

***PRIVATIZING MTA SERVICES, COST  
SAVINGS OR POLITICAL BUZZWORD?***

**A REPORT BY THE PERMANENT CITIZENS ADVISORY  
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## **PRIVATIZING MTA SERVICES, COST SAVINGS OR POLITICAL BUZZWORD?**

### **Executive Summary**

Today, New York's Metropolitan Transportation Authority faces decreasing subsidies and, at the same time, faces increasing needs for service, infrastructure repair, and expansion. Some economists and policy makers are of the opinion that privatization of public services increases agency efficiency and decreases costs. Privatization is an omnibus word for private participation in public agency service provision. This paper explores three types of privatization for public transportation agencies: the sale of a state owned enterprise; placing a public agency under private management; and the use of private funding and management, rather than public, for new capital development. The goal is to determine whether privatization, when applied to the Metropolitan Transportation Authority (MTA), will meet the goals of decreasing costs and increasing efficiency.

Many public transportation agencies have experience with these types of privatization, including London Transport, British Rail, the Washington Metropolitan Area Transit Authority, and New Jersey Transit. Lessons are to be learned from the experiences of these agencies. Privatization is not an easy process and results differ from case to case. In many of the agency examples, there have been both negative and positive consequences of privatization. These results include union protests and halts in services on one side and dramatic cost savings in subsidies on the other. In the case of the sale of the United Kingdom's British Rail, service has suffered under private ownership. In Indianapolis, bus services have become more efficient and expanded under private management. At New Jersey Transit, private management of a capital project is saving time and money. Privatization of services is not a simple answer for the financial difficulties facing the MTA.

Conclusions and guidance are offered as to the process of privatization of public transportation services:

- Privatization is not a panacea for investment starved public transportation agencies.
- Intense examination of contracting out and selling public transportation systems is necessary to determine financial benefits of privatization.
- Private operations of transportation systems work best when public oversight is maintained versus deregulation.
- Gross cost contracts encourage more competition than net cost contracts.

- Union issues are barriers to contracting private management of services operated by public employees.

In terms of privatization of MTA services, the PCAC recommends that the MTA:

- Not contract out or sell the MTA public transportation network on a large scale.
- Examine the benefits of contracting out or selling Staten Island Railway to a private firm.
- Examine the benefits of contracting out new bus routes to private operators.
- Study the development of upcoming London Underground infrastructure contract for benefits which may be applied to MTA contracts.

Although large scale privatization of operations is not recommended for the MTA, generating private funding and utilizing private management of capital projects is encouraged. Public private partnerships generate private revenue for public transportation agencies. Public private partnerships between public transportation agencies and private developers are widespread, because proximity to transit access is an attraction for developers.

Real estate value capture mechanisms, like tax increment financing, are promising tools for generating private funding for public transportation capital and operating budgets. Real estate values can increase due to public transportation development. This increase can be gleaned by public transportation agencies and used to pay for construction projects. The MTA should look to partner with New York City and New York State to mandate exactions from private developers. Many MTA projects are candidates for private partnerships.

Greater private participation in the construction process is also promising as a time and cost savings technique. The turnkey procurement method bundles the design, build, operate, and maintenance aspects of the construction process. Public transportation agencies invite private firms to team together to propose and construct new developments. This technique has been proven efficient by New Jersey Transit and might also benefit the MTA in certain circumstances.

In terms of generating private funding and using private management for capital programs, the PCAC recommends that the MTA:

- Pursue public private partnerships in which private developers contribute directly to capital construction costs or in which private partners lease public transportation property above or next to stations.
- Invite private retailers to design, construct, and maintain retail spaces in stations in order to shift the financial burden of design and construction to the private sector.
- Capitalize on voluntary programs like Adopt-a-Station and the Franklin Street Economic Development Corporation example, where developers contribute to rehabilitating stations while performing a community service and promoting their philanthropic activities.
- Be aggressive with developers to secure financial contributions when developments negatively impact MTA services, or team with the city or state to legislate a set mandatory exaction on new developments that impact MTA services.
- Work with legislators to implement a tax increment financing mechanism to collect revenues generated by increases to real estate values that occur following transit improvements.
- Use turnkey procurement for standalone developments.

There are many opportunities for the MTA to utilize private partnerships and private management for projects which are currently in planning phases. The MTA must begin to work on private partnerships now, while there is still adequate time to incorporate these time saving and revenue generating techniques in the planning process. The MTA is an integral aspect of public services which benefits both riders and non-riders. Developing new MTA services impacts real estate prices and New York's economic vitality. The MTA should look to capture some of this financial benefit.

The MTA should further explore public private partnerships, real estate value capture mechanisms, and the turnkey procurement method for:

- An intermodal transportation hub at Sunnyside Yard serving the MTA agencies and other carriers. The facility would be an expansion of the station the Long Island Rail Road proposes to build as part of *East Side Access*.
- The proposed Second Avenue Subway.
- The Metro-North Railroad *Hudson Line Extension* project.

Privatization works best for failing, inefficient, financially strapped public transportation agencies. With agencies that exhibit high operating subsidies and low operating efficiency, contracting out to private service providers can be a good remedy for their financial difficulties. However, the MTA does not fit this mold. In recent years, the MTA has cut costs through its 1995-1999 financial plan, increased bus and subway services, and cut passenger fares. Under strong leadership, the MTA has pulled itself out of a state of complete disrepair into an era of growth. As a vital public service, the MTA should remain under public management.

However, privatization for capital construction can benefit the MTA. Private management for development projects, the turnkey method, is promising as a cost and time savings technique and should be further explored by the MTA. There are also many opportunities for the MTA to generate private funding through public private partnerships and real estate value capture mechanisms. The MTA should capitalize on its importance to land values. The MTA can do more to meet the needs of its riders by expanding its capital construction program with the help of private funding and management.

## INTRODUCTION

The privatization of public services is offered by politicians and policy makers as a method for increasing public agency operating efficiency and decreasing tax expenditures. In New York, the services on the list for private sale or contracting out include park services and street cleaning. Some policy makers point to the success of Business Improvement Districts (BIDs) that perform street cleaning and sometimes add private security to public streets as an argument in favor of privatization. In Jersey City, the management of public libraries is being contracted out. As one planning professional put it, "Privatization is the buzz word concept of the '90s."<sup>1</sup>

This paper examines the usefulness of private participation for constructing and operating public transportation services. The experience of local, national, and international public private partnerships is assessed, and guidance is offered to the Metropolitan Transportation Authority (MTA) on their use. One goal is to determine whether the MTA might better meet the needs of its riders by privatizing service operations or through public private partnerships. Other goals are to determine if the MTA can become a more efficient provider of services through private partnerships and if the MTA can find additional funding sources for capital programs in the private sector.

This paper defines privatization of public transportation services and examines recent experiences of public transportation agencies in the context of the MTA. Private financing and joint financing techniques are plentiful and becoming increasingly popular. A brief overview of many successful styles of incorporating private monies to build public transportation infrastructure is given and examples pertinent to the MTA are highlighted. Discussion begins with the contracting out of services and sale of public services to the private sector, followed by an examination of public private partnerships in station development, and ends with turnkey development.<sup>2</sup>

There are three forms of privatization. In *Going Private, The International Experience with Transport Privatization*, authors Jose A. Gomez-Ibanez and John R. Meyer describe the most common forms of private participation in public transportation:

- Sale of a state owned enterprise to the private sector.
- Use of private funding and management rather than public for new capital development.
- Contracting out to private service providers public services previously provided by government employees.<sup>3</sup>

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<sup>1</sup> Linda R. Cox, Interview by Author, New York, NY, (June 1998).

<sup>2</sup> Turnkey development is a capital construction application that incorporates private operations, and in some cases, private funding. Turnkey is discussed in detail in Part 2.

<sup>3</sup> Jose A. Gomez-Ibanez and John R. Meyer, *Going Private, The International Experience with Transport Privatization* (The Brookings Institute: Washington, DC, 1993), p. 1.



These forms are discussed in depth and examined for the benefits they could provide to New York's public transportation riders, whether theoretically or in reality.

### **Financing the MTA**

The Metropolitan Transportation Authority (MTA) is an enormous public agency as parent to Bridges and Tunnels, Long Island Bus, Long Island Rail Road, Metro-North Railroad, and New York City Transit. The public transportation network managed by the MTA is the largest public transportation network in the United States. Average paid ridership per weekday for the MTA is 5.7 million. In 1997, the operating budget for the entire MTA was \$5.5 billion. The New York City Transit (NYC Transit) share of the operating budget for subways, buses, paratransit, and the MTA Staten Island Railway was \$3.7 billion. The commuter railroads, Long Island Rail Road and Metro-North Railroad, accounted for \$1.6 billion.

MTA administrators and its governing board recognize the need to be cost-effective, efficient providers of public transportation services. The MTA is working to reduce expenses by \$3.3 billion cumulatively over five years as part of its 1995-1999 financial plan. The plan includes reducing and consolidating administrative functions, increasing revenues, and developing new revenue sources to support the capital program. As the MTA works to cut expenses, it has privatized some services and outsourced others. In 1997, the MTA contracted out the Long Island Rail Road freight service. NYC Transit's light truck maintenance was outsourced, Bridges and Tunnels' E-Z Pass customer service unit was contracted out, and the MTA Data Center was placed under private management. These outsourced activities are considered to be outside of the core mission of the MTA - moving people.<sup>4</sup> The MTA has sought to save costs while concentrating on providing public transportation services. The program of outsourcing and contracting out some services has been successful for the MTA in terms of helping it to achieve its goal of cutting costs. It is expected that by the end of 1999, the MTA's \$3.3 -billion goal in savings will be accomplished. Further, private partnerships may be one way for the MTA to meet its goal of developing new funding sources to support its activities.

