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## FISCAL IMPACT REPORT

ORIGINAL DATE 02/06/13

SPONSOR Keller/Cook LAST UPDATED \_\_\_\_\_ HB \_\_\_\_\_

SHORT TITLE Transportation Public-Private Partnerships SB 273

ANALYST Soderquist

### APPROPRIATION (dollars in thousands)

Appropriation		Recurring or Nonrecurring	Fund Affected
FY13	FY14		
	Indeterminate		State Road Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY13	FY14	FY15		
	Indeterminate	Indeterminate		

(Parenthesis ( ) Indicate Revenue Decreases)

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY13	FY14	FY15	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
<b>Total</b>		Indeterminate	Indeterminate	Indeterminate		State Road Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

Duplicates, Relates to, Conflicts With, Companion to  
Relates to Appropriation in General Appropriation Act

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Department of Transportation (DOT)

Attorney General's Office (AGO)

New Mexico Finance Authority (NMFA)

Department of Finance and Administration (DFA)

## SUMMARY

### Synopsis of Bill

Senate Bill 273, the "Transportation Public-Private Partnerships Act", amends the New Mexico Procurement Code, NMSA 1978, § 13-1-28, et seq. The proposed legislation authorizes the New Mexico Department of Transportation (NMDOT) and local governments to enter into public-private partnerships ("P3s") with private partners based on solicited and unsolicited proposals from private entities for the development, financing, maintenance or operation of transportation facilities. In the legislation, "transportation facility" is defined to mean all publicly owned modes and means of transporting people or goods and related structures and properties, and includes roads, airports, rest areas, railways, bus and transit systems, and ports of entry. P3s would be otherwise exempt from the Procurement Code. SB 273 also authorizes the department to transfer the use or control of publicly-owned property to private companies by the conveying of leases, permits and easements. In order to allow private companies to recoup their investment, the proposed legislation specifically authorizes private companies to charge user fees such as tolls or other charges for the use of a transportation facility. The proposed legislation establishes the procedures for selecting a proposal and the terms of an agreement, including grounds for terminating an agreement. The initial term for a P3s agreement may not exceed 25 years.

The proposed legislation grants the department rule-making authority to carry out the purposes related to P3s. All proposed P3s would require review and approval by the Attorney General's Office and the State Board of Finance. The proposed legislation authorizes the use of alternative project delivery methods ranging from design-build agreements to design-build-finance-operate-maintain agreements. Concession agreements, which are not defined, are also authorized by SB 273; the term concession agreement is typically used to describe a negotiated contract between a company and a government that gives a company the exclusive right to operate a specific business on department transportation facilities, i.e., a long-term lease where a private partner pays a concession fee in order to lease an existing toll road.

The procurement of P3 agreements by the department may be facilitated through a number of processes including the issue of requests for proposals, request for qualifications, best-value selection procurements based on price or financial proposals, short-listing of qualified proposers, negotiations, the use of best and final offers, and "other procurement procedures." SB 173 also authorizes the department to consider unsolicited proposals, if a reasonable opportunity is afforded for other companies to submit competing proposals.

The department would be responsible for acquiring rights of way related to the property for the P3 through the department's exercise of eminent domain. Section 11 of the proposed legislation includes the provisions that allow the exercise of eminent domain by the state for P3s.

The department may retain experienced financial, legal and other experts to assist in the evaluation, negotiation and development of P3 agreements for a transportation facility. Agreements covered by the proposed legislation may not exceed a term of 25 years but may contain provisions providing: (1) the establishment of user fees, rents, advertising and sponsorship charges, service charges or other charges; (2) how revenue will be collected, accounted for and audited; (3) enforcement of user fees, including the use of cameras; (4) for a reasonable rate of return on the private partner's investment and the adjustment of user fees and other charges during the term of the P3; (5) a variety of traffic management strategies, including

general purpose toll lanes; high-occupancy vehicle lanes; (6) performance-based payments to the private partner; (7) how costs, risks, and payments may be shared; and (8) how cost overruns will be allocated.

