“SAFETEA—LU” Promotes Private Investment in Transportation

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On Friday, July 29, 2005 the House and Senate passed the “Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users’’ or ‘‘SAFETEA–LU”. President Bush has announced he will sign it. The Act, which authorizes $286.5 billion in funding for surface transportation projects through FY 2009, also includes long-sought provisions that will enable public funds to be leveraged with billions more in private investment. Public-private partnerships will now have new tools to implement innovative financings for highways and intermodal facilities, including:

- *private activity bonds* for highways in surface freight transfer facilities,
- enhanced authority to use *tolling* to finance construction of interstate highways,
- increased flexibility in using *design-build contracting*,
- *streamlined environmental processes*, including a 180-day statute of limitations on actions contesting federal agency approvals for transportation projects, and
- improvements to innovative finance programs, including *TIFIA and SIBs*.

<u>$15 Billion of Private Activity Bonds (“PABs”) for Highways and Surface Freight Transfer Facilities</u>

New Category of Exempt Facilities. Section 1143 of Title XI of the Act creates a new category of exempt facilities for which private activity bonds may be issued -- “qualified highway or surface freight transfer facilities.” This new category includes:

(1) any surface transportation project receiving Title 23 funds;

(2) a project for an international bridge or tunnel for which an international entity authorized under Federal or State law is responsible and which receives Title 23 funds; and

(3) facilities for the transfer of freight from truck to rail or rail to truck (including any temporary storage facilities directly related to such transfers) which receives Federal assistance under Title 23 or Title 49.

Because private activity bonds are limited to projects that otherwise receive federal assistance, projects using private activity bonds will be subject to requirements such as Davis-Bacon prevailing wage rates, Buy America and Federal-aid procurement requirements. However, the summary of the tax provisions provided by the House Committee on Ways and Means notes that “the provision is not intended to expand the scope of any federal requirement beyond its application under present law and does not broaden the application of any federal requirement under present law in Title 49.”

Cap on PABS. The Act includes a $15 billion cap on PABs, but does not include separate annual limitations. (These bonds are exempt from the state-wide caps that are applicable to many other categories of private activity bonds.) The $15 billion cap does not apply to current refundings of qualified highway and surface freight transfer bonds, if "(A) the average maturity date of the issue of which the refunding bond is a part is not later than the average maturity date of the bonds to be refunded by such issue, (B) the amount of the refunding bond does not exceed the outstanding amount of the refunded bond, and (C) the refunded bond is redeemed not later than 90 days after the date of the issuance of the refunding bond." (Subsection (b)(4) of Section Section 1143).

The Secretary of Transportation has discretion to allocate the $15 billion allotment among qualified highway or surface freight transfer facilities in such manner as the Secretary determines appropriate.

Impact on Public-Private Partnerships. Access to lower-cost bond financing should permit much greater private sector investment and risk taking in highway projects and lower the cost of financing freight intermodal projects. Prior to enactment of these changes, the private sector was generally limited to assisting in the development stage of projects (with its investment reimbursed upon issuance of the bonds), supplying design-build services or providing operations and maintenance services under contracts that comply with rigid IRS management contract rules. It should be noted that a private entity cannot directly issue PABs; a governmental "conduit" bond issuer is still required.

While it is unlikely that PABs could be accessed to finance the acquisition of existing transportation facilities by a private entity, PABs could be used to finance improvements and extensions on facilities leased to private concessionaires.

Tolling of Interstates: Express Lanes and Value Pricing Pilot Programs

Express Lanes Demonstration Program. Section 1604(b) of the Act creates a new "Express Lanes Demonstration Program," limited to 15 projects during FY 2005 through FY 2009. This provision permits tolling of:

- existing tolled facilities;
- existing high occupancy vehicle (HOV) facilities;
- facilities that are "modified or constructed after the date of enactment of this Act to create additional tolled lane capacity (including a facility constructed by a private entity or using private funds)"; and
- in the case of a new lane added to a previously non-tolled facility, only the new lane.