Federal, state, and local government financial support to the MTA determines its ability to operate services and invest in capital construction projects, because fare and toll collection do not cover expenditures. The role of government financing for operating public transportation has changed in recent years. Federal assistance for operating public transportation has been reduced steadily. For example, in 1996, total Federal operating assistance to public transportation agencies was \$500 million, and in 1997 it was \$400 million. In 1996, the MTA received \$43 million of Federal subsidies for operations, and in 1997, it received \$33 million. For areas with populations of more than 200,000, Federal operating assistance is no longer available. New York State and New York City have also reduced their operating assistance to the MTA in recent years, thus

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<sup>4</sup> Metropolitan Transportation Authority, 1996 Annual Report, p. 15.

the MTA must look elsewhere for operating financing. Privatizing services might help meet the operating financing gap by reducing the need for subsidies, if it is determined that privatizing services is cost-effective for the MTA.

The discussion of privatization is relevant as the MTA heads into its next capital program for years 2000-2004. The capital budget for the entire MTA system for 1995-1999 is almost \$12 billion. This figure includes infrastructure and rolling stock needs. The MTA network suffered from a lack of maintenance in the 1970s, and there is still a great need to repair and to maintain infrastructure, as well as to expand the system. Three capital construction projects in the planning phases, which the MTA is either lead agency or involved with, *Access to the Region's Core*, *Manhattan East Side Alternatives*, and *Long Island Rail Road East Side Access*, are estimated to cost upwards of \$13.4 billion. Traditional sources are inadequate to meet the maintenance, infrastructure, and expansion needs of the MTA system. New York State and New York City capital assistance has dropped in real terms over the last ten years. There may be private partnerships that can contribute funds for the MTA's capital needs.

Public private partnerships for public transportation projects are relevant, especially in the context of Federal transportation policy. The Transportation Equity Act for the 21<sup>st</sup> Century (TEA-21), the recently enacted Federal transportation act, allocates Federal tax monies for transportation projects. The act supports the use of public private partnerships through its new program, the Transportation Infrastructure Finance and Innovation Act (TIFIA). Under TIFIA, the Federal Department of Transportation will assist public private partnership developments with capital market access by providing loans to support up to 33% of the project costs. The Federal Transit Administration will grant to such partnerships access to loans with terms more flexible than would be available in the private market. Hence, TIFIA acts in support of the use of private partnerships.

Given that the MTA faces many capital needs and limited funding, and given that TEA-21 supports innovative private participation, the MTA might benefit from public private partnerships to introduce new funding sources for capital development. Also, in light of its current operating funding challenges, the MTA might benefit from privatizing some of its services. These issues will be explored in the pages which follow.

## PRIVATIZATION OF PUBLIC TRANSPORTATION SERVICES

### Arguments For and Against Privatizing Services

Privatization of public transportation can take many forms. A direct sale of state-owned and operated services to the highest private bidder, who assumes operations, is one form. Generally, private service providers then operate in regulated or unregulated markets. A regulated market is one in which a local authority retains some controls over aspects of service, such as service levels or fares. Another form of privatization is the contracting out of services. In this form, a public transportation agency requests bids for service provision from a private operator. Service levels and fare policies are prescribed, and private providers compete to propose the lowest price for operations. In the United States, the state or municipal agency usually owns the infrastructure for the given service, like buses and rail rights-of-way, and the service provider is responsible for staffing and maintaining the rolling stock.

Transportation experts point to the presumed higher efficiency of the private sector over the public sector. Gomez-Ibanez and Meyer argue that the motivation for contracting out state services is the belief that the private sector, being profit-motivated, is inherently more efficient than the public sector. The private service provider may be more customer oriented and cost conscious than the public agency, because passenger revenue determines profit.<sup>5</sup>

Further, the public sector is inherently restricted in its ability to operate productively because of its institutional structure, say others. Conventional wisdom shows that private companies are organized to be most efficient in meeting their objectives.<sup>6</sup> The argument for privatization of public transportation services is that private service providers can supply public transportation services with lower costs, higher efficiency, and better customer service than the public sector.

One of the most compelling arguments for privatizing public transportation services is to cut the cost of salaries. Economists argue that public employee salaries are artificially high and that private operators are able to expend less on salaries. Salaries and benefits together are the largest expenditures of public transportation agencies' operating budgets. For example, of the total \$853.9 million annual cost for running NYC Transit buses, salaries and wages account for \$609.5 million, which is over 70% of the budget. Private service providers are able to employ part-time workers and pay lower salaries than public agencies. Through the employment of part-time employees, private service

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<sup>5</sup> Gomez-Ibanez, p. 3.

<sup>6</sup> Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, (Summer 1997), p. 76.

providers effectively avoid paying benefits packages. Private firms manifest lower operating costs through the employment of non-union laborers.

However, employment of non-union laborers may not be a long-term solution. If a public agency breaks its relationship with a union and replaces public operations with private operations, will it realize cost savings over the long term? Given time, the unions will reappear and the same high cost of labor will be evident. This is an argument for working towards greater efficiency and productivity with current employees.

Assuming that private providers are able to perform the same level of service for lower costs, privatizing public transportation operations is still a complex endeavor. Contracting out or wholly privatizing a public service must be monitored so as to ensure quality and levels of service. Employee contractual issues need to be explored. Many questions arise. Is the net cost savings of privatizing a public-operated service greater than the increase in unemployment and severance payments to displaced workers? If the state discontinues subsidizing services, will the burden of financing be transferred to the users of the service through higher fares? Who pays when the cost of operating a private service exceeds its income? Is it in the best interests of the riding public to allow the responsibility of route planning to be market driven? Also, since private companies are profit motivated, how are less financially attractive services ensured? A bus line, for example, may not be profitable but may be necessary public transportation in a service area.

Whether to subsidize public transportation is an ethical issue. Public transportation is a public good which serves the mobility needs of many populations including people who are unable to afford or unable to operate private automobiles. Public transportation services are also an integral aspect of urban life and, as such, have been supported with public subsidies. Public subsidies were invested in public transportation systems to maintain and expand services when services were no longer profitable and companies were going out of business. Low fares did not cover operating expenses. Public subsidization is defended by the social argument for preserving affordable fares.<sup>7</sup> Public transportation serves the greater good by reducing the reliance on private vehicle use, thus protecting the environment by reducing auto congestion and emissions. Does public transportation rightfully belong in the private, market-driven sector?

Also, public transportation operations currently cross-subsidize. Profits from popular routes are used to subsidize less lucrative routes. Would that policy remain under a profit-motivated company? Author Elliot D. Sclar argues that privatizing public transportation prioritizes profit generation and not cross-subsidization.<sup>8</sup> Generating a profit is not the goal of public transportation; providing a public service is the goal. The

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<sup>7</sup> Ibid, p. 68.

<sup>8</sup> Elliot D. Sclar, K. H. Schaeffer, and Robert Brandwein, "The Emperor's New Clothes, Transit Privatization and Public Policy," *Economic Policy Institute*, p. 1.

objective of privatization is to reduce tax expenditures, which subsidize public transportation operations. Yet, public transportation systems are public goods which meet the needs of transit-dependent people, reduce congestion, reduce pollution, and contribute to the economic efficiency of an urban area.<sup>9</sup> Privatization is not a simple solution for public transportation's financial difficulties.

### **The History of Privatization in Public Transportation**

Private industry initiated transportation for the public as a market-driven, for-profit operation in the United States in the 1800s. When high operating costs and dropping ridership threatened the continuance of public transportation services earlier in this century, local and state governments stepped in and assumed financial and operating responsibility for public transportation in order to maintain mass transit as a public service. Gomez-Ibanez and Meyer give a good explanation of this process in *Going Private*. The stages in the public transportation privatization-regulation cycle begin with the entrepreneurial stage, when private companies provide for-profit services to meet the growing demand for convenient transportation in and out of the central business districts of developing cities.

The next phase, consolidation, is the creation of monopolies. Following consolidation is government regulation of fares and franchises. Then, transportation providers experience a decline in profitability, which leads to the withdrawal of capital and services. The public sector takes over and infuses subsidies. Efficiency declines under public administration, and what follows is a dilemma of subsidy cuts, fare increases, and service cuts. The final stage, as defined by Gomez-Ibanez and Meyer, is privatization.<sup>10</sup> Privatization is chosen by public authorities under the assumption that private agencies are able to operate transportation services more efficiently than public agencies. This is a simplified version of history, but it puts the public transportation privatization cycle into context.

New York City experienced this first stage of private ownership and operation of public transportation in the middle of the 19<sup>th</sup> Century with privately operated horse drawn carriages, elevated rail, and electric trolleys. New York public transportation experienced the stage of public takeover in the middle of the 20<sup>th</sup> Century, when New York City began to assume operations for the then private subway system.

From the 1970s until recently, the stage most representative of the MTA was the period of efficiency declines, subsidy cuts, fare increases, and service cuts. This trend of fare increases and service cuts has only recently been reversed at the MTA. Beginning in July 1997, the two-fare zone for bus and subway riders was eliminated with the introduction of the MetroCard free intermodal transfer. Ridership increased that year.