For both solicited and unsolicited proposals, the proposed legislation expands the Trade Secrets Act by establishing that portions of proposals may contain confidential trade secrets that are not subject to public disclosure under the Inspection of Public Records Act (IPRA). However, private companies submitting proposals would be required to prepare an executive summary of their proposals which would be subject to public disclosure.

The proposed legislation contains a number of provisions with regard to the funding and financing of P3s. SB 173 allows any funding vehicle available to the state or a private company to fund such projects. Funding sources would include grant anticipation revenue bonds (GARVEE bonds), private activity bonds, revenue and toll revenue bonds, grants, loans, loan guarantees, lines of credit, and other federal, state or local revenues, and other available forms of public and private capital. A private partner would be able to secure financing by pledging the revenues from the transportation facility; however, such pledges would not constitute a general obligation of the department. Further, the proposed legislation authorizes the department to issue revenue bonds on behalf of a private partner which, in turn, would be considered, under certain circumstances, to be appropriate investments for the severance tax permanent fund. While such department issued bonds would not be a general obligation of the state, it would be a department obligation from pledged revenues.

According to the American Association of State Highway and Transportation Officials (AASHTO), 25 states have passed legislation to allow P3s and most have used P3s to fund transportation infrastructure improvements. AASHTO has published a document entitled “Public Private Partnerships in Surface Transportation” that outlines some of the critical components of P3s (<http://www.transportation.org/Documents/Lee-2012-08-23.pdf>). The National Conference of State Legislators (NCSL) has also discussed the issue extensively – including details of enabling legislation used in other states and states that have used the legislation effectively – and has published a document entitled “Public-Private Partnerships for Transportation: A Toolkit for Legislators” (<http://www.ncsl.org/documents/transportation/PPPTOOLKIT.pdf>).

## **FISCAL IMPLICATIONS**

Without any identifiable P3 project in the state pipeline, the fiscal implications of passage of SB 273 cannot be determined. In general, P3s are agreements that allow private companies to take on traditionally public roles in infrastructure projects, while keeping the public sector ultimately accountable for a project and the overall service to the public. According to the NMDOT response, in a time of constrained state capital improvement budgets and dwindling road fund revenues, P3s – when implemented well – could leverage additional sources of funding and financing for infrastructure. However, while helpful for raising finance for large, highly leveraged investments, project finance comes at a cost. Interest rates for project-financed debt are usually higher than traditional government borrowing. The transaction cost – setting up the contractual structure and carrying out adequate due diligence -- can make it unattractive for smaller projects.

According to the response from the Department of Transportation (NMDOT), assuming the department identified appropriate P3 projects, the department would be expected to require

additional FTEs in order to provide adequate staffing for such projects. Additional staffing needs would be required to meet the need for supervising engineers, inspectors, and other compliance officers. The department would also expect to contract with consultants to provide financial, legal and other assistance in the evaluation, negotiation and development of P3 specifications and agreements.

The NMDOT also provides a further caveat on the P3 concept, stating the lack of fiscal clarity and miscalculation of projected public use of a P3 facility may lead a government agency to overestimate the extent to which P3s are genuinely increasing the resources available to pay for infrastructure. As a result, an agency may accept higher commitments to deliver new and improved infrastructure while incurring greater fiscal risk under P3s than would be consistent with prudent public financial management. According to the NMDOT, a number of states have under-projected the user fees generated by a P3 resulting in states incurring additional risk and costs to operate a P3 facility.

The Federal Highway Administration (FHWA) actively encourages the use of P3s, arguing “the private sector can bring creativity, efficiency, and capital to address complex transportation problems facing State and local governments”. The FHWA provides specific direction on P3 best practices through their Innovative Program Delivery Program. However, according to the NMDOT response, although the proposed legislation allows for federal funding of P3s, they are not eligible for direct federal funding – primarily because federal regulations generally require that eligible federal-aid projects be awarded to the lowest responsible bidder (see CFR 635.114, 23 CFR 172.5a, and 23 CFR 635.104). P3s may be eligible on a case-by-case basis for FHWA loans, loan guarantees, or lines of credit.