The Express Lanes program does not authorize tolling of existing lanes, other than existing HOV lanes.

The provision contemplates private investment in Express Lanes. Subsection (b)(2) provides that tolls may be collected by "a public or private entities [sic] designated by States." Revenues may be used for (I) debt service; (II) a reasonable return on investment of any private financing; (III) the costs necessary for the proper operation and maintenance of such facilities (including reconstruction and rehabilitation), or (IV) if the operating entity annually certifies that the facility is being adequately operated and maintained, any other purpose relating to a highway or transit project "carried out" under Title 23 or 49.

The Express Lanes provision contains some special requirements. Subsection (b)(5) requires tolls to be collected only through the use of non-cash electronic technology. Variable pricing is required for tolled HOV lanes and optional for other lanes. The Secretary is also directed to adopt a rule specifying standards for automated toll collection systems implemented under this section.

Value Pricing Pilot Program Continued. Section 1604(a) of the Act authorizes funding for the Value Pricing Pilot Program (23 USC §149 (note)) for FY 2005 through FY 2009, continuing the program originally authorized by Section 1216(a) of TEA-21. No substantive changes in existing law were made. Projects submitted for approval under the VPPP must have the potential to reduce congestion, improve system performance and promote mobility through the use of value pricing (i.e. variable priced tolling), including in the commercial freight sector.

The 15 states that have been approved to participate in the VPPP program are: California; Colorado; Florida; Georgia; Illinois; Maryland; Minnesota; New Jersey; North Carolina; Ohio; Oregon; Pennsylvania; Texas; Virginia; and Washington.

Tolling New Interstates: 3-Facility Construction Toll Pilot Program

Section 1604(c) of the Act creates a new pilot program that will permit a State (or an interstate compact of States – see below) to collect tolls on a highway, bridge or tunnel on the Interstate System for the purpose of constructing Interstate highways. This program is limited to three "facilities" on the Interstate System. Eligibility criteria include "an analysis demonstrating that financing the construction of the facility with the collection of tolls under the pilot program is the most efficient and economical way to advance the project." (This language is more liberal than the standard for tolling under the existing interstate reconstruction pilot program discussed below).

***Application Requirements*.** In addition to demonstrating the efficiencies and economies of tolling, applicants must also provide a facility management plan that includes:

(i) a plan for imposing tolls on the facility;

(ii) a schedule and finance plan for construction of the facility using toll revenues;

(iii) a description of the public transportation agency that will be responsible for implementation and administration of the pilot program; and

(iv) a description of whether consideration will be given to privatizing the maintenance and operational aspects of the facility, while retaining legal and administrative control of the facility.

Selection Criteria. The Secretary is responsible for selecting pilot projects based on a determination by the Secretary that:

(A) the State's conclusion as to the efficiency and economy of using tolls to finance the facility is reasonable;

(B) the State plan for implementing tolls takes into account the interests of local, regional, and interstate travelers;

(C) the State plan for using toll revenues to construct the facility is reasonable;

(D) the State will develop, manage, and maintain a system that will automatically collect the tolls; and

(E) the State has given preference to the use of a public toll agency with demonstrated capability to build, operate, and maintain a toll expressway system meeting the criteria for the Interstate System.

Interstate Compacts. This provision permits tolls to be collected by a State or an "interstate compact of States" to collect tolls on a facility. It should be noted that an interstate compact requires approval of the Congress under Article I, Section 10, clause 3 of the United States Constitution.

Electronic Tolling. Exclusive use of electronic tolling is not required under the Interstate Construction Toll Pilot Program.