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<sup>9</sup> Ibid.

<sup>10</sup> Gomez-Ibanez, p. 17.

Because of a large increase in ridership, NYC Transit realized revenue above its projections. The additional funds were allocated to unlimited ride passes, which were introduced in 1998. Ridership continued to grow. At the end of 1998, NYC Transit again under-estimated ridership growth and revenue grew. NYC Transit added \$56 million of new bus and subway services to meet the growing demand. It is possible that the MTA will add a new chapter to the cycle of ownership and regulation of public transportation by avoiding the privatization stage and creating a stage of state agency efficiency and service increases.

Striking differences in the experiences of developing countries and developed countries are notable in this cycle. In developing countries, many service providers are still in stage one, the entrepreneurial stage. In Mexico City, for example, small bus services are owned and operated privately with little government oversight. The majority of the older public transportation agencies in the United States are in the latter stages of declining efficiency, subsidy cuts, fare increases, and service cuts. Because this paper looks at New York City, its focus is on agencies in the developed world for a comparative analysis.

### **The Politics of Privatization**

As discussed above, privatization of public services raises political and social issues, as well as financial issues. The consequences of privatization on the users of a public service are important. The results of privatization for public employees are also important.

Union members are constituents, and unions are political lobby organizations. Public transportation unions do not want to see their contracts let to private providers. Because the MTA is a state agency, the legislators responsible for the direction of state services closely monitor and influence the MTA board decisions. "Privatization" was identified earlier in this paper as a political and financial buzzword, which has great ramifications for the users of the services, the providers of the system, and the financiers (the taxpayers) of the system. New York State politicians keep a watchful eye on the MTA because millions of voters can be influenced by the quality of the services provided.

Even when privatization of services is justified by cost-effectiveness and decreases in expenditures, politics may prevent a plan to privatize public transportation services. Where transit agencies employ large numbers of people, privatizing services may not be easily accepted. Privatization may be politically unacceptable.

Legislators react to MTA decisions. New York State Assembly bill A08017, originally created in 1997, is a direct response to the MTA's decision to contract the services of one company, Lockheed International, for data analysis. The bill specifically refers to the MTA's need to award contracts on a cost-effective basis and creates a

privatization advisory board to oversee the MTA.<sup>11</sup> Justification for this legislation is listed as, "The MTA has recently decided to contract out its data services to Lockheed International. This decision is not supported by a true comparison of costs or benefits. The MTA is a major employer in the metropolitan area, and effective legislation is needed to ensure that its decisions are truly in the best interests of the region's economy. . . ."<sup>12</sup>

The MTA justification for using Lockheed International versus in-house employees is to save money while focusing on its core competency, operating public transportation services. According to the Minutes of the MTA Finance Committee meeting of July 23, 1998, the potential savings to the MTA for this contract are \$4.9 million over the seven year term of the contract.<sup>13</sup>

The New York State Senate version of the privatization bill, S4198, takes the issue a bit further and reflects the later discussed concerns of the British government in contracting out the London Underground Limited (London Underground) services, in terms of accountability. "While often assumed to be a cost-saving solution, contracting out services performed by the public workforce often result in higher costs and a loss of accountability, thus creating more fiscal problems to state and local governments."<sup>14</sup>

In both bills, a privatization board is proposed to oversee MTA operations. The role of the existing MTA board is to ensure that MTA contracts are awarded on a cost-effective basis, and a privatization advisory board would be a duplication of these responsibilities. Another option for New York State and the MTA may be to follow the example of the State of Massachusetts.

Massachusetts is also dealing with privatization issues. In this case, Massachusetts legislated oversight of proposals to privatize the services of state agencies to the Office of the State Auditor. Privatization proposals are strictly reviewed in an attempt to balance the costs and benefits of the plans. All privatization contracts must be approved by the State Auditor who determines whether the services will be less costly than services provided by the state. Privately provided services must be of equal or better quality than publicly provided services.

The State Auditor halted the Massachusetts Bay Transportation Authority (MBTA) in its plans to privatize the operation and maintenance of bus routes and to privatize bus shelter maintenance. In the case of the MBTA's 1997 proposal to contract out its public operations, the Auditor found that the proposal would cost the MBTA more

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<sup>11</sup> New York State Assembly web site at <http://assembly.state.ny.us> (July 22, 1998).

<sup>12</sup> Ibid.

<sup>13</sup> Minutes of the MTA Finance Committee Meeting, July 23, 1998, p. 4.

<sup>14</sup> New York State Senate web site at <http://senate.state.ny.us> (July 22, 1998).

than its current operations. Unaccounted for severance payments to displaced workers, incentive payments, and unsubstantiated savings led the Auditor to determine that the proposal was incomplete and incorrect. In the case of bus shelter maintenance, cost estimates were incomplete.<sup>15</sup> However, the MBTA successfully proposed the privatization of the activities of its real estate department. The State Auditor found that service would be retained at levels met by public management and cost savings would occur, albeit at a minor savings of \$206,257 over five years.

This type of check on the contracting out of services might be considered a more realistic approach to dealing with the political ramifications of privatization than a "privatization board" like that proposed in the New York State Assembly and Senate legislation. Neither bill passed in 1998. Regardless of whether the New York State Assembly or Senate bills are eventually passed into legislation, the intervention of state legislatures indicates the politics the MTA will confront if it chooses to privatize.

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<sup>15</sup> Joe DeNucci, Massachusetts State Auditor, "DeNucci Returns MBTA Bus Service Privatization due to Failure to Document Savings and Quality," Press Release, May 16, 1998, p. 1.



## **PRIVATIZING SERVICES – THE EFFICIENCY, SUBSIDY ARGUMENTS**

Municipal bus services are contracted out more often than rail services. Bus services are more flexible than train services and more municipalities have bus services. Contracting out means that a local government owns and operates its public transportation system and offers it by bid to private companies for operations. The goal in contracting out the service is to save on costs by using a more efficient provider than the public sector. One underlying assumption is that private companies, being profit-motivated and customer-oriented, are able to cut costs while delivering quality service. Another important assumption is that private market competition among transport providers will follow, and contract price to the public transportation agency will decline as a result. One U.S. city has reaped those rewards through a successful process of contracting out.

### **The Indianapolis Experience - Contracting Out**

Indianapolis Mayor Stephen Goldsmith is credited with re-inventing his city's government. During his tenure, bus service operations have been let to competitive bid, along with other public services in the city, such as garbage collection and street repair. As of 1997, Indianapolis Public Transportation Corporation (Metro) operated an average of 220 buses, serving a population of 950,000. The operating budget for buses and paratransit for Metro for 1999 is \$28 million. The Metro system passed into the stage of efficiency declines in the early 1990s. This stage is defined by subsidy cuts, fare increases, and service cuts. The City of Indianapolis and Metro management decided to contract out bus services. The goal of contracting out the bus services was to increase the quality of service while reducing the cost of operations.

Metro prepared for contracting out bus services by decreasing its workforce through attrition. It then contracted out ten routes in 1995. As a municipal corporation, Metro is subject to the local authorities. In order to avoid labor issues and increase the number of routes contracted out, Mayor Stephen Goldsmith lobbied the Indiana state legislature to give its share of the Metro subsidy to the City of Indianapolis government. Metro was forced to cut part of its service and the City of Indianapolis then became the contracting agency.

Indianapolis then published a request for bids for the reduced service, which consists of weekend and less popular routes. Metro put in a bid and won the city's contract. Metro was able to bring in the same service at a lower cost through negotiating a lower starting salary with its employees. Metro also reduced its number of employees when the city privately contracted oversight of the bus systems. This group is the Office of Mobility Management and is responsible for system wide planning, marketing, customer service, as well as oversight.

The City of Indianapolis and the public transportation agency successfully increased efficiency and service without increasing fares. In their 1997 article "Impacts of

Privatization on the Performance of Urban Transit Systems,” authors Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham explored the experience of the Indianapolis Transit System in contracting out its bus routes. They determined that privatizing the operation of the bus service did save money, as well as increase operating efficiency. Also, because Indianapolis maintained oversight of system planning and service levels of the system, instead of deregulating bus service, service levels were sustained.

How the success of contracting out is measured is critical to the discussion of the benefits of privatizing services. In the Indianapolis example, several performance indicators, versus simply subsidy savings, for the Indianapolis bus system were studied. The indicators were labor productivity, vehicle utilization, cost-efficiency, service utilization, system revenue generation, and safety. Labor productivity and cost-efficiency improved markedly from 1994 through 1997. Labor productivity, measured as total vehicle miles over total employees, rose from 1,254 to 2,013 miles, and cost-efficiency, total vehicle miles divided by operating expenses, rose from 0.283 to 0.346 with privatization.<sup>16</sup>

All but one of the seven performance indicators improved under privatization. Service utilization, defined as passengers per total vehicle miles, dropped. The ratio of service utilization decreased, but vehicle miles operated and number of passengers both increased in the period of the study. This drop in the ratio may be explained by poor route planning, said the researchers. The authors suggested that route planners changed or expanded routes to cover transit-captive riders that were not served.<sup>17</sup>

The transition to private service providers has not been perfectly smooth. The local area transit workers union protested the plan to contract out and filed a grievance against Metro. What is more subtle is the break in trust between the union and Metro and the resulting resentment.<sup>18</sup>

With the exception of the labor issues, the Indianapolis experiment was successful. Most recently, Metro established a new, privately contracted route, which provides additional service.<sup>19</sup> In 1995, Metro experienced its first ridership gains in ten years, due in part to the success of the contracted out routes.<sup>20</sup> The Indianapolis bus experience has been beneficial to the city with increased ridership, increased efficiency, and decreased cost.

