive).

California's selection criteria are similar:

- Experience of Principal Organization and Consortium Members. (30 points)
- Record of Financial Strength to Commit to a Major Transportation Facility Project. (30 points)
- Ability to Work Cooperatively With a Broad Range of Governmental Agencies and the Public. (20 points)
- Individual Qualification of Key Project Team Personnel. (10 points)
- Organizational and Management Approach of Project, Company, or Consortium. (5 points)
- Familiarity and Experience With Automated Traffic Operations, Automatic Vehicle Identification (AVI), and Electronic Toll Collection (etc.) Systems. (5 points)

### C. Issue Request for Proposals and Select Winning Proposal

Formally announce the RFP through traditional State procedures (newspapers, industry journals and periodicals, etc.). It should be distributed to a wide group of potential private partners in order to ensure maximum participation in the toll road program. The RFP should be accompanied by material that explains the concession program concept, including a detailed description of the bidding process and selection criteria. The State should also consider holding a pre-bidders conference in order to discuss the concession program with interested parties in person.

An alternative to beginning the bidding process with an RFP is to first issue a Request for Qualifications

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(RFQ). In response to an RFQ, interested firms would submit a description of their experience with highway projects and resumes of the personnel that would manage the project. The State would then issue an RFP to a select group of the most qualified firms. The RFQ process can be effective in reducing the administrative burden to the State of reviewing proposals from unqualified firms, and reduces time and expense required for the RFP submission by interested firms.

Winning proposals should be selected through the process defined in the RFP. The implementing agency, established and empowered by the enabling legislation, ranks each proposal according to the selection criteria stipulated in the RFP, and the highest ranked proposals are selected.

#### **D. Negotiate Public-Private Agreement**

##### **1. Allocation of Rights and Responsibilities**

In developing the franchise agreement, the allocation of rights and responsibilities between the public agency governing the project and the private developer is very important for the final product of the public-private partnership. Examples of these partnership-defining rights and responsibilities are: the explicit right to use design-build construction phasing, considerations which may reduce the competitiveness of the private developer, and compensation allowances for planning and permitting costs.

##### **a. Design-Build Construction and Procurement**

Explicitly allowing private transportation developers to use the design-build mode of infrastructure development, subject to State oversight of results, may reduce construction costs. Design-build is the process in which construction begins after basic planning and design is completed, but before the more detailed construction plans are done. This speeds the time from conceptualization to project completion and reduces costs because final design and construction can be done concurrently. Currently, most State procurement laws work against this higher-speed, lower-cost mode of construction, yet design-build is the method of choice for private infrastructure development firms. Design-build can be regulated within the franchise by specifically laying out when construction may begin according to design approval.

At the present time, Federal law also restricts the use of design-build on Federal-aid highway projects. One provision, 23 U.S.C. 112 (b) (1), generally requires competitive bidding on construction contracts, with award to the lowest responsive bidder. A conflicting provision, 23 U.S.C. 112 (b) (2), requires that design contracts be based on the best technical proposal, with the price being negotiated. Although 23 U.S.C. 112 (b) (1) provides for an exception to the competitive bidding requirements if the "State highway department demonstrates, to the satisfaction of the Secretary, that some other method is more effective ...", the design-build concept has been approved by FHWA only on an experimental basis for a few contracts.

Although design-build can take on many forms, the typical process involves a contractual delegation to a builder of full authority and responsibility for assembling and managing all disciplines and resources required to complete the design and construction of the project on a fixed-price basis.

Initially, given appropriate environmental clearances, construction can begin while design is being completed. Thus, construction is accelerated and costs decrease as a result. Also, interim financing may be provided by the engineering and construction firms, if they are willing to assume the risks of financing on a fixed-price basis at that stage of design. Along with the financing risks, the risks of delay and cost increases are assumed by the contracting firms if the contract is at a fixed price.

Disadvantages of the design-build concept include the enforceability of receiving the product at a given time at a given fixed price if delays arise. Also, cost savings achieved by shifting financing and construction cost risks to the engineering and construction contractors may disappear if they require the same premiums expected by market rate financial institutions.

State procurement laws often restrict the flexibility of the public sector in designating contractors and equipment suppliers. Because contractors and equipment suppliers may constitute major partners in the private sector consortium, the State may wish to remove procurement restrictions from the private partners of public-private partnerships. Lifting procurement restrictions from the private consortia should allow the private sector to operate more efficiently.



**b. Permitting and Planning Costs**

Local implementing agencies could be allowed to fully or partially compensate private infrastructure proposers for planning and permitting costs for projects sanctioned by the State. The permitting and planning process is the period during which private infrastructure developers are at greatest risk. They could make a substantial investment in good faith planning on a project tentatively approved by the State only to see the project collapse because a key permit or financing component could not be obtained. This risk is one of the greatest barriers to private development of infrastructure.

There are three basic options available to the State government for sharing these risks and encouraging more private participation in the planning process.

1. A revolving fund could be established at the State level to reimburse the private partner, fully or partially, for planning and permitting expenses of a State sanctioned, privately developed transportation project that could not progress to construction.
2. The State government could provide a tax credit for those expenses.
3. The State government could conduct the environmental review and permitting for the private firm, which would then reimburse the State if the project goes to construction. For this option to work, however, explicit permission should be given to use Federal/State funds in support of a private project proposal.

**c. Intellectual Property Protection**

The State should consider providing intellectual property protection for unsolicited, non-competitive proposals and negotiations in progress and protecting the proposals and negotiations from Freedom of Information requests. Good faith planning and design efforts by private infrastructure development firms should not be subject to capture by competing firms. Private developers may invest considerable amounts of time, money, and expertise in identifying potential projects, developing innovative designs, drafting preliminary engineering plans, and attract-

ing partners to a consortium. If proposals are not protected from competitors, the private sector may be unwilling to expend the resources necessary for careful, innovative project selection and proposal preparation. Further, intellectual property protection may encourage the private sector to be more innovative and to conduct thorough investigations into project feasibility and design before submitting proposals. This preparation may benefit the road-using public and the private developer.

Negotiations between the public and private sectors often require revelation of highly proprietary information on corporate finances, strategic business plans, and unique design and technology. Such information should be protected, especially where the private firm is bearing the financial risk and sharing information with the State in a good-faith effort to achieve public objectives.

**d. Automatic Vehicle Identification Systems**

The ability to collect revenues is the first requirement of a private infrastructure project. Automatic Vehicle Identification (AVI), in which travelers pay in advance for electronically readable toll vouchers, is particularly important to the efficient operation of toll road projects (i.e., avoiding long toll booth queues). It also allows many more high-traffic facilities to be tolled than would otherwise be possible. Explicit recognition of this right in the concession agreement (or in the enabling legislation) protects the public-private agreement and improves a project's ability to attract financing.