Private Investment in Toll Facilities. The use of public-private partnerships to advance these pilot projects is clearly contemplated by subsection (6)(a)(ii) of Section Section 1604(c), which permits tolls to be used for, among other things, "reasonable return on investment of any private person financing the project." However, it would be advisable for FHWA to clarify certain other requirements that could be interpreted in a manner in inconsistent with an innovative procurement approach. Specifically, Subsection (c)(1) states that under the pilot program "a State or an interstate compact of States" may collect tolls. FHWA should clarify that this would permit a private entity that finances the facility to collect the tolls under agreement with a State or interstate compact of States. With respect to the preference for the use of a "public toll agency," FHWA should clarify that such a toll agency could contract with private entities for the financing, construction and operation of toll projects.

Non-Compete Provisions. The Express Lanes provisions (discussed above) do not prohibit non-compete covenants. By contrast, the Interstate Construction Toll Pilot Program requires that the State commit not to enter into an agreement with a private person under which "the State is prevented from improving or expanding the capacity of public roads adjacent to the toll facility to address conditions resulting from traffic diverted to such roads from the toll facility, including—(A) excessive congestion; (B) pavement wear; and (C) an increased incidence of traffic accident injuries or fatalities." It is not known whether FHWA would nevertheless preclude non-compete clauses for the Express Lanes program, or whether it would allow use of a "modern" non-compete clause in either program; such a clause does not bar the State from constructing other improvements, but only requires that the State compensate the tollroad owner for declines in revenue resulting from such improvements.

Tolling Existing Interstates: Reconstruction Pilot Program Continued

The Act did not terminate the 3-state pilot program created under Section 1216 of TEA-21 (23 USC 129 (note)). The eligibility language for that program continues to require "an analysis demonstrating that the facility could not be maintained or improved to meet current or future needs from the State's apportionments and allocations made available by this Act (including amendments made by this Act) and from revenues for highways from any other source without toll revenues." TEA-21 authorized the Secretary to conduct the program for a term to be determined by the Secretary, but not less than ten years (i.e. until at least June 6, 2008).

HOV Lanes and Tolls

Section 1121 of the Act concerns use of high occupancy vehicle (HOV) lanes, allowing States to permit single-occupancy vehicles to use HOV lanes subject to payment of a toll (HOT lanes). Automatic toll collection is required. This authority is separate and independent of the Express Lanes pilot program that permits tolling of existing (but not newly created) HOV facilities.

States May Permit Use of HOV Lanes by Hybrids. The Act permits States, at their option, to allow certain low emission vehicles and energy efficient vehicles (hybrids) to use HOV facilities. A State may elect to charge no toll for these vehicles, or to charge a toll that is less than the toll charged to other single-occupancy vehicles. It remains to be seen whether States will be willing to allow toll-free use of HOT lanes by hybrids, given the adverse impact on revenues that would result.

Impact on Operations. Subsection (d) requires the State agency to limit or discontinue use of an HOV facility by single occupancy vehicles if the presence of the vehicles has "degraded" the operation of the facility. Operation of the facility is deemed "degraded" if vehicles operating on the facility are unable to maintain a defined minimum operating speed 90% of the time over a consecutive 180-day period during morning or evening weekday peak hour periods (or both). "Minimum operating speed" is defined as 45 mph on an HOV facility with a speed limit of 50 mph or greater; and not more than 10 mph below the speed limit, in the case of an HOV facility with a speed limit less than 50 mph. This provision may be troublesome to investors in such projects, since they cannot be certain that tolling will continue if use by single occupancy vehicles "degrades" the operating speeds of the HOV facility.

New Rules for Design-Build Contracting

Section 1503 of the Act eliminates the $50 million floor on the size of contracts that can use design-build contracting without special approval.