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<sup>16</sup> Karlaftis, p. 73.

<sup>17</sup> Ibid.

<sup>18</sup> Jill Henry, Interview with Author, (January 1999).

<sup>19</sup> <http://indygov.org/mayor> November 1998.

<sup>20</sup> Karlaftis, p. 71.

## The British Experience

London Bus, British Rail, and London Underground have all undergone some type of privatization in recent years. London Bus has been contracted out with regulation maintained by London Regional Transport (London Transport). British Rail has been wholly sold off and is privately operated. Plans for a private partnership for London Underground are on the drawing table. The British experience with privatization is relevant to the MTA because of the similar age, size, and history of the British and American systems.

### *London Bus - The Case for Managed Competition*

London Bus is currently comprised of 5,000 buses on 700 routes, which carry four million passengers per day. (NYC Transit bus operates 4,046 buses on 234 routes with a daily ridership of 2 million.) In 1985 London Bus Limited (London Bus), a subsidiary of London Transport, embarked on a plan to contract out and privatize its bus fleet. Routes are contracted out to bus companies that assume operations. London Transport first divided its system into 12 smaller area companies, contracted out those smaller company routes, and then sold the area companies as operating companies. The goals of contracting out were to use a more efficient provider and to build competition for contracts.

Some reasons for the change from a publicly owned and operated bus fleet to a privately owned and operated bus fleet were that it was believed that the public system stifled innovation, protected outdated industrial practices, and cost the taxpayer too much.<sup>21</sup> Ridership began to drop in the mid-1950s for the bus industry in the UK. By the 1970s, 25% of the ridership had been lost, and subsidies more than doubled.<sup>22</sup> Under the Thatcher administration, which came to power in 1979, many state owned companies were privatized and contracted out to private operators.

London Transport retains regulatory responsibility for determining routes, frequencies, vehicle specifications, fares, and ticket sales. London Transport determines a route and needed service levels and then opens the route to competitive bid. The lowest price bidder wins the contract. The London Bus contracts are currently let on a net cost basis. Net cost contracts are let by bid and then all revenue generated above the bid price is retained by the contractor.

Net cost contracts, which are used in London, and gross cost contracts, which are used in Indianapolis, have particular issues in terms of competition and payment. Gross cost contracts include all the costs of operations in the bid price. Service suppliers are requested to bid competitively for a fixed price contract, which does not consider ridership

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<sup>21</sup> Bayliss, David, "Bus Privatization in Great Britain," *Proc. Instn Civ. Engrs Transport*, Paper 11362 (May 1997), p. 81.

<sup>22</sup> *Ibid.*

fare revenue. Service levels, route definition, and service frequency are specified by the contracting agency. Fees and penalties are built into the contract with the provider to ensure service levels. The incentive to the private service provider is to be cost-effective so as to deliver services at a price below the contract price, hence making a greater profit. In a gross cost contract, passenger fare revenue is collected by the regulatory agency, which uses it to pay for the privately operated service. The responsibility for generating greater ridership through better route planning and other techniques is the contracting agency's.

In the net cost contract, service levels and route definition are included in the contract. Like the gross cost contract, the contracting agency specifies services and requests competitive bids for the contract. Unlike gross cost contracting, the service provider of the net cost contract receives fare revenue over a fare level set by the contracting agency. This additional revenue is profit to the contracting agency. The incentive is to attract ridership to generate fare revenue above the contract price. Increased ridership is beneficial to the service provider and the general public.

However, net cost contracts may deter small service operators that may not be able to assume revenue risk up front while developing ridership. Deterrence of small operators is bad for competition. Also a problem with net cost contracts is fare collection. Some riders have reduced fares and monthly passes which are flashed at the drivers as opposed to collected by the drivers. It may be difficult to determine the ridership revenue by bus route.

In terms of operating efficiency, London Transport reports a strong reduction in vehicle cost per kilometer. From 1985 to 1996, the price per vehicle kilometer dropped 45% and costs per passenger trip fell by nearly a third.<sup>23</sup> Another important trend is the increase in London Bus ridership of 8% since 1985, the first year of privatization. There have been significant benefits to riders from the privatization of London Bus. On-time performance has improved. Excess waiting time has decreased.

Private contracting has led to lower costs and lower subsidies for London Bus. In this respect, London Transport has been successful in achieving a decrease in subsidies of 70% since 1985.<sup>24</sup> Also, new bus purchasing is no longer limited by state budgeting. Companies are only limited by their own investment abilities.

Subsidy savings are not necessarily the sole determinant of success for privatization. In Indianapolis, subsidies were cut and new services were added. Because of the lower subsidies, the British example is considered a success. However, there is at least one indicator that points to a lack of success from the riders' perspective in Britain.

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<sup>23</sup> "Buses in London: A Comparison with the rest of Great Britain," *London Transport Planning*, (January 1998), p. 8-9.

<sup>24</sup> *Ibid*, p. 15.

The fares, one of the factors that need to be weighed in evaluating privatization, have increased. London Bus fares have increased dramatically from 1985 to 1996/97. In constant prices, adjusted for inflation, fares on London Bus have increased 38%.<sup>25</sup> For the same period of 1985 to 1996/97, NYC Transit fares increased 50% in real terms from \$1.00 to \$1.50. Adjusted for inflation, NYC Transit fares have increased 9%.<sup>26</sup>

Another indicator of long term success is growth in competition for contracts. Competition among operators for route contracts increases the chances of financial success of London Transport's privatization plan. Will there be competition over the long-term? It is in the best interest of the private provider to build a monopoly in the market and decrease competition in order to become sole provider. As the sole service provider, the private company may then demand a higher price for its services.

In the New York City region, there is an example of contracting out of bus service where competition has decreased over time. The number of private companies operating bus routes in Westchester County, New York, has steadily declined from 16 in 1975, to eight in 1985, to four in 1998.<sup>27</sup> Competition for contracts must be fostered in order for the real purchase price of services from government to decrease, or an agency is simply replacing a non-profit monopoly with a for-profit monopoly. Professor Peter White states in his talk, "The Current Role of Tendered Bus Services in London," that the average number of bids received for bus contracts in London decreased from 7 in 1995 to 3 in late 1996.<sup>28</sup> This trend may cause the bid price for contracts to grow; hence, London Transport will save less money on subsidies in the long term.

The London Regional Passengers Committee (LRPC), which has a similar mandate to that of the Permanent Citizens Advisory Committee, agrees that the privatization of London Bus has been comparatively better than in other areas of the country. For instance, outside of London, the buses have been both deregulated and privatized versus contracted out. Service levels were not ensured by a public agency, and passenger journeys decreased by 38% from 1986 to 1996/97 outside of London.<sup>29</sup> This experience demonstrates the case for contracting out while retaining a public oversight authority.

The London Bus experience is a mixed success for the agency and riders. Although subsidies to the London Bus have been cut, fares have risen dramatically. Service levels

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<sup>25</sup> Bus and Coach Statistics Great Britain, 1996/97, *Department of the Environment Transport and the Regions*, p. 11.

<sup>26</sup> Assuming a three percent rate of inflation.

<sup>27</sup> Sclar, p. 19.

<sup>28</sup> White, Peter, "The Current Role of Tendered Bus Services in London," (Lecture at Westminster, August 1998).

<sup>29</sup> Bus and Coach Statistics, p. 9.

have been ensured to the benefit of the riders, but competition for service contracts is decreasing to the detriment of the contracting agency.

### *British Rail - Sale and Regulation of Public Services*

The system chosen for privatizing British Rail, the national long distance and commuter rail network of the UK, is complex. The goals of privatization were to create revenue through the sale of the system, increase efficiency, and shrink government, while maintaining service. One change of policy from a publicly subsidized and publicly operated rail system to a privately operated system is that the private companies have the ability to plan for the financial future and invest heavily up front. Under the public regime, annual funding levels were uncertain and limited.

The British Rail infrastructure operator and the train operators were split into different companies. Railtrack is the private owner of the infrastructure, generating income by renting stations and tracks to the train operator companies. Rail passenger service was divided into 25 franchises and competitively contracted out.

The Franchise Director retains the regulatory role of British Rail and determines fares and service levels. Levels of passenger service include frequency of trains, which stations are served, and maximum journey time. The Franchise Director must approve a proposed service closure. The contractors of service are known as Train Operating Companies (TOCs). They lease the rolling stock from Rolling Stock Leasing Companies (ROSCOs). Railtrack and the TOCs still receive annual subsidies for operations from the government.

The success of the sale and private operations has yet to be determined. In terms of system service, the evaluation seems to be bleak. According to the publication *Save Our Railway*, "Privatization has left us with an unstable and fragmented network, where too much public subsidy is leaking out as excess profit, and too little is being invested."<sup>30</sup> Some TOCs will not hold connections for services run by other providers, although one estimate of rail users states that one third of inter-city passenger trips involves a transfer of trains.<sup>31</sup> The Franchise Director may assign connections as deemed necessary and some connections are specified in the service requirements. The Office of Passenger Rail Franchising (OPRAF), which oversees the train operators for the government, released statistics on the performance of the passenger rail network for the two years ending March 31, 1998. Generally, services and ridership are growing, but punctuality is declining.