**e. Limit on Free Alternative Routes**

If the sponsoring State agency has the authority to enter into public-private agreements which limit future unidentified competition from free or toll facilities within an appropriate zone around the private facility, the availability of private operators may be significantly enhanced. Project developers and their investors have every reason to expect competition from existing and planned transportation facilities, and will consider this in their development and investment decisions. If, however, after signing the public-private agreement the State were then to build a previously unidentified (e.g., not previously in the State transportation plan) facility competing with the public-private facility, the investors could face diminished revenues and difficulty in earning a

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reasonable return on their investment.

For the public sector implementing agency, the difficulties presented by exclusive franchise zones lie in the definition of the zone in terms of geographical size and time period. It can be difficult to determine the geographical area served by a road and even more difficult to forecast traffic patterns 30 years in the future. The size and duration of the exclusive franchise zone may best be determined on a project-specific basis.

However, granting an exclusive franchise zone constitutes the creation of a quasi-monopoly. This quasi-monopoly may require government regulation of rates of return, safety standards, and features that are discussed in other sections of this guide. Because the exclusive franchise zone may affect citizens who live and travel through the area, the State may create a standardized process by which affected local groups can provide input into the establishment of such zones.

In light of the many concerns affecting exclusive franchise zones for the California toll road projects, the California Department of Transportation agreed to limit parallel (providing service to/from the same areas) and some perpendicular (siphoning off development and traffic to other routes or areas) competition within several miles *unless* the private facility becomes overcrowded or reaches its allowable rate of return limit. However, perpendicular development was generally excluded from classification as a competitive facility.

**f. State Government Procurement Requirements**

The State may modify procurement requirements (except fair labor treatment and Equal Employment Opportunity requirements) for projects in which the private sector bears most or all of the financial risk for the project. State procurement requirements are a set of rules designed to ensure that the State acquires services and supplies at the lowest price for projects in which the State bears all financial responsibilities and that there is an opportunity for fair competition among bidders. The requirements are not designed for projects in which the private firm is the bearer of the financial burden and/or takes the risk that the project will not cover its costs. Therefore, State procurement requirements may need to be modified to protect public interests while at the same time allowing the private risk-bearer the flexibility to hold

down costs and share risks among its contractors. Specifically, the lead developer/operator needs the full freedom to enter into cost-effective joint venture arrangements with its private partners and suppliers.

If more than one firm or consortium offers to develop the same infrastructure project, the State will need to decide among them. In doing so, the State will need to use decision criteria more appropriate to the situation, such as: benefits to the public, most financially feasible, ease of proposal implementation/degree of local support, ability of the project to spur economic development, the track record of the participating firms in similar projects, lowest contribution from the State, highest value:cost ratio for project's users, and (as in the case of the California Assembly Bill 680 projects) the degree to which the State's minority and women-owned business objectives are achieved.

**g. Diminution of Opportunity to Earn a Reasonable Return**

The State may need the authority to negotiate with a developer/operator seeking compensation for State diminution of the opportunity to earn a reasonable return, including change of law. Any infrastructure project is vulnerable to changes in law or regulation that increase costs or reduce revenue. These impacts can be substantial, and can occur at all stages of the project, from planning to operation.

When any new laws and regulations are passed by a State that negotiated a public-private agreement, the implicit and explicit compact between the State and private partners may be violated and the private developer and investors may be vulnerable to suffer significant economic loss, for which they may be entitled to compensation. Investors would be discouraged by the potential for such changes in law without an opportunity to seek redress. For these reasons, each of the franchise agreements in California makes it possible for the developers to seek compensation for State default on its part of the agreement.

**2. Implementation of Rate Regulatory Provisions**

One of the key issues to be negotiated in a public-private partnership is regulation of return to the private entity. The return on any project must meet the private sector needs without sacrificing public welfare. There are a number of issues which should be

considered when negotiating rate regulation.

**a. Congestion/Peak-Period Pricing**

Peak-hour pricing (sometimes referred to as congestion pricing) is sometimes used in mass transit systems and, with the growth of IVHS, is now being considered for toll roads. Peak-hour/congestion pricing could be essential to the financial success of privately developed and operated alternatives to congested State-owned facilities. Thus, explicitly allowing the private operator to vary toll rates by time of day can significantly increase the attractiveness of the project.

Peak-hour pricing is also economically rational and effectively provides more service for less money. Most of the capacity in an infrastructure project is built to accommodate the bulge of users that choose to drive or ride at the same time of day. These peak-hour users should be asked to pay for the bulk of the additional capacity. Higher peak-hour prices could entice some users to off-peak hours or carpools, thus reducing congestion and allowing the facility to be smaller and less costly.

**b. Toll Regulation**

One of the most important areas of risk for investors is toll regulation, or the risk that the State will not allow sufficient toll rate increases to provide investors with an expected return on investment. There are three common methods of regulating tolls.

**i. Toll Rate Regulation**

Under the simplest form of toll rate regulation, the concession contract stipulates a maximum toll rate for each class of vehicle, and the toll rates are adjusted each year according to a pre-determined index, such as the consumer price index. Toll rate regulation is used on most existing toll road facilities, and will be on the proposed Dulles Greenway toll road project in Virginia.

The advantage of toll rate regulation is that it can be relatively easy to administer and enforce, and it ensures that real toll rates never rise above a pre-determined maximum.

The disadvantage of toll rate regulation is that it is not flexible or precise in limiting investors' earnings. Capital costs, operating costs, and traffic levels

usually vary from expected levels which can result in substantially higher or lower than expected returns for investors. Traffic levels are particularly difficult to forecast accurately. Under these conditions, rate adjustment usually is not sufficiently flexible.

An additional disadvantage of toll rate regulation is that rate adjustments can be blocked for political reasons if the adjustment mechanism is not fully automatic and frequent. Such political barriers could amount to huge losses incurred to the toll road operator.

**ii. Rate of Return on Equity Regulation**

Under rate-of-return regulation, a maximum rate of return on investment is imposed rather than a maximum toll rate. Any earnings received in excess of the rate of return ceiling must be turned over to the State. The four demonstration projects in California and two of the Arizona projects use rate-of-return regulation.

The advantage of rate-of-return regulation is that it is precise in limiting investors' earnings. Earnings are limited to a pre-determined maximum regardless of actual capital costs, operating costs, or traffic levels. In addition, the lack of toll rate limits allows the private consortium to use innovative rate setting techniques, such as peak-period pricing.