Lastly, the NMDOT observes that P3s, while leveraging new opportunities to finance new and improved transportation facilities, may result in reducing the need to increase the department’s budget to meet growing needs it but does so by directly shifting those costs from the taxpayer to the travelling public. Some states have found this arrangement worth pursuing, while others have found it to be a burden they do not want to transfer.

## **SIGNIFICANT ISSUES**

The proposed legislation exempts P3s from the Procurement Code. More specifically, SB 173 would not require competitive sealed bids and the award of contracts to the lowest responsible bidder pursuant to NMSA 1978, § 13-1-102. Instead, the award of P3 contracts would be based on subjective assessments of proposals – all of which remain undefined in the proposed legislation. The primary purpose of the Procurement Code, NMSA 1978, § 13-1-28, et seq., is the fair and equitable treatment of all bidders, to maximize the purchasing value of public funds, to provide safeguards for maintaining a procurement system of quality and integrity, and to protect "against the evils of favoritism, nepotism, patronage, collusion, fraud, and corruption in the award of public contracts." (see *Planning and Design Solutions v. City of Santa Fe*, 118 N.M. 707, 710, 885 P.2d 628, 631 (1994)). According to the NMDOT, moving to a more subjective procurement process raises issues with regard to the goals of, and the protections contained in, the Procurement Code. In addition, inasmuch as Section 6 [page 8, ll. 13-18] of the Act allows much of the content of proposals to be treated as Trade Secrets not subject to public disclosure an issue arises regarding the appropriate level of transparency on government procurement.

Other specific issues are addressed as follows, reflecting the concerns of both the NMDOT and the Attorney General’s Office in their respective responses:

Does the definition of “regional transit authority” also include councils of government (COGs) in the state?

The definition of ‘transportation facility’, is overly broad and could be expanded beyond tollways which would appear to the intent of the proposed legislation.

The terms “availability payments” and “performance-based payments” are not defined although used in the provisions of the proposed legislation.

The term “concession agreements” is not defined. While in the context of transportation-related P3s the term ‘concession agreement’ is typically used to describe a long-term lease where a private partner pays a concession fee in order to lease an existing toll road, the lack of a definition may result in its application to situations not contemplated in the proposed legislation. The proposed legislation would also benefit by imposing limitations on the use of, and the minimum fees to be generated by, concession agreements.

Section 3(B) [p. 5, ll.2-7] states the Attorney General and the State Board of Finance should review and approve or disapprove a proposal for a P3, but the criteria required of a successful proposal are not defined. It is unclear what the Attorney General’s Office and the State Board of Finance should be reviewing.

Section 5(A)(2) [pps. 6 and 7] states that a public partner may consider an “unsolicited proposal” and a “reasonable opportunity” must exist for other persons to submit competing proposals, but it does not define what is meant by a “reasonable opportunity” or what protections ensure that one private partner does not have inappropriate or disproportionate access to a potential agreement.

Section 5(1)(b) [p.6, ll. 10-13] allows the department to procure P3s through “negotiations, best and final offers or other procurement procedures” is arguably overbroad, provides too much discretion in the department, and could invite unnecessary bid protests and litigation. The proposed legislation should set forth firm ground rules for bidding and negotiation of P3s. The department should be required to use a more constrained, objective means of awarding P3 contracts, and should at least receive specific direction on the procurement methods authorized by the proposed legislation.

Section 5(1)(c) [p. 6, ll. 14-15] allows the department to procure P3s agreements by “seeking development and finance plans that are most suitable for the project.” This section would better serve the taxpayer by requiring that the department procure such agreements that are “most advantageous to the department and suitable for the project.”