There are policy regulation checks and balances on the privatized British Rail structure. The Franchise Director may penalize a TOC for non-compliance with service

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<sup>30</sup> "Britain's Railway, The Impact of Privatization, The Way Forward," *Save Our Railways*, (January 1998), p. 2.

<sup>31</sup> *Ibid*, p. 6.

specifications. Another check on the system is the awarding of incentive payments to Railtrack, the infrastructure company, for improving performance. A new balance for the operations of the railroads is the involvement of private investors and market confidence. Poor performance, publicly announced by OPRAF, may affect investment and shareholder support in the train operating companies.

Also at issue is whether British Rail actually realized a profit through the sale of the network. The complex nature of the privatization plan cost more than the sell off through legal and other fees and by creating more bureaucracy. Also, the sale of the infrastructure reportedly did not return a profit. The sale price for Railtrack was 2.4 billion British pounds (\$4.08 billion at 1.7 British pounds to \$1)<sup>32</sup> less than its declared value.<sup>33</sup>

Customer complaints are another issue. In response to the unprecedented number of customer complaints received by rail operators in 1997, nearly one million, the national government is establishing a new check on the national rail system. In "A New Deal for Transport: Better for Everyone," a national policy paper published in July 1998, a Strategic Rail Authority for better oversight was established. The Authority will assume the responsibilities of the Office of Passenger Rail Franchising. The Authority will act as a board, with members appointed by and accountable to Government Ministers. The group will address the problems of the privatized railway. The management of passenger rail franchises and subsidies will be the responsibility of the Authority. The group will support integrated transport initiatives. In fact, the government has addressed many other issues related to national transportation policy in "A New Deal for Transport." The paper states that privatization and deregulation of public transportation ignores the public interest by fragmenting the public transportation networks. This evidence supports the public retention of operations and oversight responsibility when contracting out and privatizing services, which is something the British Government plans to do as it reorganizes the London Underground.

#### *London Underground - An Innovative Plan for Financing*

London Underground is a public agency, responsible for the operation and maintenance of the extensive London rapid transit network. London Underground is a wholly owned subsidiary of London Transport, similar to the relationship of NYC Transit and the MTA. London Underground is the oldest underground railway in the world and one of the largest. The London Underground was assumed by public operations in 1933. The twelve line system includes 244 route miles and 267 stations. London Underground carried 832 million passengers in 1997.

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<sup>32</sup> Exchange rate is as of January 1999.

<sup>33</sup> Mary Faraday, "British Rail: A Verdict on Privatization?", *MetroTransit*, (November/December 1997), p. 37.

London Underground has been underfunded and is in need of investment to reach a state of good repair, to expand the system, and to increase services. Public investment in London Underground has decreased continually over the last ten years. The system has deteriorated significantly because of this underfunding, yet ridership has been increasing. Levels of service need to be increased, consequently. In order to meet the growing need, the British government has embarked on a program to set up a public private partnership to meet the maintenance and investment needs of the system.

The immediate investment backlog for the London Underground is 1.6 billion British pounds (\$2.72 billion). However, the system generated an operating surplus, estimated to be 226 million British pounds (\$384 million) in 1998. London Transport's income is estimated to be 1.3 billion British pounds (\$2.21 billion) and cost of operations to be 1.1 billion British pounds (\$1.87 billion) in 1998.<sup>34</sup> As a comparison NYC Transit has estimated that the operating revenue and operating expenses for subways for 1998 to be \$1.4 billion.<sup>35</sup>

London Underground's operating surplus does not take account of the system investment needs. These needs include rolling stock, stations, signaling, civil engineering structures, and track. "Very few of the projects in London Underground's investment program earn a financial return. In general, they are justified by the wider benefits they provide to Tube users and, by encouraging people not to use their cars, their road congestion relief and environmental benefits."<sup>36</sup> The same is true of New York's subway system.

The proposal put forth by the UK Deputy Prime Minister to the House of Commons in March 1998 outlines the government's plans for a public private partnership. The Deputy Prime Minister also included an extra 365 million British pounds (\$621 million) in the next two years for investment in the network and preparation of the partnership. Seven billion British pounds (\$11.9 billion), the estimated investment requirement for the next 15 years, are expected to be invested in the London Underground system through this public private plan.

London Underground will not be wholly sold off, as with other privatization plans. This option has been ruled out as politically unacceptable. The services will remain as one unit versus broken up and sold, like British Rail. As with the case of British Rail and the separation and sale of the infrastructure and franchise operations, the government has little authority to influence the companies to improve the services. The responsibility of

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<sup>34</sup> "An Introduction to London Transport," *London Transport*, (1998), p. 4.

<sup>35</sup> MTA, Materials Being Submitted in Fulfillment of the Requirements of Section 17-A of the State Transportation Law, Appendix B, (July 23, 1998), p. 18.

<sup>36</sup> "London Underground, Public-Private Partnership Facts and Analysis," *Department of the Environment Transport and the Regions*, (March 1998), p. 2.



operations and ownership of the London Underground system will remain in the public sector and continue under the authority of the agency. This includes the operation of trains, management of stations, marketing the network, and ensuring system safety. London Underground will retain responsibility for the ticketing, travelcards, and the system map.

The plan for the inclusion of the private sector includes the awarding of one to three contracts to maintain and modernize the infrastructure of the London Underground. The contracts will be based on groups of lines. Similar to NYC Transit's construction contracts, the contractors will be selected through a competitive bidding process. The contractors' responsibilities will include eliminating London Underground's investment backlog, and maintaining and modernizing the trains and other assets: track, signaling, stations, and escalators. The contracts will include performance-based penalties and incentives. At the end of the contract term, as yet to be determined, the assets will be returned to London Underground.

The burden of financing the much-needed, immediate investment will be given to the private sector through the infrastructure contracts. The contractors have the ability to borrow private capital at much above the government's limited annual public expenditure plans. The contractor's investments will be collected by "appropriate returns," to be achieved via leasing charges, from London Transport over time.<sup>37</sup> The time line for repayment has not yet been determined and the government has stated that more research into the private sector financing of the plan needs to be conducted.

The plan is not without its opponents. In June of 1998, thousands of rail workers went on strike in opposition to the privatization plan. The Rail, Maritime, and Transport Union, which staffs stations, protested the possible worsening of job conditions under the plan and demonstrated itself as a determined force for bargaining. In July, the union went on strike again, closing 15 subway stations, to protest the insecure future of the London Underground.

The London Underground plan will affect employees. Some staff, who currently manage the procurement, installation, and maintenance of hardware, are expected to transfer to the employment of the private contractors. The employment contracts have yet to be outlined, but the government has assured "protection" for the staff.<sup>38</sup>

The goal of the public private partnership for private investment in the maintenance and upgrading of the London Underground is to access private capital markets in order to avoid raising taxes or breaking public expenditure budgets, while increasing service productivity. The program proposed by the Deputy Prime Minister should simplify the contracting of infrastructure contractors and should be cost-effective

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<sup>37</sup> Ibid, p. 9.

<sup>38</sup> Ibid, p. 8.

over the long term. The British government has experience with this type of contracting with highway construction.

In the UK, highway construction has been successfully contracted out in a similar fashion. Design, build, finance, and operate contracts have been let for highway construction. These contracts are for fifteen to twenty years. The goal is to have the private company invest capital up front on construction in order to save money over the long term on maintenance. Risk is transferred from the public agency to the private construction and maintenance company for construction performance. The highway projects are paid back through tolls.<sup>39</sup>

From the riders' perspective, investment in the infrastructure of the system will increase reliability and efficiency of the system. In the short term, riders will be negatively impacted by service disruptions during construction. Hopefully, any inconvenience to the riders will be eclipsed by the service improvements.

Many important issues have yet to be resolved with the public private partnership plan. The current plan is, at best, a rough outline. Net savings, or cost-effectiveness, have not been well defined yet in the plan. New line construction has not been addressed in the plan. The issue of whether the fares will be raised to meet a financing gap has not been resolved. The LRPC has voiced many of these concerns at public hearings on the plan. The British government should take seriously the issues raised by customer organizations, like the LRPC, and incorporate suggestions that will better define the role of the London Underground and better outline expected savings from contracting out the maintenance of infrastructure needs. The London Underground private investment plan is still being developed and will not go into effect until 2000.

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<sup>39</sup> Dr. C. Michael Walton, "Governmental Reform in Transportation: International and Domestic Trends," talk at the Visiting Scholars Seminar sponsored by the University Transportation Research Center Region 2, October 23, 1998.

## Conclusions and Recommendations

Privatization sounds like an easy answer to the tough question of improving service efficiency and of infusing needed financing to public transportation. On the contrary, privatizing services and selling public assets is complicated. Cost savings through competitive bidding have not yet been proven over the long term. The MTA's operating budget is \$5.5 billion a year. It would be difficult to develop a system of successful competition for such an expensive and extensive operation.

Also, as the above discussion illustrates, there is no set formula for successfully contracting out. Each case of privatization and contracting out has had different results. For example, the Indianapolis experience has shown a real savings in subsidies and an increase in service to the riders. At London Bus, fares have risen dramatically under privatization, and net cost contracting discourages competitive participation in the bidding process.

When looking at privatizing services or contracting out, a public transportation agency must be aware of, and look out for, the pitfalls of privatization. Careful consideration needs to be given to the checks and balances placed on a private service. Conclusions can be drawn as to the use of regulation and deregulation. The responsibility of determining routes and frequency of service appears to be best handled by the state agency. The experiences of British Rail and the deregulation of buses outside of London support the argument for state agency control. For example, outside of London, bus service levels have decreased post-deregulation, whereas London Transport ensures this does not happen through oversight of bus services and contracts.