The disadvantage of rate-of-return regulation is that it can be extremely complicated to administer and enforce because it requires a reliable mechanism for tracking the private consortium's earnings on an annual basis. In addition, rate-of-return regulation is more difficult to administer when project earnings are expected to grow rapidly over time as is often the case with toll road projects. Rate-of-return regulation may be more appropriate for a stable enterprise with level earnings.

In using rate-of-return regulation, the sponsoring State must limit the developers to a reasonable return on investment without unduly interfering with the ability of the projects to attract financing. It should be understood that, with a rate-of-return ceiling, the maximum return that the developers may earn is defined, but these returns are not guaranteed. In fact, the State or the developers may not expect the private returns to reach the ceiling given traffic uncertainty or potential cost overruns; therefore, a

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rate-of-return ceiling must be set high enough to provide the developers with enough potential upside return to balance the downside risk.

### iii. Other Rate of Return Issues

In calculating the rate of return for private developers, consideration must be given to calculating it before or after taxes. The strongest argument for using after-tax calculations is due to the wide variation in tax impacts of the same project on different business structures. Arguments against using after-tax figures result from public sector wariness in dealing with private sector tax concepts. These calculations may be complicated by uncertainties regarding future tax code provision changes.

A second important consideration for regulators of private toll roads is adjustment for inflation. While upward adjustments in rate-of-return calculations are certainly acceptable to private developers, the public is justified in limiting the costs it pays to these developers. However, in order to promote the financial stability of the project, a benchmark, such as inflation, or a floor on returns to the private developer, can be used to fairly maintain the original expectations of both the public and private sectors.

## 3. Other Finance-Related and Risk Management Provisions

Other considerations for including in an agreement between the public and private sectors are State assumption of some financial risk, or development of concessions and other commercial facilities. These agreements can significantly increase private sector willingness to participate in infrastructure projects.

### a. State Financial Support

The principal business and financial risks that States frequently assume, at least in part, are toll revenue risk and debt service coverage risk. The following options are available for addressing these risks:

- Traffic Guarantee. The State could guarantee a minimum level of traffic at an agreed-upon toll rate. In effect, this would be a guarantee for a minimum amount of revenues. If the minimum level of traffic is not achieved, the State could make up the revenue shortfall or

extend the term of the franchise.

- Loan Guarantee. The State could guarantee all or a portion of project loans.
- Equity Guarantee. The State could guarantee a minimum return on equity for the equity investors, as in the Puerto Rico project.
- Insurance. Instead of providing the guarantees listed above without charge, the State could insure these risks in exchange for fees.

The State should seek to minimize the financial exposure that results from these guarantees; however, it may be necessary to extend some guarantees in order to attract financing to the project. The effectiveness of this approach should be weighed against the ways to finance the project and how these alternative funding mechanisms will affect project implementation.

### b. Ancillary Commercial Facilities

The State may allow the development of ancillary commercial facilities within the boundaries of the right-of-way acquired by the State for the transportation project. These facilities, such as gas stations, hotels, restaurants, and office/retail space can provide important revenue sources to supplement toll and fare revenues. Such revenue can significantly enhance the financial feasibility of constructing the facility using private toll road developers. The developer may be given ancillary land by the State as a “social equity” contribution to the project, allowed to lease it from the State for a fixed charge, or allowed to pay the State a percentage of the revenues. In all cases, ancillary development should not be permitted to interfere with the safe and efficient operation of the transportation facility.

Allowing the development of ancillary facilities raises two immediate questions: (1) whether or not the profits (if any) from those facilities should count against any limits on the rate of return investors are allowed to earn; and (2) whether the toll road developer should have the first or exclusive right to build and operate them. As to the first question, some ancillary facilities, such as gas stations and fast-food restaurants, are usually (but not always) no more speculative than investing in the primary transporta-

tion facility, with revenues closely linked to the number of travelers, but they usually contribute only a small portion of total tollway revenues. However, other facilities, such as hotel, retail, and office development are (in their respective order) usually more speculative. Investments in these facilities may be constrained if their earnings rate is limited to that of the toll road.

As for whether the transportation developer should be given first or exclusive ancillary development rights, much depends upon whether or not the project would be financially feasible without profits from the ancillary facilities. Many, if not most, privately financed transportation projects are likely to require the *opportunity* to earn ancillary revenues in order to attract investors to the transportation project. If the State charges market-based rents, then it diminishes this opportunity. Non-exclusivity eliminates it completely. In the California Assembly Bill 680 projects, Caltrans chose to allow use of the right-of-way for ancillary development for 35 years (the term of the franchise agreement) at a nominal fee of one dollar per year, after which the State expects to be paid full market rents. Ancillary revenues were not counted toward the rate-of-return limit.

#### 4. Tort Liability and Safety

Agreements should be made between the State entity and the private sector entity regarding both liability limitations and safety requirements and regulation by the public sector of the privately operated facility.

##### a. Tort Liability

The State may wish to incorporate into the concession agreement or the enabling legislation a limit on the tort liability of the developer/operator to at most the same level as that enjoyed by State-provided projects. Transportation projects are particularly prone to personal injury and product liability lawsuits, but private projects are often held to higher standards of liability than similar State-owned projects. Limiting the liability of infrastructure developers to at most that of the State would greatly improve the ability of the private project to attract investors. Alternatively, the State may determine it is more capable of bearing the tort liability burden, and so, in the interest of making the partnership project more feasible, may seek to take more or all of the burden in the public-private agreement.

In the California private toll road projects, the State will inspect the design and construction of the projects and take legal title to them before they are open to the public. This approach was taken in part to eliminate or minimize the tort liability exposure of the private developer/operator.

##### b. Public Safety

The State may be interested in allowing the private operator to contract with public law enforcement units to provide security for the private transportation facilities. Law enforcement on a partnership project can be done by contract private security staff or by existing State law enforcement staff. However, it may be more convenient or publicly preferable for the private firm to contract with the existing police force, particularly for a toll road, where speed and safety law enforcement is usually done by the State highway patrol. Therefore, the enabling legislation may need to address permitting the private operator to contract with local or State police, especially for toll roads. If the police agency is not interested, the private operator should have the option of contracting with other public police units or with private contractors.

