

The Public-Private Indiana Toll Road Is in Trouble

The problems facing the nation's largest public-private road venture show how difficult it can be to apply business principles to sprawling public projects

By Carol Wolf



Amount the Indiana Toll Road came up short in 2010 Frank Polich/Bloomberg

Eleven million trucks. That's how many 18-wheelers needed to rumble across northern Indiana in 2010 for the state's 157-mile toll road to break even. Unfortunately, only about half that many did and the road came up \$209 million short. This sounds like the beginning of yet another story about recession-ravaged states bleeding cash. And it is, sort of. The twist is that the Indiana Toll Road is managed not by the state but by a group of corporate investors, part of a public-private partnership experiment intended to show how businesses can help government run more efficiently and save taxpayers money—all while turning a profit.

President Barack Obama and politicians from both parties have held up such private sector alliances as a model for the future, as cities and states find it increasingly difficult to shoulder the enormous cost of building and maintaining roads and bridges. California, Illinois, Michigan, Kentucky, and Georgia are all courting investors, hoping to strike deals in which corporations will assume some of the expense and risk in exchange for a share in the profits. This moneyloser in Indiana shows how difficult it can be to apply business principles to sprawling public projects.

Now five years old, the Indiana deal has yet to turn a profit, or break even. Two overseas companies—Cintra Concesiones de Infraestructuras de Transporte, a unit of Madrid-based Ferrovial, and Macquarie Infrastructure Partners, an investment fund managed by

Macquarie Group (MOG) of Sydney, won the right to run the road with a daring \$3.8 billion bid—\$1 billion more than the next-highest offer. The companies each owned a 50 percent stake of the project, which was backed by several overseas banks. The group then attracted other investors who bought pieces of the deal.

It turned out to be a bargain for the taxpayers of Indiana. The state received the upfront payment and has avoided more than \$100 million a year in operating costs. “The state got a great deal,” says Jane Jankowski, a spokeswoman for Indiana Republican Governor Mitch Daniels. “The lease agreement contains numerous protections for the taxpayer and travelers and ensures the continued successful operation of the road.”

The private investors haven’t made out so well. Had the road been profitable, they stood to make millions per year over the life of the 75-year project. As it is, they have not been able to get past the debt they incurred winning the bid. They have met their annual debt payments only by borrowing money and may default before loans mature in 2015, according to disclosure documents from Macquarie Atlas Roads, one of the investors. The project’s 2010 prospectus said that revenue from the highway is “expected to remain insufficient to cover debt service obligations over the medium term.” The document cautions that “any default under the loan documents may lead to lender actions which may include foreclosure of the project assets or bankruptcy.” Even Governor Daniels, who had enthusiastically backed the venture, recently said that the foreign investors had overpaid.

In an e-mail, Macquarie spokeswoman Paula Chirhart said the prospectus was prepared in 2009 during the global financial crisis and “was never stated as a forecast or an expectation.” She added that “we expect the Indiana Toll Road to continue to meet its debt service payments as they fall due.” Patrick Rhode, a Cintra spokesman, said in an e-mail that more vehicles are using the Indiana road as the economy recovers. A reserve account was created to cover financial gaps that occur over long periods of time, he said. “We do not expect a default.”

Even so, the poor results could dampen enthusiasm for similar projects elsewhere. In Ohio, which faces a budget shortfall of as much as \$8 billion over two years, lawmakers are considering a bill that would give Republican Governor John Kasich the authority to seek a sale or lease of the Ohio Turnpike. Kasich has optimistically suggested the road might be worth \$3 billion. Given the way things are going next door, he may have a hard time finding takers willing to plunk down that kind of cash.

Is the Indiana Toll Road Operator in Danger of Default?

By [Matt Dellinger](#) | July 29, 2011 – 3:42 pm

(Matt Dellinger – Transportation Nation) For the last month, while national news coverage has focused on the federal debt ceiling and the threat of a historic default, transportation watchers have been nervously contemplating the possible failure of the largest toll road privatization from the last decade.



Indiana Toll Road Concession Company, a 50/50 consortium made up of the Spanish operator Cintra and the Australian bank Macquarie, paid \$3.8 billion dollars in 2006 for a 75-year lease of the Indiana Toll Road. The bid, made at the height of the economy and in the first blush of real PPP highway investment in America, exceeded that of the nearest competitor by a billion dollars. In what seemed like significant serendipity, the money changed hands on the 50th anniversary of the signing of the Federal-Aid Highway Act of 1956, which initiated construction of the Interstate highway system. The sum was so large that it had to be sent in several wire transfers.

At the time, critics of the plan complained that the lease of a public asset for profit amounted to a corporate giveaway. But proponents lectured that the road would never be worth that amount in public hands, and pointed out that any potential for gain came along with some significant risks.

