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# With upfront payments, toll operators gamble on more money down the road

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**By THEODORE KIM / The Dallas Morning News**
**tkim@dallasnews.com**

Profit now, pay later. That is the familiar Wall Street mantra behind the push for toll roads that has swept Texas and other states in recent years.

WILLIAM DeSHAZER/DMN
**Crews put finishing touches** on State Highway 121 in Lewisville. The North Texas Tollway Authority paid more than $3 billion for its toll rights last year, hoping to generate $5 billion or more on the road over the next several decades.

Private companies and public agencies have paid billions for the chance to collect your tolls. States have used that cash to build new roads. And road operators hope to cash in on built-in rate hikes and increased traffic over time.

For politicians, the easy money is more palatable than the alternative: raising fuel taxes, the traditional source for transportation funding.

"Everyone wants those big numbers upfront," said toll road expert Jonathan Peters of the College of Staten Island.

The North Texas Tollway Authority agreed on Wednesday to pay the state more than $1 billion for tolls on State Highway 161. Last year, the agency shelled out more than $3 billion for State Highway 121. Private firms have cinched similar agreements and hope for more.

But even as lawmakers and experts agree that toll roads will play a role in helping budget-strapped states keep pace with highway needs, they caution that the strategy is hardly a panacea.

The deals – built on the idea that one road pays for many – are forcing some toll road commuters to pay more than their fair share, some critics say.

"Basically, we're saying, 'We are going to try to make one set of toll road users pay for the roads of everybody else,' " said Jose Gomez-Ibanez, a professor of planning and policy at Harvard University.

The implosion of the credit markets also raises questions about the financing behind the big upfront payments.

At their core, these new deals are a tool to borrow more money than ever before in the road-building business, a potentially hazardous strategy with the global economy in freefall.

Toll road operators are gambling billions that your tolls will lead to long-term profits. But if operators fail to meet aggressive traffic and revenue goals, experts say, the bubble could burst, leading to a landscape of bankrupt highways.

In addition, because these deals are so highly dependent upon debt, the highways face a far greater risk of financial failure than traditional toll roads.

Supporters assert that payouts fulfill one of America's biggest looming challenges: closing an estimated $2 trillion shortfall to build new and better roads, from California to the Carolinas.

"You're never going to solve it jacking up gas taxes and borrowing a bunch of money," contended Indiana Gov. Mitch Daniels, who helped pioneer the approach in America.

Instant cash infusion

No one knows exactly how much state and federal fuel taxes would have to increase to generate enough cash for all the new roads Texas needs.

Fuel levies generated $3 billion in state revenue last year, but transportation officials say they need much more.

The toll road concept is hardly new. But only recently have states begun leveraging tolls to drum up cash payments far beyond the cost of the road itself.

Experts say such payouts are a modified version of an approach used in Europe and elsewhere since at least the 1970s.

Private firms agree to build and maintain several roads in exchange for toll collections on the most lucrative road of the bunch, a strategy supported by Gov. Rick Perry's and President Bush's administrations.

In some cases, the public and private sectors share toll profits. Other times, private firms agree to give an upfront payout and a share of profits.

Two overseas firms working together, Cintra of Spain and Macquarie of Australia, started the trend in the U.S. when they took over two existing highways: the Chicago Skyway in 2005 and the Indiana Toll Road in 2006. The deals combined generated more than $5.6 billion for Indiana and Illinois.

Using that private model as a guide, the North Texas Tollway Authority won the right last year to collect tolls on Highway 121 for the next half-century. In exchange, the agency paid the region more than $3 billion.

For states, the instant cash is a godsend as transportation to-do lists are long and construction costs are rising. Critics say politicians also reap the benefits of the upfront payment while avoiding the fallout of toll increases in the distant future.

"You're seeing people mortgage the future in return for instant cash today," said Jere Thompson, a former NTTA chairman and privatization critic.

Deals' appeal for states

Private deals are particularly enticing to states because outside firms can inject their own money into the equation, absorb some of the risk and, in most cases, outbid the public sector.

Wall Street experts say states such as Texas can generally get some of the lowest interest rates on their debt. But privatization supporters say that firms such as Cintra have the ability to take out bigger, and often riskier, loans than the government.

The Bush administration also has opened up public financing tools such as low-interest loans to the private sector, a move that negates the advantages of government borrowing.

For road operators, both public and private, the chief reward is years of toll collections.