#### 5. Other Considerations

Other areas which may be considered in agreements with private sector entities, and which serve to limit the risk of the private sector entity include force majeure guarantees. An important aspect to attracting private capital to toll road projects is to include risk-reducing elements in the agreement, such as a guarantee, or insurance, against financial jeopardy due to circumstances beyond the control of the parties. In the context of infrastructure, "force majeure" is likely to include acts of God and other unforeseen damage to a project and its revenue base which are not the fault of either the State or the developer/operator. Force majeure provisions usually come in one of two forms. First, the schedules for the beginning and completion of construction may simply be set adequately long so that only the most extreme of delays will cause violation of these commitments. Second, in the case of force majeure events, contract schedules can be amended and lengthened to allow time for the developers to make up losses resulting from the unfortunate circumstances. For example, if a major earthquake were to wreck the tollbooths on a privately developed toll road with only a 35-year BOT agreement, the developer/operator might be given a short extension to the agreement to make up

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for downtime and lost revenues.

Arguments against including force majeure guarantees in a toll road contract arise from the public's interest in getting the project completed as quickly as possible. Providing force majeure insurance could be viewed as a disincentive to the private developer's completing work on time. The State may find, however, that allowing the developer/operator to receive an extension of the concession agreement or another adjustment in the agreement for "force majeure" circumstances is sufficiently effective an instrument for attracting private capital that its negative aspects are outweighed.

### **E. Final Steps**

The final implementation steps which must be taken are generally limited to execution of the sale or lease and ongoing oversight.

#### **1. Execute Lease or Sale of Facility to the Private Partner**

The public and private partners must execute a lease or sale agreement that formally grants the private partner the right to improve, operate, and collect tolls on the facility. Terms of ownership or leasing such as duration or structure of operation must be outlined.

#### **2. Oversee Operation, Maintenance, and Toll Collection on the Facility**

The State will have an ongoing responsibility to oversee the private concession in order to ensure that it is in compliance with the public-private agreement. Ongoing State responsibilities include:

- administration of the toll regulatory mechanism to ensure that the private partner is not collecting tolls in excess of the agreed-upon amount;
- review of road conditions and operations to ensure that the private partner is providing an adequate level of service; and
- approval of road expansions and other major capital expenditures on the facilities.

These responsibilities are often delineated in the enabling legislation or in the concession agreement

or in both. Successful implementation of a public-private toll road program requires broad State support and strong initiative on the part of the sponsoring State agency. Execution of the steps listed above combined with the enactment of enabling legislation should assist in such a program being successfully implemented.

## VI. GLOSSARY OF TERMS

Terms which have been used in this document to refer to public-private partnerships, tolling, and legislation are defined below.

### **average annual return on investment**

the average rate of interest and/or earnings paid to project investors for the use of their money in an infrastructure project for all years of a project's life; more specifically, the ratio of the sum of the present values of the annual net revenues divided by the sum of the present values of the capital invested.

If payments to bond holders (interest costs) are not included in expenses and their loans not included in the capital invested, return on investment refers to the return on total employed capital, including debt and equity. If interest costs are included in expenses and loans are included in the capital invested, then return on investment refers to specifically to the return to equity. Returns to equity that are above the basic cost of capital may be characterized as profits.

### **cost-based pricing**

setting user fees according to the costs of providing the service to the individual user or to a particular category of users.

Depending upon the circumstances of a particular infrastructure facility, cost-based pricing can include the following:

- (1) charging all users the same amount regardless of when they use the facility;
- (2) charging users different fees according to what time of day they use the facility (i.e., peak hours versus off-peak hours);
- (3) charging different types of users (e.g., heavy trucks versus passenger cars) according to how much deterioration their usage imposes on the facility.

### **direct tax revenue**

corporate and personal income taxes and property taxes paid by the owners and investors of an infrastructure project that are the result of taxing the income or market value of the infrastructure facility.

### **economic feasibility**

the demonstration of sufficient net public benefits to justify the expenditure of public funds; because not all of the public benefits of a project can be captured by user fees or other revenue-collecting techniques, many projects that may be economically feasible are not financially feasible.

### **financial feasibility**

a demonstrated likelihood that a project will cover all of its costs with user fees and other revenues and offer sufficient rewards to investors to entice them to invest in the project.

### **financial risk**

the risk that the project will not be able to cover its costs from user charges and other revenues, causing financial loss for investors or, in the worst case, project bankruptcy.

### **fully allocated cost**

the cost of providing a service that includes its appropriate share of overhead and other shared expenses.

For example, the *marginal* cost of an hour's worth of bus service may be \$25 for the fuel, oil, and the driver's wages, but the fully allocated hourly cost may be \$50, including the depreciation of the bus, the cost of maintaining the bus for each hour of operation, a share of the cost of supervising the drivers and planning the bus route, and a share of the cost of managing and administering the transit agency. For the most part, the ratio between direct and overhead/shared costs remains relatively constant among transportation operations of different sizes. Therefore, some form of fully allocated costing is usually the appropriate method for calculating the State-provided option in a State-versus-private sector cost comparison.

### **government-developed infrastructure**

infrastructure in which the design, planning, financing, and operation are the responsibility of the State, although the financing may include some form of

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involuntary value capture of private economic activity.

**indirect tax revenue**

taxes collected on the induced economic activity noted above.

**induced economic growth**

the new economic activity (usually measured as the sum of new consumer spending, the increase in capital investment, and the increase in property values) generated by the following:

- (1) direct spending on construction of the project;
- (2) direct and secondary spending by project employees;
- (4) the spending by and at the new firms and businesses locating around the new infrastructure facility; and
- (3) new economic activity attributable to the improved competitive position of the region served by the infrastructure facility.

**infrastructure ground lease**

a contract between the State owner of a parcel of land (the lessor) and a private firm (the lessee) to allow the private firm to develop and operate an infrastructure project on the property; in exchange, the private firm pays the State rent, which can be fixed or vary with project revenues.

**market pricing**

setting user fees based on the users' willingness to pay rather than according to the fully allocated cost of providing the service at that time of day or to that category of users.

**peak-hour/congestion pricing**

charging more to the users of a facility during the hours of greatest demand than during periods of relatively low demand.

Economists generally consider peak-hour pricing to be logical, equitable, and efficient because peak-period users (e.g., rush hour commuters on a toll road) are forced to pay the larger share of the project's cost. In general, an infrastructure facility must be built large enough to

meet peak demands; otherwise a smaller, less expensive facility would be adequate. Therefore, peak-hour users should pay not just their share of the "base" cost (what the smaller facility would cost if the total demand were spread evenly over the day) but also the added cost of having to make the facility larger to accommodate peak-hour demand. Moreover, peak-hour pricing promotes efficient use of the facility because it gives users an economic incentive to shift their trips to less congested hours, other routes, and other modes, including mass transit and car-pools, thus allowing a smaller facility to service the need, which reduces the cost for all users.

