Knik Arm Bridge–State as Last Sucker?

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There may be no better Alaskan example of a big spending government project misrepresented as a "public-private partnership" than the Knik Arm Bridge, Alaska's second and only surviving "Bridge to Nowhere". This study examines the financial aspects of the Bridge project and looks at the long term financial impact to the State of Alaska.

The Knik Arm Bridge has always been a wholly government-funded project seeking more government funding to get off the ground. Funded early on by an original $230 million Congressional earmark, with the state taking about half for other projects, the Knik Arm Bridge and Toll Authority (KABATA) has spent $60 million to date on studies and salaries.

In March, 2010 KABATA told the Anchorage Assembly that the private sector would assume the financial risk of making up the inevitable toll shortfall to pay off the bonds. In fact, KABATA had already applied for another government $300 million loan declaring that annual appropriations from the State would be needed to backfill the lack of toll revenue. (See p. 7 http://www.knikarmbridge.com/documents/TIFIAcoverandLOI.pdf)

With the toll shortfall, what might the state's liability be over 35 years of cumulative private contractor payments? In KABATA's latest federal loan application, it estimated this liability at $ 3 billion. (See p. 4 http://knikarmbridge.com/TIFIA/2011/12-2011-KABATA-Model-PABs.pdf) And this may even be on the low side.

A public records act request to the State Transportation Department revealed that the toll revenue forecast may be overestimated by a factor of two. When Scott Goldsmith's (University of Alaska, ISER) estimate of future population was modeled into vehicle trips by Ch2M Hill, it concluded 17,700 vehicles would use the Bridge daily in year 2035. However, KABATA's comparable number that it uses for its toll revenue projection is 36,000 trips a day. This is difficult to imagine because today there are less than 30,000 trips now between the Mat Su and Anchorage on the Glenn Highway.

This possible 103% overestimation of toll revenue by KABATA over the ISER-CH2MHill toll numbers is consistent with the study of a retired federal economist. This economist documented a 118% average overestimation error by the KABATA traffic and toll consultant, Wilbur Smith Associates, for the first five years a toll facility was open in all US projects. (See http://www.scribd.com/doc/79582705/RCA-Study-Wilbur-Smith-Traffic-amp-Revenue-Forecasts-012712.%3Cbr%20/%3E.)

The vast majority of the present MatSu commuters would continue to use the Glenn Highway since Palmer and Wasilla are closer to Anchorage via the Glenn than via the proposed Knik Arm Bridge. In addition, these commuters would not have to pay a $5 one-way toll rising 2.5% a year.

An independent estimate of the Knik Arm Bridge costs concludes that it would accumulate $1.1 Billion in deficits by 2035. (See http://knikbridgefacts.org/wp-content/uploads/2012/02/The-Real-Finances-of-the-Knik-Arm-Bridge-v3.pdf).

We will spare ourselves having to debate over population and traffic projections and just focus on which consultants are paid by KABATA and watch who is left holding the bag. If the private sector were willing to finance the project, it is more than likely the project would already have been financed. But there were no takers.

Instead, KABATA went to the legislature last year with two bills tapping the General Fund to provide another $150 million for the project and also to make any contract KABATA would sign with the private contractor "obligations of the state" – the inevitable blank check. As David Boaz of the free market-oriented Cato Institute observed of the Knik Bridge project: "Yes, the largest investment companies — and the largest construction companies — would be delighted to work on this project, if someone else would actually put up the money. " http://www.huffingtonpost.com/david-boaz/bridge-to-nowhere_b_984839.html

Clearly, the private sector is not interested in taking any risk on having sufficient toll revenue to pay off the Bridge bonds and operating costs. Rather, KABATA has promised the two losers of three short-listed consortia bidding for the expected $1.1 billion contract a "stipend" of $2 million each to submit a final proposal. Supposedly, KABATA will pay for the intellectual property of the losers' bids, but industry observers consider this amount excessive.

If the KABATA legislation (HB 158-159 and SB 79-80) passes this session of the legislature, the winning contractor will have 35 years of state-guaranteed "availability payments" that KABATA estimates will total $3 billion. Even this $3 billion assumes KABATA will get $350 million in federal TIFIA and TIGER loans and grants which it failed to get in the past three years.