Section 5(2)(D) [Page 7, ll. 13-17] authorizes the department to charge, and accept, an administrative fee from an entity to evaluate an unsolicited proposal. This provision likely runs counter to Section 5 of the Act as it seeks to encourage unsolicited proposals while still providing a “reasonable opportunity for other persons to submit competing proposals for consideration.” A private entity has likely invested significant time and money in developing an unsolicited proposal, which would then be put out for competition to other contractors who could submit competing bids without having incurred the costs of developing the initial idea. While

recognizing that the department would likely expend considerable effort in evaluating the unsolicited proposal, charging a fee to consider unsolicited proposals would be expected to stifle the submission of unsolicited proposals. It may also be observed that other states which have adopted PPP enabling legislation typically do not assess a fee for unsolicited proposals.

Section 5(E) [page 7, ll. 18-20] requires that the department “follow substantially the procedures of the Procurement Code in so far as practicable” runs counter to the Act which specifically exempts P3s from the Procurement Code and authorizes the use of procurement procedures which are not authorized by the Procurement Code.

Section 6 [page 8 and 9] allows individuals or entities to prevent disclosure of their proposals as Trade Secrets. Although not referred to in the proposed legislation, New Mexico has adopted the Uniform Trade Secrets Act, NMSA 1978, § 57-3A-1, et seq., which allows for the secrecy of trade secrets. SB 173 would appear to expand the protection of alleged trade secrets into the documents produced as part of a procurement proposal. Because the evaluation of proposals under the proposed legislation is based upon subjective, qualitative assessment, protecting disclosure of proposals raises an issue with regard to government transparency.

Section 8(A)(2) (p. 11, ll. 15-18) authorizes the department to include within a P3 agreement a provision providing for “a reasonable rate of return on the private partner’s investment.” The section discusses means by which user fees may be charged and collected, such as price adjustments and the use of high-occupancy lanes. The proposed legislation provides no parameters by which a reasonable rate of return may be gauged or quantified by the parties. The issue of determining how a reasonable rate of return is complicated and the proposed legislation should provide additional direction on this issue. For instance, should user rate increases due to inflation be keyed to major economic indices? How are user fees and a rate of return determined? How much compensation for the design/build/operate or other work the private firm is granted goes into the profit determination and how is the calculation determined? Should P3 agreements provide caps on rates of return or revenue sharing above certain equity returns?

Section 8(A)16) [p. 14, ll. 13-17] allows the private partner to acquire real property related to the transportation facilities by exchange of real property owned by the state. If the purpose of a P3 is to use private resources to operate a public facility, it is unclear as to the reason that a private partner would be required to acquire public property.

Section 8(D) [p. 15, ll. 1-15] allows “reasonable compensation to the private partner” for adverse effects resulting from the agreement, but does not define what “reasonable compensation” should be, nor does it state explicitly that a private partner would be prohibited from applying for this compensation.

Section 10(A)(1) [p.16 (1, 2, & 3) authorizes a number of funding vehicles for a P3 including grant anticipation bonds and revenue bonds which are financial tools already used by the department. The proposed legislation would expand use of innovative financing techniques to include private activity bonds which are tax-exempt bonds issued by or on behalf of local or state government for the purpose of providing special financing benefits for qualified projects. Such financing is most often for projects of a private user. While Section 10(H) is clear that revenue bonds are not general obligations of the state, Section 10(A)(1) is silent as to whether or not the department is prohibited from pledging its credit with regard to private activity bonds. Unconstrained use of alternative financing mechanisms could significantly affect public debt obligations.

Section 10 (B) [p. 16, ll. 17-22] states that “no pledge of revenue constitutes...a general obligation of state or local government, but the Attorney General’s Office questions whether this provision could withstand legal challenge.