The 2008 banking crisis and resulting recession have proven them right. A month ago, on the five-year anniversary of the lease, [Debtwire](#), a subscription-only wire service operated by London Financial Times, estimated that the Indiana Toll Road Concession Company was in danger of defaulting on its debt as soon as early next year. With the economy in a slump, traffic and revenues were well below the company's projections.

Mitch Daniels, the Governor of Indiana, who spent significant political capital to ink the deal, gloated to the Associated Press. "They overpaid," he said. "That's why you hold an auction. Sometimes you hit the jackpot."

Michael Lindenberger, the transportation reporter for the Dallas Morning News, immediately picked up on the report and Bloomberg Businessweek soon followed. For some, the mere specter of default was cause enough for worry. National and state leaders from across the political spectrum have championed public-private partnerships as a way to help us "do more with less." A major default could make such deals seem riskier, and might mitigate the excitement among banks to invest.

Aware of these reports, Cintra US put out a press release earlier this week, in which Patrick Rhode, vice president of corporate affairs, insisted that the concessionaire was on solid financial footing. "The Indiana Toll Road project is fulfilling all of its financial obligations and payments, and will continue to do so," he said. "In public private partnerships, the underlying financial condition of the investor is key, and in our case extremely robust, with net cash position at our parent company level [Ferrovial] and available capacity to invest of over \$1.5 billion."

Cintra's business, it should be noted, is built on patient investment: The lease term is more than double that of a thirty-year mortgage, and allows for many economic ups and downs. But is turbulence for Cintra enough to limit the investment appetite of other banks? We'll be watching this story, and will have more thoughts shortly on what default would look like — and what it might mean

Statement of Cintra US regarding Indiana Toll Road and other PPP projects

The following statement may be attributed to Patrick Rhode, vice president of corporate affairs for Texas-based Cintra US:

Source: Cintra US

Publication date: 2011-07-26

"There have been questions posed recently about the Indiana Toll Road (ITR) - a project in which we are proud to invest, operate and maintain. We hope that this note will clarify any confusion among community members and our stakeholders relative to the financial model we use and our ability to make payments and meet our project-related debt obligations.

"First, the Indiana Toll Road (ITR) project is fulfilling all of its financial obligations and payments, and will continue to do so. All of our projects have a financial structure that, characteristic of public private partnership (PPP) projects, guarantees their solvency.

"ITR and other Cintra projects are financed using an innovative model originally developed in Europe - PPPs - to assist governments in financing much needed infrastructure projects that would otherwise not be possible. It is important to understand that under a PPP framework, it is virtually impossible for a project to default during construction. The developer's ability to perform through construction and operation is linked to the strength of the legal and financial structure of each project, guaranteeing that reliable contractors have taken construction risk, that funds are available to complete construction and that the developer will be able to pay back debt with future toll revenues. (And, reserve funds are part and parcel of this model.)

"For example, the financial structure of projects like the North Tarrant Express and the LBJ Express in North Texas could hardly be stronger:

- They benefit from robustly guaranteed lump-sum, fixed-price and delivery design build contracts.
- Bonds have already been issued; the federal loan is fully committed; the Texas Department of Transportation has allocated its public funds; and all project investors have already contributed \$274 million and have provided firm commitments for three times as much.
- Through the operation phase, even if they were to realize revenues 50 percent below projections over the course of the 52-year lease agreement, cash-flows would still be sufficient to repay the debt, and therefore default will hardly occur.
- Fitch and Moody's rating agencies have independently reviewed the financial structure of each of the projects for the bond issuance providing "Investment

Grade" ratings.

"A key feature of this model is that each individual concession project is wholly independent from the others such that the developer's ability to perform in one project in no way affects its ability to perform in another. Each of our 25 highway projects in seven different countries has an isolated, non-recourse financial structure. There are safeguards built into the project agreements with the States in which we operate that protect taxpayers. Under the PPP model, the State retains ownership of the project at all times, and toll rates are governed by contract rules that cannot be modified for whatever reason.

"There is always a possibility that a project could default following completion of construction if net toll revenues fall materially below projections over extended periods. But it is worth noting that although default would be extremely unpleasant for investors, it would allow the State to take over a much-needed project at a fraction of its cost.

"Second, all of our projects are backed by Cintra. Cintra is one of the world's leading private infrastructure companies spanning more than 40 years of innovative highway development experience on three continents, with more than 25 highway concession projects currently underway in seven countries.

"In public private partnerships, the underlying financial condition of the investor is key, and in our case extremely robust, with net cash position at our parent company level (www.ferrovial.com) and available capacity to invest of over \$1.5 billion.

"At Cintra US we are proud to be working with state and local partners to create safe and reliable congestion-relieving roadways, some of which languished for decades because of the lack of government-funded solutions. Our public-private partnerships are creating tens of thousands of U.S. jobs, and those projects, once complete, will account for tens of billions of dollars in economic development opportunities.

"Having been a pioneer in introducing the PPP model in the U.S. market, we look forward, as a long-term investor, to the opportunity to continue to help fund vital public priorities."