The next phase in the battle of the Bridge is likely to take place over the approval of the Anchorage Metropolitan Transportation Plan (MTP) beginning with a public hearing April 10, 2012 at the Anchorage Assembly. The Knik Bridge remains in the MTP with the new transportation plan, unlike the existing one, overturning the Assembly's previous position that no further State or local funds would go to support the Bridge.

Unfortunately, readers of the new draft MTP would learn nothing of the size of the downside risk to the State on this $1.1 billion project. The draft "assumes" the KABATA bills will pass and that if the State has to make up what has been independently estimated as an average of $55 million a year in deficits, that none of this expected body blow to State transportation funds will impact funds going to South Central Alaska. (See pp. 6-29-31 http://www.muni.org/Departments/OCPD/Planning/AMATS/Documents/MTPChapter-6_123011.pdf

A diligent reader of the MTP would see only the sources and uses of funds to finance the $1.1 billion project. He would not see any of the overall financing costs and ballooning annual availability payments to the private contractor which go from $34 million in year 1 to $133 million in year 36. (p. 4 http://knikarmbridge.com/TIFIA/2011/12-2011-KABATA-Model-PABs.pdf)

The draft MTP shows an estimated $79 million in private equity from the contractor which may seem impressive. Not disclosed is that under the proposed state-guaranteed contract KABATA estimates a 12% compounded return of net cash flow to repay the contractor's equity. So that $77 million in private contractor equity would end up costing the state a KABATA-estimated $920 million before the bonds are paid off in 2050.

While the final RFP competition may only result in a compounded return to the contractor of, say 10%, the whole proposed deal structure begs an obvious question: Why would a state with a AA credit rating that can borrow long term at 4% guarantee a contract providing a contractor a 10-12 % compounded return? The State assumes all the risk, the private contractor assumes none. Only in the world of crony capitalism would this make sense.

The marketing of the Bridge project has been an ongoing exercise in the euphemisms necessary to mask a typical bottomless government liability. The proposed $150 million in additional State funds is just a loan that will be paid back according to the rosy trip forecast. A small print footnote to KABATA's 12/30/11 federal loan application notes that "if" – more likely "when"– the reserve fund dips below $50 million, it will trigger an automatic appropriation request to the legislature to have the fund "replenished" back to $50 million (see p. 8 in KABATA's latest Financial Plan http://knikarmbridge.com/TIFIA/2011/12-2011-KABATA-Model-PABs.pdf).

So, this reserve fund will apparently be automatically replenished by annual legislative appropriation, regardless of the state of Alaska's budget.

The fundamental misleading description of the selling of the "public-private partnership" project by KABATA is its assurance to the legislature that the contractor will "finance" the project. Technically, the contractor will take the State of Alaska-guaranteed contract to the credit agencies and the State's credit rating will likely be the evidence the contractor needs to provide the investment grade necessary for the firm to then go to the bond market for the funds to build the project. So in reality it's the proposed State guarantee on the KABATA contract – or the continually replenishing $150 million "reserve fund" by the State — that finances the project and not the balance sheet of the contractor which is put at risk.

The original legislation establishing KABATA made clear that the new agency could not pledge the State's credit or sell bonds without earning an investment grade. But in a 11/30/11 legislative briefing, KABATA now seeks to "clarify" that prohibition to make the bonds "obligations of the State" by amending the original statute "to reflect current market realities."

Senate Finance Chairman Bert Stedman (R-Sitka) is opposed to the State guarantee in the current bills but KABATA Board member Senator Linda Menard (R-Wasilla) is now rewriting the KABATA bills to overcome that objection. However, it is still likely that the continual replenishing of the $150 million reserve fund will remain in the bills to provide a backdoor State guarantee. Without the State holding the bag, it is unlikely KABATA will be able to put the RFP on the street this year.

Hopefully, both the Anchorage Assembly and the Alaska Legislature will pay close attention to the risk-free financial arrangement of this "public-private partnership" and recognize it for what it is. Public assumes the risk, private sector assumes the benefits.

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