**policy risk**

the risk that State agencies or the legislature will impede a private infrastructure project by changing (or failing to change) policies, rules, and regulations that affect the cost and revenues of the project and thus its viability.

**private infrastructure franchise**

a privilege or right granted by the State to develop, finance, operate, maintain, and collect revenues from a public-use infrastructure facility.

**privately developed infrastructure**

infrastructure in which the private firm designs, plans, finances, and operates a facility with limited financial participation (if any) by the State .

**privatization**

one of the following:

- (1) the private development and operation of public-use infrastructure and the provision of public services that have traditionally been provided by State;
- (2) contracting out of services, which does not usually include private sharing of financial responsibility;
- (3) the sale of State-owned enterprises to private firms, with the expectation that the buyer will improve operating efficiency, invest new capital, and take full advantage of the enterprise's commercial development potential, all at lower cost to the State.



**project performance ratios**

numerical measures of the managerial success of a project in comparison to similar projects, such as cost per unit of output, labor hours per unit of output, management hours as a fraction of total labor hours, etc.

Historic project performance ratios are often used to decide whether an infrastructure project should be developed and operated by the State or by a private firm.

**public-private agreement**

a written contract that specifies the respective responsibilities of the State agencies and private parties involved in a partnership project; the agreement usually includes basic standards for service quality, provisions for monitoring compliance with these standards, provisions for enforcing the terms of the agreement, and provisions for terminating the agreement.

**public-private partnership**

a cooperative venture by State and private firms to provide public-use infrastructure or public services that traditionally have been provided by the State alone. At a minimum, a public-private partnership is characterized by the sharing of financial responsibilities between the public and private parties; public-private partnerships are sometimes referred to as privatization.

**public-private profit-sharing**

the sharing of net revenues (the money left after expenses are paid on the project) by the private developer/operator with the sponsoring State.

**public-use transportation infrastructure**

the physical, structural transportation base for economic activity, including roads, bridges, airports, mass transit, waterways, ports, and railroads systems, most of which has been traditionally provided by State or local governments.

Non-transportation infrastructure that is suitable for public-private partnerships includes sewer systems, wastewater treat-

ment plants, water supply and purification systems, solid and hazardous waste disposal facilities, and State buildings, such as prisons, schools, convention centers, and offices.

**shared ownership**

a situation in which a single infrastructure facility is jointly owned by the State and a private firm under one of several mechanisms:

- (1) a private firm holds title to the entire facility, but the State holds a deeply subordinated lien and a right to share in the profits;
- (2) the facility is divided into State-owned and privately owned portions, even though the whole facility is operated by the private firm;
- (3) the State owns the land upon which a privately developed facility is located, entitling the State to a share of the facility revenues;
- (4) the State holds title to the facility but the private firm is fully or partially responsible for the financial viability of the project.

Note: In most cases, States will not own stock or equity in a private corporation.

**special financing district**

a geographic area drawn around a new infrastructure facility within which new and/or existing commercial properties are assessed special taxes (usually property taxes), annual fees (usually based on square feet of commercial space), or one-time charges to help pay for the infrastructure facility.

**sponsoring State agency**

the State agency, often a State Department of Transportation, that initiates, directs, and/or financially supports a public-private partnership project.

**tax-exempt debt**

unlike the debt of private corporations, the interest payments on tax-exempt debt issued by a State or local entity are deductible from the lender's (bondholders) Federal (and often State and local) taxable income; because the interest is not taxable, rates of interest are usually

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about one-third lower than for corporate rates of similar risk.

**title to the facility**

the coincidence of all of the legal rights required to control or dispose of an infrastructure facility.

**value capture**

the capture, usually through taxing or various types of leasing, of part of the increase in property values, sales activity, or rents that can be attributed to the development of a nearby infrastructure facility to help pay for that facility.

Value capture can be done either by the private infrastructure developer or the sponsoring State. *Privately implemented value capture* usually requires that the infrastructure developer own (or hold the development rights to) the developable land around facility. *State implemented value capture* usually requires the creation of a special financing or tax district that encompasses the developable land around the facility.

## VII. SUMMARY OF STATE PUBLIC-PRIVATE HIGHWAY LEGISLATION

### Arizona

#### Arizona Legislature House Bill 2224: An Act Relating to Transportation Project Privatization, enacted in June 1991

This Act of the Arizona legislature provides the framework under which the Arizona Department of Transportation (ADOT) can enter into agreements with private entities for the construction of transportation facilities by private entities, for the lease of transportation facilities constructed by the ADOT to private entities, and for a refund of the State motor fuel and weight-distance taxes to motor vehicles operating on a transportation facility or toll road built in Arizona.

The Act is divided into two articles. Article 1 is modeled after the California legislation AB 680, and Article 2 is modeled after the Virginia legislation.

Article 1 allows the ADOT to request proposals and to enter into written agreements with private entities relating to construction of up to two pilot projects. An agreement between ADOT and a private entity will provide for the following:

- State ownership of the facility;
- lease of the facility to the private entity for a period mutually agreeable to ADOT and the private entity;
- reversion of the facility to the State after expiration of the lease at no expense to the State;
- reimbursement to the State for the cost of its services provided after signing of an agreement; and
- authorization for the private entity to collect tolls during the term of the lease to cover costs and provide a reasonable rate of return on its investment.

This Article also provides that the facilities must conform to State standards. It provides recourse to the State in the case of default in the private entities'

performance or contractual obligations. It provides that a reasonable alternative route must remain available after a new toll facility is in operation. And, when the facility is turned over to the State, ADOT will be allowed to continue to charge tolls for the use of the facility.

Article 2 of this Act allows a private incorporated person or entity to apply to the Transportation Board (Board) for written authority to construct, operate, or enlarge a roadway. Up to two pilot projects are allowed. The Board is required to ensure that the following conditions are met by the operator:

- the roadways meet State standards;
- a periodic review and inspection process is maintained with ADOT;
- all services provided by ADOT are reimbursed;
- private entity may not exercise eminent domain;
- a schedule of toll rates to be provided to the Board at all times, along with a certification that the rates apply uniformly to all users;
- financing details are disclosed to the Board; and
- recourse for the State is provided in case of private entity default.

Public liability insurance is maintained by the private entity in an amount and form satisfactory to the Board, and the State maintains its right to immunity or affirmative defense.