How the success of contracting out is measured is critical to the discussion of the benefits of privatizing services. In the case of the Indianapolis bus experience, researchers highlighted the importance of looking at a number of performance indicators to determine the success of contracting out. The riders' experiences, as well as cost savings and service improvements, were explored. Any plan to privatize NYC Transit or Long Island Bus services should carefully examine what effects of the change will be dealt to riders. In the London Bus plan, services are contracted by route so as to ensure against service cuts of unprofitable routes. This should also be an integral part of any plan to privatize NYC Transit bus.

The political ramifications of privatizing MTA services need to be considered as well. Reaction to the contracting out of the MTA's data processing center, just a small piece of the agency's operations, was strongly negative. Labor opposed the move and the state legislature drafted legislation that would have set up a board to oversee future privatization efforts. Although this legislation did not pass in 1998, it may be reintroduced in the future. Most significantly, when NYC Transit sought to implement one-person train operation on some subway lines, the Transit Workers Union fought to stop the initiative. The agency succeeded only after the issue was brought to arbitration, and even after two years of the program, the union remains opposed to it. Any large scale privatization of

transit or commuter rail operations would face even greater opposition and almost certainly not succeed.

Despite the difficulties inherent in privatizing its services, the MTA may want to consider initiatives similar in scope to the contracting out of the data processing center. Options include privatizing some of the agency's other departments, such as human resources, marketing, and real estate. The MBTA successfully contracted out the activities of its real estate department, and the MTA may find it beneficial to do the same. Any decision should be based on the same analysis that was used in outsourcing the data processing center: whether it is more productive and less expensive to have an outside firm do the work of the departments that are privatized.

Small scale privatization of operating services might be feasible and result in lower operating budgets for some aspects of MTA services. One such aspect of service that might be well suited for private management is new bus routes. NYC Transit and Long Island Bus, which own its buses, might request proposals from private companies to operate its new bus routes. With retention of agency management of routes and service levels, passenger service would be ensured. These routes should be let on a gross cost basis so that fare collection does not determine profit. Like the London Bus example, the MetroCard free transfer and bulk pass discount makes it difficult to determine passenger revenue by route, so a net cost contract would not work. As previously stated, union issues may stand in the way of contracting private workers for bus operations. Union contracts must be explored to determine whether contracting out breaks union agreements.

Another possibility is privatizing the Staten Island Railway (Railway). From an administrative standpoint, the Railway likely would be a good candidate for privatization. Operated by NYC Transit, it is a standalone system and is the smallest of the MTA's operating agencies. It has approximately 300 employees and had operating expenses of \$23 million in 1997.<sup>40</sup> New York City decided in 1998 to eliminate its subsidies for the system, prompting the MTA to threaten to cease operations. Without New York City subsidies, the MTA has incurred additional annual expenses of nearly \$15 million. Because of the financing difficulties facing the Railway, now may be the time to explore whether the system can be privatized.

There are two privatization options for the Staten Island Railway: contracting out its operations or selling off the system. Both options present benefits and problems for NYC Transit. By contracting out the operations of the Railway through a gross cost contract, NYC Transit would most likely save money over its current operating budget. The previous discussion shows that operating subsidies are decreased with privatization of services. However, any contract would have to provide some type of protection for

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<sup>40</sup> MTA, Materials Being Submitted in Fulfillment of the Requirements of Section 17-A of the State Transportation Law, Appendix B, (July 23, 1998), pp. 155 & 160.

current employees, and even with the best of safeguards, workers may still object. The discord could spread to NYC Transit and other MTA agencies.

NYC Transit could sell the Railway to a private company. A sale of the Railway would benefit NYC Transit by creating capital and decreasing its operating budget. A private owner and operator may be more customer oriented than the public agency because profits depend on customer revenue. However, the unions would most likely protest this plan, as well.

How the system would be financed is another issue. Privatization likely would only succeed if the Railway could be made self-sustaining. Considering that New York City does not want to support the system today, it probably would not provide subsidies to a private owner. An option then would be to reinstitute fare collection, which was eliminated in July 1997 for trips not originating at the St. George ferry terminal. Would riders be willing to pay for a system that is now mostly free? Also, what level fare would need to be charged? The Railway required \$15 million in subsidies in 1996, when the fare was \$1.50.<sup>41</sup>

As part of their examination, the MTA and New York City would need to determine whether the issues discussed above can be resolved. Negotiations with the unions could yield an acceptable labor settlement. Financing concerns could be addressed if private operations result in greater operational efficiency than NYC Transit can achieve. The resulting cost savings would lower the subsidy requirement, possibly making it more attractive to New York City to support the system, or make a \$1.50 fare sufficient.

The fare collection issue is also not as significant as it appears to be. It would only affect St. George-bound riders, since the fare is collected for people who enter the system at St. George. In addition, not everyone would actually pay a fare if fare collection were reinstated. Riders with unlimited ride passes would not experience any additional costs, and people who do not take a bus to reach the Railway would be able to use the free bus-to-subway transfer to connect to the subway in Manhattan at no charge. People who use both the subway and a bus or two buses would have to pay an additional fare, but they could purchase an unlimited-ride pass. The only riders who would be negatively affected would be non-commuters who only use the Railway. However, this loss could be offset by any service improvements that might occur as a result of privatization. Any decision on privatizing the Staten Island Railway should be based on this and the other considerations noted. Although these issues may be too much to resolve, it is still worthwhile assessing the benefits and disadvantages of privatizing the Railway. All affected parties - the MTA, New York City, and transit riders - may gain.

Any larger-scale privatization of MTA services is probably not feasible. As discussed, outsourcing has had mixed success in London. Given the similarities between London and New York City, it is this example that is most relevant for the MTA as it

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<sup>41</sup> Ibid, p. 251.

considers the benefits of privatization. Before contracting out its services in any meaningful way, the MTA should carefully monitor the experiences of London.

The MTA may ultimately determine that the only model that will work is the London Underground infrastructure investment plan. The Long Island Rail Road, Metro-North Railroad, and NYC Transit are all burdened by an investment backlog. If the London Underground experiment succeeds, the MTA should consider this approach for its own capital rebuilding program. Station rehabilitation is one candidate. NYC Transit in particular is struggling with its subway station rehabilitation program and has been exploring measures that will help it bring all its stations to a state of good repair in approximately 2020. A partnership with a private company or group of private companies may be beneficial.

However, even the London Underground model presents problems. As public workers are displaced by private laborers, for example, a period of transition and poor maintenance performance may ensue. More London Underground service disruptions may occur due to labor strikes. New York City labor unions are also very powerful and could cause major service disruptions through strikes if the MTA adopts a similar plan.

Privatization is not the only option for decreasing the MTA's operating budget. A restructuring of operations may be necessary to create more savings. There are aspects of the MTA's provision of services that could be more cost-effective and cost-efficient. According to Dr. Robert E. Paaswell, director of the University Transportation Research Center - Region II, a transportation policy think tank established by the Intermodal Surface Transportation Efficiency Act in 1991, there are overhead costs that are difficult to determine in hard figures but may account for wasteful practices at the MTA and other large government agencies. For example, in simple purchase orders, there is perpetual paper work and bureaucracy. There may be some aspects of the business that would be more efficient if privatized, for example inventory management. The MTA found that data services would be better handled by an outside firm. As part of the MTA's 1995-1999 financial plan, savings were actualized by cost cutting. This approach, or outsourcing small departments, may be the answer for the MTA, as opposed to any large scale privatization.

## **PUBLIC PRIVATE PARTNERSHIPS FOR CAPITAL PROJECTS**

This section discusses the many ways in which the private sector can aid public transportation agencies in meeting their capital needs. Options include joint development, financing techniques that leverage private dollars, and turnkey procurement. Joint development strategies are discussed first. In these examples, the private sector has partnered with public transportation to develop properties for commercial and retail use, while contributing to the agencies' goals of providing service to the riders. Where applicable, the MTA's experiences with joint development are described.

Included here is a discussion of financing mechanisms which utilize private monies, such as development impact fees and tax increment financing. Development impact fees and other forms of financing capitalize on the benefit of public transportation access and services to the private sector real estate market. Municipalities, states, and public transportation agencies look to provide opportunities for private financial contributions to system operations and developments by taxing and offering incentives.

The turnkey procurement method utilizes the private sector's ability to coordinate four different aspects of the capital construction development process. Public transportation agencies request that private sector contractors team together to design, build, operate, and maintain public transportation developments. This new method of procurement is promising because it removes redundant administration and speeds up the construction process.

### **Joint Development**

The goal of this section is to illustrate how the MTA might benefit from using joint development private partnerships to augment its construction programs. Joint developments are formalized partnership agreements between public transportation agencies and the private sector in which the private sector contributes financially to public transportation development. Joint development private partnerships are sought in order to generate private funding and participation in capital construction and maintenance for projects. Examples of public transportation agencies that have actively pursued direct private participation are discussed.

As previously stated, the Federal government actively supports the use of private partnerships in transit development. As part of the recent Federal transportation legislation, TEA -21, the Transportation Infrastructure Finance and Innovation Act (TIFIA) program provides for flexible loans for public private partnerships. Also important is the decline in traditional funding sources of state and Federal aid in recent years to public transportation agencies.