Section 12(A) [p. 18, ll. 16 -25] authorizes the department to issue revenue bonds on behalf of a private partner. Section 12(D) allows the department to “enter into other financial arrangements.” While the use of innovative financing techniques such as revenue bonds and other arrangements (which would presumably include “availability payments” wherein the department would make regular payments to the private partner based on the facility’s availability and level of service achieved for operations and maintenance) on behalf of a private partner may allow financing at rates that are almost as low as tax-exempt debt, the department may be required to accept some of the revenue risk and may provide some level of initial funding to offset capital requirements. Thus, the proposed legislation should be more specific as to the permissible and required conditions, terms and limitations of P3 financing.

Section 16(D) [p. 25, ll. 5-21] would authorize the department to sell a publicly owned transportation facility prior to issuance of bonds. The section would authorize the department to sell a state road to a private entity in return for lease payments for a period of time not to exceed 25 years. As written, the NMDOT believes the section would appear to allow the private partner, at the expiration of the P3 term, to cease operating the facility or to do so without any consideration for the needs of the public.

Section 16(E) [pp. 25-26] states that a public partner may borrow money “subject to constitutional limitations on public debt”, but the Attorney General’s Office questions whether this provision could withstand legal challenge.

Section 16(F) [p. 26, ll. 8-17] states “the public partner may obtain commitment from a financial institution to borrow money”, but the Attorney General’s Office questions whether this provision could withstand legal challenge.

Section 21 [p. 32, ll. 8-16] exempts financial instruments used by the state or political subdivision – including bonds, lease and installment purchase agreements, and revenue derived from lease or sale by the public partner – from taxation, but the Attorney General’s Office questions whether this provision could withstand legal challenge.

NMSA 1978, § 13-1-98(FF) expands the exemptions under the Procurement Code such that “procurements pursuant to the Transportation Public-Private Partnerships Act” would be exempt. Thus, while Section 5(E) [page 7, ll. 18-20] (discussed above) requires that the department “follow substantially the procedures of the Procurement Code in so far as practicable,” it is clear the P3s are exempt from the Code.

An additional issue left unresolved by the Act involves a “hand-back” of the transportation facility. The proposed legislation is silent on when a transportation facility becomes private property, but the NMDOT states the proposed legislation should contain a requirement that a facility be returned to the department at the end of the term in a state of good repair.

## **PERFORMANCE IMPLICATIONS**

The NMDOT response states that the performance implications of the proposed legislation cannot be determined at this time, but assuming that the department identified appropriate P3 projects, the department would be expected to require additional FTEs in order to provide adequate staffing for such projects. Additional staffing needs would be required to meet the need for supervising engineers, inspectors, and other compliance officers. The department would also expect to contract with consultants to provide financial, legal and other assistance in the evaluation, negotiation and development of P3 specifications and agreements.

## **ADMINISTRATIVE IMPLICATIONS**

According to the NMDOT response:

Because SB 273 authorizes the department's unrestricted use of design-build on P3s, it would conflict with NMSA 1978, § 13-1-119.1, which prohibits the department from engaging in design-build project delivery system projects absent specific legislative authority.

Because SB 273 expands the use of protected trade secrets within the procurement context it should be considered in light of the Uniform Trade Secrets Act, NMSA 1978, § 57-3A-1, et seq.

NMSA 1978, § 13-1-98(FF) would be amended pursuant to SB 273 in order to exempt PPPs from the Procurement Code.

## **CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP**

Relationship with House Bill 4 related to transportation infrastructure appropriations.

## **TECHNICAL ISSUES**

See comments in Significant Issues section of this analysis.

## **WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL**

The department and procurements related to road construction projects and transportation facilities would continue to be made subject to the New Mexico Procurement Code. The department would also be restricted from entering into P3s.

Current revenue for state road funds, even when combined with federal funds, is insufficient to address needs critical to the economic welfare of the state. NMDOT economic analysis suggests state road funds will be negatively impacted even further as a result of fuel-efficient vehicles and declining population in the state. Within the constraints mentioned in the previous section concerning FHWA funding, the proposed legislation offers a potential although likely partial solution to funding shortfalls.

RS/bm