The private entity is required to contract with the State and local authorities for law enforcement. An improvement fund from a portion of toll revenues will be set up for State and local facilities affected by the toll road, and appropriate jurisdiction approval is required when interconnections with other roadways are involved. Finally, the Article provides that a reasonable alternative route must remain available after a new toll facility is provided.

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## California

### **Assembly Bill Number 680: An Act Relating to Transportation Facilities, enacted in July 1989**

Under previous legislation, the Department of Transportation (Caltrans) is generally responsible for the design, construction, and operation of State-owned transportation facilities.

This bill authorizes Caltrans to:

- enter into agreements with private entities for the construction by, and lease to, private entities of four transportation projects, including at least one in northern California and one in southern California;
- lease rights-of-way in, and airspace over and under, State highways;
- grant necessary easements; and
- issue permits and other authorizations to enable private entities to construct transportation facilities, and to lease those facilities to the private entities for up to 35 years.

The bill authorizes those agreements to contain provisions authorizing the private entities to charge tolls for the use of the facility and would require the agreements to provide for reversion of the facilities to the State at the expiration of the lease. The plans and specifications for each project constructed pursuant to this legislation shall comply with the Caltrans' standards for State projects.

## Florida

### **Florida Bill Number HB 175: An Act Relating to Private Transportation Facilities, enacted in 1991**

Prior Florida legislation did not allow private corporations to build toll roads. This bill authorizes private entities to construct and operate toll roads subject to the following:

- The department may receive or solicit proposals and, with legislative approval by a separate bill for each facility, enter into agreements with private entities, or consortia thereof, for the construction and operation of privately owned

and financed transportation facilities. Prior to seeking legislative approval, the Florida Department of Transportation (FDOT) must first determine that the proposed project:

- (a) is in the public's best interest;
- (b) would not require State funds to be used unless there is an overriding State interest; and
- (c) would have adequate safeguards in place to ensure that no additional costs or service disruptions would be realized by the traveling public and citizens of the State in the event of default or cancellation of the agreement by FDOT. FDOT shall ensure that all reasonable costs to the State and substantially affected local governments and utilities, related to the private transportation facility, are borne by the private entity.

- The agreement may allow the private entity to impose tolls or fares for the use of the facility, but the amount and use of toll or fare revenues may be regulated by FDOT to avoid unreasonable costs to users of the facility.
- Each private transportation facility constructed under this legislation shall comply with all requirements of Federal, State, and local laws; State, regional, and local comprehensive plans; FDOT rules, policies, procedures, and standards for transportation facilities; and any other conditions which FDOT determines to be in the public's best interest.
- FDOT may exercise any power possessed by it, including eminent domain, with respect to the development and construction of State transportation projects to facilitate the development and construction of transportation projects under this legislation. FDOT may provide services to the private entity. Agreements for maintenance, law enforcement, and other services entered into under this legislation shall provide for full reimbursement for services rendered.
- Except as provided, the provisions of the law are not intended to amend existing laws by granting additional powers to, or further restricting, local governmental entities from regulating and entering into cooperative arrangements with the private sector for the planning, construction, and operation of transportation facilities.
- FDOT is prohibited from receiving or soliciting proposals for private transportation facilities.

ties until all rules necessary to implement the provisions of the law are adopted. Such rules shall be published in the Florida Administrative Weekly no later than January 1, 1992.

## Minnesota

### Minnesota Legislation 1184: An Act Relating to Transportation, enacted May 1993

This act authorizes State road authorities to develop, finance, design, construct, improve, rehabilitate, own, and operate toll facilities, and to enter into agreements with private operators for the construction, maintenance, and operation of toll facilities. The Act passed the Minnesota legislature and was signed by the Governor on May 14, 1993.

State road authorities may solicit or accept proposals from, and enter into development agreements with, private operators for developing, financing, designing, constructing, improving, rehabilitating, owning, and operating toll facilities within the road authority's jurisdiction. If the road authority solicits proposals, it must publish a notice of solicitation in the State Register.

The Minnesota Highway Commissioner must approve a development agreement between a road authority and private operator before the agreement may be finalized. In metropolitan areas, additional approvals are required, and governing bodies of a county or municipality through which a facility passes may veto the project within 30 days of approval by the commissioner.

A development agreement for a toll facility may provide for:

- any mode of ownership or operation approved by the road authority, including ownership by the private operator (with or without reversion of title), operation of the facility under leases or management contracts, toll concessions, and BOT or BTO facilities;
- private operator permission to assemble funds from any available source and to incorporate existing roads, highway bridge and approach structures, and related improvements;
- grants of title, easements, rights-of-way, and leasehold estates necessary to the toll facility;
- private operator authorization to charge variable rate tolls based on time of day, vehicle characteristics, and other factors approved by the road authority;
- maintenance, snow removal, and police standards that exceed the standards of the road authority for facilities of the same functional classification; and
- road authority authorization for the private operator to exercise powers available to the road authority for similar facilities.

A private operator may acquire right-of-way by donation, lease, or purchase, and a road authority may acquire right-of-way by eminent domain and may donate, sell, or lease right-of-way to a private operator.

A development agreement that requires transfer or reversion of a toll facility to a road authority must provide the terms and conditions of the transfer or reversion. Under these terms, the facility shall meet at least the maintenance standards of the road authority for facilities of the same functional class during the term of the agreement.

A development agreement must include the following provisions:

- the toll facility must meet the road authority's standards of design and construction for roads and bridges of the same functional class;
- the commissioner must review and approve the location and design of a bridge over navigable waters as if the bridge were constructed by a road authority (this requirement does not diminish the private operator's responsibility for bridge safety);
- the private operator shall manage and operate the toll facility in cooperation with the road authority and subject to the development agreement;
- the toll facility is subject to regular inspections by the road authority and the Commissioner;
- the agreement must provide the terms and conditions of maintenance, snow removal, and police service to the facility, meeting at least the road authority's service standards for roads of the same functional class, and the road authority must provide the services;
- the agreement must establish a reasonable rate of return on investment and capital during the term of the agreement.

Toll revenues must be applied to repayment of indebtedness incurred for the toll facility; payments to a road authority under the development agreement or a related lease, management, or toll concession agreement; costs of operation necessary to meet applicable standards of the road authority; and reasonable reserves for future capital outlays. This is not to be construed as priority order for use of the revenue.

Residual toll revenues after the payments specified above belong to the private operator.

After expiration of a lease for a BTO facility or after title has reverted for a BOT facility, the road authority may continue to charge tolls for the facility.

The balance of this legislation describes Minnesota's provisions for public toll facilities.