The Act also eliminates an obstacle contained in FHWA's existing design-build rule, relating to the ability of transportation agencies to take certain preliminary actions prior to receipt of NEPA approval for a project. Specifically, the FHWA rule prohibited agencies from issuing requests for proposals and entering into contracts until after issuance of NEPA approval. This has been a particular problem for public-private partnerships where the expectation is that the private sector partner will be involved in the project definition process. Section 1503 directs the Secretary to revise the regulations applicable to design-build contracts to permit transportation agencies to proceed with certain actions relating to design-build contracts, prior to receipt of final NEPA approval. Specifically, the regulations may not require compliance with section 102 of the National Environmental Policy Act of 1969 prior to any agency: (a) issuing requests for proposals; (b) proceeding with awards of design-build contracts; or (c) issuing notices to proceed with preliminary design work under design -build contracts. The Act directs the Secretary to issue the revised regulations not later than 90 days after the date of enactment of SAFETEA-LU.

Statute of Limitations for Federal Approvals

The Act includes a provision that will reduce a major risk associated with development of transportation projects – namely, the possibility of an action to enjoin the project based on alleged flaws in the NEPA approval process. In the past, project opponents have often waited until construction was underway, when the cost of stopping work is high, before filing an action to contest the validity of environmental approvals. The prospect of such an action presents a risk that impacts the plan of finance for project revenue financed projects, increasing the cost of such projects even if no action is filed.

Under Section 6002 of the Act, any claim seeking judicial review of a permit, license or approval issued by a Federal agency for a highway or public transportation capital project must be filed within 180 days after the approval is published. For many projects, the risk of an injunction will be eliminated entirely as a result of this limitation. For others, the risk of an injunction will remain a concern, since there can be no guaranty that the litigation will be concluded before the scheduled date for start of construction. However, the project owner/developer will be able to take steps to mitigate the effect of an injunction, such as changing its procurement schedule, delaying the start of construction, or phasing construction so as to reduce the potential cost associated with an injunction. The provision is not limited to NEPA — it applies to lawsuits based on other federal approvals as well.

Other Environmental and Planning Changes. The bill provides a streamlined environmental approval process that addresses agency coordination, public involvement, dispute resolution, and comment deadlines. It also establishes a project delivery pilot program for the states of Alaska, Ohio, Oklahoma, Texas and California, under which all USDOT environmental responsibilities under NEPA and Section 4(f) can be delegated to the State DOTs. All States will be eligible to obtain a delegation of environmental responsibilities for categorical exclusions (CEs).

Federal Innovative Finance Programs: TIFIA, SIBs and Highways for Life

TIFIA. TEA-21 authorized the TIFIA program, which provides direct loans, loan guarantees and lines of credit to states, local governments and State Infrastructure Banks to finance surface transportation projects. Under SAFETEA-LU, public-private partnerships and other legal entities undertaking a project can directly apply for TIFIA assistance. The definition of eligible projects has been expanded to include public freight rail facilities or private facilities providing public benefit for highway users; intermodal freight transfer facilities; and access to freight rail or intermodal freight transfer facilities. Second, the eligibility threshold was lowered to $50 million for all but ITS projects. The threshold for ITS projects was lowered to $15 million. TIFIA loans may now be used to refinance long-term project obligations or Federal credit instruments if such refinancing provides additional funding capacity for the completion, enhancement, or expansion of the project.

State Infrastructure Banks. All States and the District of Columbia are now allowed the option to transfer a limited amount of the State's Highway Trust Fund allocations to State infrastructure banks (SIBs). SIB loans can be used to help finance state transportation projects, but they now retain their character as federal funds. Upon repayment, the SIB loans can be re-loaned to support other projects. The amounts that a State may transfer to a SIB is limited generally to 10 percent of its annual highway, transit and rail apportionments under designated sections of titles 23 and 49.

Highways for Life. Projects that use innovative technologies, manufacturing processes, financing, or contracting methods that improve safety, reduce congestion due to construction, and improve quality can qualify for special funding under the new "Highways for Life" program created under Section 1502 of the Act. This program can fund up to 20% of project costs or a maximum of $5 million per project. The program is limited to 15 projects per year between 2005 and 2009.

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