"These transactions can be boiled down to: 'I'll give you money today and you will pay it back over time,' " said Tom Paolicelli, a senior analyst at Moody's Investor Service.

Private firms are tight-lipped about how profitable they think these roads are. But experts assume the returns are high.

The Indiana Toll Road, for instance, generates about $160 million a year in revenue, a total that will only grow as traffic and toll rates go up. The NTTA expects to generate perhaps $5 billion or more on Highway 121 over the next several decades.

In the last few years alone, NTTA and private operators collectively have paid or promised more than $21 billion, on the hunch that U.S. toll roads will develop into long-term cash cows.

Down the road

Yet behind all of these toll road agreements, both public and private, is billions upon billions in debt.

Cintra and Macquarie put up $1.6 billion upfront in Illinois and Indiana, records show. The companies also took out $4 billion in debt. NTTA financed its payment for Highway 121 entirely with loans.

Nearly all large-scale public projects, from roads and airports to the new Dallas Cowboys stadium, are financed with debt.

But in recent toll road deals, operators are borrowing more than road projects cost to build, then making up the difference by charging higher tolls.

While states are using the extra money to build other roads, experts say the added debt puts much more pressure on the roads to turn a profit.

Also at issue is the nature of the debt. Cintra and Macquarie have deferred much of their toll road debt over the next two decades, federal records show. The goal is to glean profits now and delay payments to a time when the roads' toll rates and traffic counts are higher.

"They are kicking the can down the road," Mr. Paolicelli said.

The trade-off is higher borrowing costs and greater risk: Cintra and Macquarie, in part, use balloon-style loans that get dramatically more expensive over time.

That debt appears even more vulnerable now. The unstable economy has made lenders think twice about issuing risky debt to any company, even to those with seemingly stalwart finances. Should their lenders pull back, road operators could be in trouble.

Unlike private companies, the NTTA does not have shareholders to satisfy, but it faces many of the same financing hurdles.

The agency borrowed against several roads, including the Dallas North Tollway and the Bush Turnpike, to generate the massive upfront payment for Highway 121. The agency will need to borrow even more against those revenues in the future.

Bond agencies lowered the NTTA's debt rating last year, concluding that the authority had stretched itself too thin. The NTTA's rating, which sets its borrowing costs, remains at investment grade.

NTTA chairman Paul Wageman said his agency remains on sound footing. His competitors disagree.

Jose Maria Lopez de Fuentes, Cintra's U.S. director, pointed out that the NTTA relies on a handful of local highways for revenues.

Cintra, by contrast, maintains highways and other assets worth tens of billions of dollars worldwide. The diversification, he argued, allows Cintra to absorb more debt and withstand economic downturns.

"The infrastructure is safer with us than with the public sector," he said.

Toll hikes add up

Toll roads have failed before on a smaller scale. But no one knows what might happen if one of these billion-dollar road deals went bust.

Should Cintra and Macquarie fold their operations in the Midwest, the consortium would be forced to return the Chicago Skyway and Indiana Toll Road to the public. Illinois and Indiana also would keep the upfront payments.

The setup looks good on paper, but such a handover could end up in bankruptcy court, where a judge could require that the state pay back bondholders for the upfront payment.

Less certain is what might happen if a public agency such as NTTA became insolvent – an extreme case. Scenarios range from a state takeover of both the road and the agency to bondholders demanding a toll increase.

Succeed or fail, experts say, motorists and/or taxpayers are likely to hold the bill.

In the case of Highway 121, toll rates are certain to put pressure on drivers' wallets down the road.

While the agreements regulate the amount that tolls can go up each year, the increases add up.

For instance, Highway 121 motorists driving between McKinney and Coppell will eventually pay $14 in tolls, or nearly 60 cents a mile. Motorists will not start feeling that pain for several decades.

For policymakers, balancing those downsides with the prospect of billions in new road projects has proven difficult.

The Highway 121 deal, for instance, will pay for a collection of projects planned for years that might not otherwise get built, said Michael Morris, director of the Regional Transportation Council.

All sides predict that drivers will one day revolt if the number of toll roads continues to proliferate. That has prompted policymakers to consider alternatives such as pegging fuel taxes to inflation or even tapping public pension funds.

"For some projects, the only way to get this done is a toll road," said James M. Bass, finance director for the Texas Department of Transportation. "But you can only do that so many times."