Public transportation partnerships are attractive to private developers because transit development offers a locational advantage. Access to public transportation services

can increase property values. Station development partnerships usually need the approval and/or participation of local communities. Public transportation is attractive to local governments because it generates more for the local tax coffers through increases in property values and by creating new or better services for local residents.

### *Washington Metropolitan Area Transit Authority*

The Washington Metropolitan Area Transit Authority (WMATA) is an example of a public transportation agency which has been successful in implementing joint development projects. The WMATA joint development project goal is to partner with private developers who contribute financially to capital and operating costs. Other goals are to increase ridership and enhance tax revenue for localities.

WMATA carries over one million riders per day on its rail and bus systems. When complete, the WMATA Metrorail system will be 103 miles long. By offering properties for private residential, retail, and commercial development near and above transit stations, WMATA hopes to generate more income and have private developers contribute to station construction costs. WMATA sells or leases its land and air rights near or over its rapid transit stations to private developers. Developers fund transit station construction and pay annual rent to WMATA.

The WMATA joint development project process begins with the identification of prospective development sites to be offered by the WMATA General Manager. The General Manager is responsible for overseeing the implementation and evolution of joint development projects. The General Manager works with local jurisdictions to outline local zoning and land use issues concerning the sites. Local governments' legislation and concerns are considered and integrated throughout the selection and development program. After WMATA Board approval of the prospective development sites program, the Real Estate department issues an offering document for publication to solicit private development proposals. The proposals are reviewed by a Contracting Officer-appointed panel, which returns recommendations to the Contracting Officer for negotiation. In the case of more than one proposal, the contract is competitively bid. The authorized proposals are sent to the WMATA Board for approval and contracts are awarded.

WMATA's programs have evolved as it has extended its lines. After more than two decades of success, WMATA revisited and modernized its joint development project policies and generated national interest in its activities. In 1996, WMATA co-sponsored a conference titled, "Transit-Development and Livable Communities." At this symposium of planners, developers, and transit providers, WMATA released an offering document of 33 development sites. The response was excellent, and WMATA has moved to approve its largest joint development project.

WMATA works to make sites in economically depressed areas more attractive to developers and works to find alternatives to the traditional partnership in weak markets. For example, WMATA looks to partner with state and local governments to provide



incentives to spur developments at transit stations as part of the state and local governments' economic development programs. Another alternative is to allow the development of a site without a purchase fee until the time when the development generates profit. WMATA's goal is to encourage development around the station area by allowing the WMATA property to be the anchor site. If sites are not picked up by developers, WMATA will re-advertise the site at a later date.

WMATA has been successful in generating operating revenue and capital construction revenue. Since 1973, the WMATA joint development project has generated over \$60 million for the agency's operating budget. It is estimated that by 2003, the revenue gains will be almost \$150 million. The projects have added 50,000 new riders a day, created 25,000 jobs, and contributed millions of dollars to local taxes. Private development along the rail line has accounted for \$15 billion of development, as estimated by the Metropolitan Washington Council of Governments.<sup>42</sup> The developments range from residential and offices to retail and hotels. For example, at the Bethesda, Maryland, Metrorail Station, more than 12 million square feet of commercial office and retail space, along with 1,000 housing units have been developed next to the station. As a result of its air rights lease to the developer at the Bethesda station, WMATA receives \$1.6 million in annual revenue.<sup>43</sup>

At the Ballston, Virginia Metrorail Station, joint development has been successful for WMATA and the local municipality. Above the station, a 28-story condominium, office complex, and hotel called the Ballston Metro Center was developed. WMATA agreed to a percentage share of the sale of the condominiums versus a lease agreement, which has shown a profit to WMATA of \$200,000 per year in revenues.<sup>44</sup> The Ballston Metro Center development is part of the community's downtown, transit-oriented redevelopment goals. The access to transportation, combined with the dense land use around the Metrorail station, has increased property values at a rent premium of over \$3 per square foot for office space.<sup>45</sup>

#### *Penn Station Redevelopment - Private Participation for Retail Development*

Plans are currently underway to convert the Farley Post Office Building, New York City's main post office, into a "new" Penn Station, for the primary use of Amtrak. Adjacent to the site of the original Penn Station building, which was demolished in the 1960s amid great protest, the new complex will include a vaulted waiting room, in the

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<sup>42</sup> "Metro Means Business in the Washington Metropolitan Area," *Washington Metropolitan Area Transit Authority*, (October 1993).

<sup>43</sup> Michael Bernick and Robert Cervero, *Transit Villages in the 21<sup>st</sup> Century*, (1997), p. 228.

<sup>44</sup> *Ibid*, p. 223.

<sup>45</sup> *Ibid*, p. 224.

manner of the original building, and retail space. Passageways will connect the complex to the current Penn Station across the street, which will be turned over to the Long Island Rail Road and New Jersey Transit. Those agencies currently use the station as a commuter facility. The project is seen locally as an economic development program.

One goal in the redevelopment is to attract private funds up front for the retail aspect of the redevelopment. The Farley Building redevelopment is modeled after the Union Station Redevelopment in Washington, DC. There, 35% of the project was allocated for retailers who contributed to both maintenance and capital construction of the retail space. The Union Station retail component includes restaurants, shops, and movie theatres. Union Station serves Washington Metrorail, Amtrak, Virginia Railway Express, and Maryland Rail Commuter system.

The Farley Building redevelopment project includes 50,000 square feet of retail space with an option for expansion as the U.S. Postal Service operations are reorganized. Retailers will be invited to propose design and management of the space. The private retailers will pay for the fit-out of the retail space and pay for maintenance of their space. The burden of financing the retail aspect is given directly to the private sector.

Unlike the other joint development projects discussed here, the Farley Building redevelopment project is not coordinated by a public transportation agency. It is a New York State economic development project, managed by the Pennsylvania Station Redevelopment Corporation, a subsidiary of the Empire State Development Corporation (ESDC). Financing for the redevelopment will come from a number of different sources. The full project cost is estimated at \$260 million. Thirty-five million dollars are from the MTA's capital budget, the New York State Department of Transportation's share is \$40 million, and the Federal share is \$100 million. The ESDC has given \$25 million and the United States Post Office is to give \$30 million. As noted, the private retailers will fund the retail aspect of the project. The retail services provided in the Farley Building will add convenience to the riders' experience and add safety to the site by increasing numbers of users. Another goal of the ESDC is to attract other development in the neighboring area.

#### *Secaucus Transfer Station - Private Capital and Operating Assistance*

At New Jersey Transit (NJ Transit), there is an example of a public private partnership that features private funding for capital contribution, station maintenance, and rights of way. In addition, NJ Transit will receive on-going rental fees. This project is the new Secaucus Transfer Station, which is located in northeastern New Jersey and will connect the NJ Transit Main/Bergen County/Metro-North Railroad Port Jervis Line and the NJ Transit/Metro-North Railroad Pascack Valley Line with the Northeast Corridor. When work is completed in 2002, riders will be able to transfer to Northeast Corridor trains to reach Penn Station, instead of having to travel to Hoboken and transfer to the Port Authority's PATH rail system. The station, made possible in part by private financial contribution, will be used by about 13,000 daily riders whose commuting time to Manhattan will decrease by 15 minutes. The Allied Junction Corporation, a private

developer, owns the property of the Secaucus Transfer Station and granted NJ Transit the easement for construction work and for the station. Allied Junction plans to develop an \$800 million, 4.7-million square foot office complex above and beside the station. Because of the site's central location and access to transit, the developers expect a high demand for rental space.

The total cost of the station, track realignment, and signal improvements is almost \$483 million. The developers contributed to the capital side of the construction project for the necessary engineering of oversized foundations for the prospective overbuild of the station. When, and if, the developers construct the office complex on the site, they will pay an additional \$59 million to NJ Transit. This fee will go to NJ Transit's capital improvements program. Other capital funds for the project came from MTA Metro-North Railroad, NJ Transit, and the Federal government. Metro-North Railroad's share for design and construction is almost \$56 million, 12% of the total cost, and will be used for aspects of the realignment and improvements which benefit New York riders.

NJ Transit will also receive a portion of the rent, equaling a few cents per square foot per year, and those fees will be used for NJ Transit's operating expenses. The contract between NJ Transit and the developers ensures the future revenue and includes inflation adjustments. The developers will also contribute to the maintenance and utilities of the station. NJ Transit would like to repeat the success of the public private partnership of the Secaucus Station, but there are few opportunities in an established, transit-heavy area for new development.<sup>46</sup>

### *MTA Experiences – Stations*

MTA is looking to redevelop stations with private partnerships. The three examples discussed above illustrate ways in which the MTA can work with private developers to fund station construction and station maintenance projects. Three MTA programs, station redevelopment, station leasing, and Adopt-a-Station, encourage private developers, retailers, and companies to work with the MTA in providing services to riders. In these examples, the MTA is actively pursuing direct private participation in service provision.

### *Metro-North Railroad Harrison Station - Development Swap*

Commuter railroad stations provide opportunities for private partnerships. Beginning in the 1980's, Long Island Rail Road and Metro-North Railroad (Metro-North) began to consider joint development of properties at stations. In 1989, the FTA-sponsored report, "Feasibility Study of Joint/Multiple Use of Development of MTA Commuter Railroad Stations," examined Long Island Rail Road and Metro-North stations, properties, and locality issues to identify areas that might be suitable for joint development. With the assistance of a consultant, the MTA Real Estate Department

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<sup>46</sup> Rick Richmond, Interview with Author, New York, NY, (July 1998).

selected ten sites that could accommodate a joint development project. The report found the development market for the region to be strong, especially on Long Island and in Westchester County, "barring a major national recession."<sup>47</sup> Indeed, the market did hit a recession in the early 1990s and a lack of development activity was a result. The market revived in the mid-1990s, and the MTA followed-up with Metro-North's Harrison Station.