## Missouri

### **Missouri Senate Bills 479 and 649: Legislation entitled The Missouri Transportation Corporation Act and the Missouri Transportation Development District Act, enacted in 1990**

Sections 10 through 34 of the Missouri Senate Bill 479 (&649) may be cited as the "Missouri Transportation Corporation Act."

A group of citizens may file with the Missouri Highways and Transportation Commission (Commission) a written application, requesting the Commission to authorize the creation of a transportation corporation to develop a facility within a designated area of the State. The application must include preliminary plans and specifications, and a proposed plan for financing the project.

The Commission has the following rights and duties:

- shall give notice to all local jurisdictions that the Commission is considering authorizing a project within their boundaries, and shall order local public hearings on the project;
- after the hearings, the Commission shall consider the matter of authorizing the corporation to develop the project at a regular Commission hearing. The Commission shall designate the

area of the State in which the corporation may act, and is not prohibited from allowing more than one corporation to act in that area. The Commission is authorized to adopt reasonable administrative rules regarding transportation corporations; and

- to condemn land for the corporation in the name of the State. State and Federal laws on relocation assistance and real property acquisition must be followed.

The corporation has the following rights and duties:

- subject to Commission approval, establish fees for services provided by the corporation; charge and collect tolls to pay for project costs; purchase land or receive contributions of land and cash for project right-of-way; limit and control access from adjacent property to a corporation project; and sell and convey excess right-of-way for its fair market value;
- contract and incur liabilities appropriate to accomplish its purposes. It may issue bonds, notes, or other obligations. The corporation may contract with the Commission to assist it in issuing corporate revenue bonds. These bonds, however, will be the solely the responsibility of the corporation, and shall not constitute debt or liability of the State of Missouri or any agency or political subdivision of the state;
- contract with the Commission to provide assistance in project funding, promotion, design, right-of-way acquisition, relocation assistance services, construction, maintenance, and operation. The Commission may charge the corporation a reasonable fee, not exceeding the actual cost of providing the service; and
- if a corporation is dissolved or liquidated, and after all of its outstanding debts have been paid in full, all other income or assets of the corporation shall be liquidated and deposited in the State road fund and shall become the property of the Commission.

Sections 35 through 65 of the Act shall be known as the "Missouri Transportation Development District Act."

Transportation districts may be created to fund, promote, plan, design, construct, improve, maintain, and operate one or more projects, and to assist in such activities. The districts would be considered subdivisions of the State. At least 50 voters from each county within the proposed district, or any

local transportation authority, must petition for the creation of the district. The district will be contiguous and must cover all territory to be served by, and to adequately fund, each proposed project.

After public approval of the district by election, a district board of directors shall be elected. Before construction or funding of any project, the district shall submit to the Commission proposed plans and specifications of the project for the Commission's prior approval. If the Commission finds the project a necessary or desirable extension of the State highway system, the Commission may approve the project subject to the district making any revisions in the plans required by the Commission.

The Commission and local transportation authorities may contract with a district to provide assistance in project funding, promotion, planning, design, right-of-way acquisition, relocation assistance services, and construction maintenance and operation. The Commission or local transportation authorities may charge a reasonable fee not exceeding the actual cost of providing the service.

To construct a toll facility, a district may relocate an existing state highway subject to approval by the Commission or an existing public street or road subject to approval by the local transportation authority having control and jurisdiction over the street or road.

Any transportation development district may impose a property tax in an amount not to exceed the annual rate of 10 cents on \$100 assessed valuation, if approved by four-sevenths of those voting on the question in the district. Any district may, by resolution or by simple majority in an election, impose a transportation district sales tax, not to exceed one-half of one percent, on all retail sales made in the district.

All revenues collected shall be deposited in a special trust fund and shall be used only for the designated transportation development purpose. The sales tax may not be repealed or amended without approval of the voters in the transportation development district. If approved by a majority of those voting on the question in the district, the district may charge and collect tolls or fees for the use of a project.

## North Carolina

### **S.B. 401, an Act to Authorize the Department of Transportation to Participate in Engineering and Construction Contracts With Private Developers for Proposed Highways, enacted August 1987**

This legislation authorizes the North Carolina Department of Transportation (NCDOT) to participate in private engineering and construction contracts for State highways. In order to qualify for State participation:

- the project must be the construction of a street or highway on the Transportation Improvement Plan adopted by the NCDOT; or
- the construction of a street or highway on a mutually adopted thoroughfare plan that is designated a NCDOT responsibility.

The NCDOT participation shall be limited to 50 percent of the amount of any engineering contract and/or any construction contract let by the developer for the project and be limited to costs associated with normal practices of the NCDOT. The developer must furnish right-of-way without cost to the NCDOT.

Plans for the project and construction practices must meet NCDOT standards and specifications, and must be approved by the NCDOT. The NCDOT shall report, quarterly, to the Joint Legislative Commission on Governmental Operations on all agreements entered into between a private developer and the NCDOT under this section.

## Puerto Rico

### **Legislation to Add Articles to Puerto Rico Law to Regulate Contracts Entered Into by the Highway Authority or the Department of Transportation and Public Works, enacted in August 1990**

Puerto Rico legislation allows contracting with private entities to construct, operate, and maintain bridges, highways, avenues, and expressways, as well as contracts to finance and to issue bonds. The Authority or the Department of Transportation and Public Works shall be the contracting authority for the Commonwealth. These contracts shall be subject to the following conditions:

- the facility shall be in the public domain, and all easements shall be in the public domain;
- the right-of-way shall be acquired by the Commonwealth; however, the private entity may exercise acquisition actions as agent for the Commonwealth;
- the private entity shall give bond guaranteeing compliance with all obligations under the contract; the amount of the bond shall be determined by the Authority;
- the private entity shall indemnify the Authority or Department and cover itself and the public authorities with an insurance policy;
- the term of the contract shall be no more than 50 years and, upon expiration, the government shall take over the facility at no cost to it, and begin administration, operation, and maintenance of the facility.

The public interest shall be represented by the Secretary of Transportation and Public Works, who shall have the following duties:

- assure that the private entity fulfills its contractual duties; and
- submit an annual report to the Governor of Puerto Rico and to the Legislative Assembly about the project.

An Adjudication Board shall be created, and it shall award the contracts to the private entities, ratify the contracts, assure compliance with regulations and procedures, report to the Governor and Legislative Assembly on bids and contracts, and certify compliance with laws and by-laws on these contracts.

## Texas

### **Section 17 of the HB 749 of the 1991 Regular Session of the Texas Legislature Amended Existing Acts (Chapter 410, Acts of the 53rd Legislature, Regular Session, 1953) to Add Section 20a, entitled Private Participation in Projects, effective as of September 1991**

The Texas Highway Authority may enter into agreements with private entities, including toll road corporations, to permit them (independently or jointly with the Authority) to construct, to maintain, to repair, and to operate turnpike projects. The Authority may authorize the investment of private funds,

including debt and equity participation, as a means for financing all or any of the above functions.

In executing these projects, the Authority may utilize exclusive development agreements with private entities in which the Authority shall have broad latitude to negotiate the terms and conditions for the methods and types of financing and in which it may combine and negotiate any or all professional and consulting services, construction, maintenance, and operation of such turnpike projects.

The Authority shall allow franchises, leases, licenses, permits, and other enabling devices to sanction private entity development and operation of a facility. At the time the facility is turned over to the State, it shall be in proper condition at no cost to the Authority.

The Authority, State, and the State's political subdivisions shall not be liable for the financial obligations of the turnpike project. The Authority shall not incur any obligations for the project.

The Authority will establish the rules, procedures, and guidelines which will govern the negotiations. The intent of the rules is to promote fairness, cooperation, and confidence of the participants.

## Virginia

### **Virginia Acts of Assembly: An Act to Amend the Code of Virginia (Passed in April 1991) Relating to the Virginia Highway Corporation Act of 1988 (Passed in April 1988)**

The General Assembly of the Commonwealth of Virginia finds that there is a compelling public need for rapid construction of safe and efficient highways for the purpose of travel within the State, and that it is in the public interest to encourage construction of additional safe, convenient, and economic highway facilities by private parties if adequate safeguards are provided against default in the construction and operation obligations of the roadway operators.

A Certificate of Authority (Certificate) from the State Corporation Commission (Commission) is required before any roadway is constructed, improved, or operated. Application for a Certificate shall contain the following material:



- A survey of the route and the area to be served by the roadway;
- a list of the property owners through whose property the roadway will pass;
- the method by which the operator will secure the right-of-way;
- an analysis that shows that the route conforms to local comprehensive plans for the areas affected;
- the operators plan for financing the proposed roadway, amounts to be collected from users, and projected traffic levels; and
- a certificate from the operator that the roadway will be designed and constructed to Virginia Highway Department (Department) standards.

Once a corporation residing in Virginia has the Certificate, and is organized to conduct a public service business (other than a railroad), it has the power to:

- survey and examine proposed locations for its project;
- classify traffic according to reasonable categories for assessment of tolls;
- construct and maintain the roadway; and
- make and enforce regulations, with the consent of the Department, including:
  - 1) determination of maximum and minimum speeds;
  - 2) exclusion of undesirable vehicles or cargoes from use of the roadway; and
  - 3) establishment of commuter lanes for use during all or any part of the day and to limit the use of such lanes to certain traffic.

The Commission has the power to:

- review, approve, or deny the application of the operator;
- supervise and control the operator in performance of operator duties;
- collect information from the operator on the nature of contractual and other relationships with entities providing significant financial, construction, or maintenance services;
- review the information and disallow any amounts found improper or excessive; and
- approve or revise toll rates.

If approval of the project, project design, and connections of the roadway is granted by the Commonwealth Transportation Board (Board), the Department shall enter into an agreement with the

applicant which provides that the Department will:

- review and approve plans and specifications for the roadway;
- inspect and approve construction of the roadway to see that it conforms to the plans and specifications, and to State construction and engineering standards;
- monitor the maintenance practices of the operator; and
- be reimbursed for direct costs of its services.

The operator who constructs, operates, or enlarges a roadway under this legislation shall secure and maintain an insurance policy of public liability, and tort liability, to the public and employees, sufficient in form and amount to satisfy the Commission, and to enable the continued operation of the roadway.

In the event of material and continuing default in the performance of the operator's construction or operation duties, or failure of the operator to comply with the terms of its agreement with the Department, the Commission, after a hearing in which the applicant or operator has notice and opportunity to participate, may revoke the Certificate of Authority.

## Washington

### **SHB1006, An Act Relating to Public-Private Initiatives in Transportation; Adding a New Chapter to Title 47 RCW, effective July 1993**

In 1992, the Washington State Transportation Commission recommended that the State take a more aggressive role in pursuing public-private partnerships to make capital improvements to the transportation system in the State. A policy subcommittee, tasked with analysis of the issue, recommended that the legislature establish a framework to implement public-private initiatives and suggested key elements of the program. This proposal was presented in Statewide public forums, approved by the Transportation Commission, and reported to the legislature in 1993.

Key elements of Substitute House Bill (SHB) 1006, authorizing public-private partnerships include:

- Legislative intent to enhance the State's ability to provide for transportation services and pro-

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grams by allowing private entities to plan, design, develop, finance, acquire, install, construct, improve, operate, and maintain capital-related transportation systems and facility projects. Such projects may include highways, roads, bridges, vehicles and equipment, marine-related facilities, park-and-ride lots, transit stations and equipment, transportation management systems, and other transportation-related capital improvements.

- Washington State Department of Transportation (WSDOT) is authorized to solicit proposals and select up to six projects. Each proposal will be evaluated on its own merits and each agreement negotiated individually.
- The Transportation Commission approves the projects.
- Affected jurisdictions must be involved and consulted.
- All projects are required to be consistent with plans, rules, regulations, and statutes governing State transportation projects. This includes existing labor and civil rights legislation.
- WSDOT authority may be used to facilitate the successful financing, development, and operation of the program .
- The State will be reimbursed for State-supplied support services including planning, environmental review, design, engineering, and construction management.
- The projects may be owned by the private entity during construction. Once completed, the projects become State-owned and may be leased back to the private entity for up to 50 years unless the State elects, and the private entity agrees, to private ownership during the term of the agreement.
- The imposition of user fees or tolls may be authorized within each agreement to allow a reasonable rate of return on investment.
- A maximum rate of return on investment is established for each project. Incentive rates of return, beyond the specified maximum rate, may also be established to achieve various safety, performance, or transportation demand management goals.
- Revenues from the project must be used to pay the private entity's capital costs, including interest expense, operation, maintenance, administrative costs, reimbursement to the State for the costs of project review and oversight, technical and law enforcement services, and a reasonable rate of return on investment to the private entity.

- The use of excess toll revenues or user fees is negotiated within each agreement.
- In order to maximize the Federal funding opportunities for public-private initiatives, WSDOT is permitted to create a revolving fund for various sources of funds which can be used to make grants or loans to the private entity or used in other innovative financing arrangements.