Located in Westchester County on Metro-North's New Haven Line, Harrison Station is considered a good candidate for joint development. In 1995, the MTA published a Request for Expressions of Interest and Qualifications to develop its Harrison Station property. The MTA offered a ground lease of property alongside the railroad station to developers. The goals of the joint development project was to generate revenue and increase ridership for the railroad while enhancing station services. The MTA Real Estate Department coordinated its efforts with the Town of Harrison.

The 1995 effort did not result in a successful development project, and now the MTA is working with the Town of Harrison on a new Request for Proposals. As part of the proposed redevelopment, Metro-North would seek expanded station parking. The developer will build a new parking facility for Metro-North customers, along with other uses on the site. The plan includes a developer payment in lieu of taxes to be split by the Town of Harrison and the MTA. The MTA's share will be used to pay for the parking facility. The development group will amortize the costs of the parking garage until such time that it has paid for construction costs. After the parking facilities are paid off, the MTA will receive direct payments.

The MTA benefits through an increase in parking facilities and long term revenue stream. The Town of Harrison benefits through its share of the project and increased activity associated with development in its downtown. Harrison may also try to capitalize on the success of this development to spur others. This joint development proposal illustrates one way the MTA can benefit from public private partnerships.

#### Metro-North Railroad Peekskill Station - Station Leasing

Retail services at stations can generate rental collections and station maintenance fees. This is another way the MTA can benefit from private partnerships. The MTA Real Estate Department is developing a program to offer station spaces for retail purposes. In areas where the MTA owns the local rail station, retailers and services are invited to rent the entire station, as opposed to smaller concession areas within. In addition to rent, the MTA receives payments for the maintenance of the station. On the Metro-North Railroad Hudson Line, the Peekskill Station has been rented to a restaurant for rental payments and for station maintenance fees. There are many benefits of the program. For example,

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<sup>47</sup> Parsons, Brinckerhoff, Quade & Douglas ZHA, Inc., *Feasibility Study of Joint/Multiple Use of Development of MTA Commuter Railroad Stations*, Prepared for: MTA Real Estate Department, (August 1989), p. 4.

Metro-North saves money on maintenance costs and capital improvements, and stations are safer as there is more utilization of the station during off hours. Metro-North Railroad is looking to increase this program and is marketing spaces throughout the system.

#### NYC Transit Adopt-a-Station - Private Contribution to Maintenance

New York City Transit (NYC Transit) has attempted to make contributing to station maintenance, access improvements, and rehabilitation attractive to private developers. The Adopt-a-Station program seeks to include private partners in subway station rehabilitation. There are two types of NYC Transit Adopt-a-Station partnerships: corporate and neighborhood. The corporate program invites businesses to invest in the capital rehabilitation of stations. The program has existed for nearly 10 years, with two corporate sponsors that have paid for and maintained security cameras to increase station security. The Pfizer Corporation, at the Flushing Avenue Station on the G line in Brooklyn, and the Chase Manhattan Bank, at Broad Street in Manhattan, have both installed security cameras in subway stations.

Packages of needed station improvements are compiled by NYC Transit and presented to prospective sponsors. The corporate sponsors are asked to invest in capital rehabilitation, either full or partial investment. Corporate sponsors are eager to promote their philanthropic activities, and corporate sponsors also like to meet the needs of their employees through station security and maintenance. However, the expense of an entire rehabilitation has been a deterrent to corporate sponsors. For example, the estimated cost of rehabilitating the Lexington Avenue line, 23<sup>rd</sup> Street Station, including fixing a water leak, is approximately \$3 million. The owners of the building next to the station, Met Life, turned down the package as too expensive.

The NYC Transit Adopt-a-Station program team has responded by defining the costs of different aspects of rehabilitation and maintenance in order to give corporate sponsors less expensive alternatives. For example, the cost for extending token booth hours at a station can be \$55,000 per year. Costs for additional cleaning services are \$50,000 per year.

The neighborhood Adopt-a-Station program is similar to the New York City Parks program in which local residents volunteer to maintain the parks. Private groups supplement the services at stations. There are a number of examples of successful neighborhood Adopt-a-Station programs. Merchant associations, high-school groups, and individuals, such as the Broad Channel Civic Association in Queens, the Church Ave Merchants Association in Brooklyn, and Lehman College in the Bronx, participate in maintaining and beautifying stations. Sometimes union rules for station maintenance employees stand in the way of community-backed improvement plans. For example, only union workers are allowed to paint a station.

Neighborhood and corporate Adopt-a-Station programs benefit both the public transportation system through financial contributions and benefit the users of the system

by improving station services. Offering different options to corporate sponsors is a good way to encourage private participation in station rehabilitation; however, more might be done with the corporate Adopt-a-Station.

### **Real Estate Value Capture Mechanisms - Indirect Participation**

As public transportation agencies and municipalities seek to augment their traditional sources of funding for capital construction projects, new forms of financing have been developed which capitalize on the benefits of public transportation on real estate markets. Agencies have looked for opportunities to generate revenue for construction projects outside of the traditional sources. Among these are innovative financing techniques, such as fees and taxes, which exact charges from private property owners and developers to pay for public transportation projects. Benefit assessment districts, tax increment financing, and value capture mechanisms are examples of these techniques. Private developers are also invited to participate in public transportation construction projects by receiving zoning bonuses.

#### *Grand Central Terminal - Revenue-Backed Financing*

Revenue-backed financing was utilized for the renovation of Grand Central Terminal, hub of Metro-North. The goals of the Grand Central Terminal renovation project were to ensure the transportation role of the facility, to preserve the architectural integrity, to revitalize the commercial properties, and to encourage public and private neighborhood activities. As part of the renovation, the MTA has expanded the retail spaces in Grand Central Terminal, as well as offered some previously under-utilized space to restaurateurs. The retail space was expanded to 170,000 square feet from 105,000 square feet.

The expected revenue to the MTA is greatly enhanced by the expansion of the retail space. In 1988, KHW Associates Inc. prepared a program guideline for the redevelopment of Grand Central Terminal, advising that the retail aspect of services be expanded. Retail and advertising leases produced over \$7 million in 1987, and the projected amount to be collected annually from the expanded retail space and services is \$20 million.<sup>48</sup> This additional revenue will help to pay for the costs of the project.

The Grand Central Terminal renovation project was budgeted at \$113.8 million, \$30 million of which came from the MTA capital program for Metro-North related aspects of the renovation. The remaining \$84 million was financed by bonds outside of the MTA capital program. These bonds are MTA Commuter Facilities Revenue Bonds. The bonds, unlike traditional public infrastructure bond issues, are secured by retail, commercial profit. Through rent received in the renovated facilities, the MTA will pay

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<sup>48</sup> KWH Associates, Inc., *Grand Central Terminal Program Guidelines*, Prepared for: Metro-North Commuter Railroad, (1988), p. 34.

back the \$84 million debt. The burden of financing the retail construction is moved from the taxpayer and rider to the retailer.

The MTA enlisted the aid of a development group, GCT Venture, to be responsible for the development and leasing of the retail space. GCT Venture is made up of Michael J. Ewing, a retail developer, and La Salle Partners, a commercial real estate management group. Mr. Ewing and La Salle Partners were also involved in the Washington, DC, Union Station redevelopment. As of the fall of 1998, the expanded retail space at Grand Central Terminal was ninety percent rented.

### *Zoning Bonuses - Incentive Based Agreements*

Development zoning bonuses are offered to developers in exchange for subway station access improvements. In 1972, New York City began extending zoning bonuses to developers that improve subway entrances and incorporate entrances in their developments. In this example of private partnerships, NYC Transit saves costs on its improvements program in exchange for a zoning trade that allows a developer to build larger buildings than zoning otherwise permits. A number of developers have taken advantage of this offer, and in some cases, the developers maintain the spaces after constructing them.

In 1989, the PCAC examined the practice of awarding bonuses to developers in exchange for subway station improvements in its study, "The Subway vs. the Sky: Awarding Private Developers Zoning Bonuses for Improvements to the New York City Subway System."<sup>49</sup> The PCAC found that the system of awarding the bonuses was not working well. In general, the improvements were not well-planned and were done on an ad-hoc basis. In many instances, the developers proposed the improvements to the stations as opposed to the transit agency directing the developers in order to affect the needed improvements. NYC Transit and New York City could better coordinate the program by specifying required subway improvements in the zoning code. The PCAC found that developers were discouraged from participating in the program because working with NYC Transit was difficult and complicated.<sup>50</sup>

Three recommendations for the program were made by the PCAC: end the zoning bonus and collect a transit tax from developers; specify station improvements and approach the station improvements comprehensively; or improve the current system by facilitating negotiations and encouraging developer participation.<sup>51</sup> The PCAC also

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<sup>49</sup> Jennifer Stern, *The Subway vs. The Sky: Awarding Private Developers Zoning Bonuses for Improvements to the New York City Subway System, A Report to the Permanent Citizens Advisory Committee to the MTA*, (July 1989).

<sup>50</sup> *Ibid*, p. viii.

<sup>51</sup> *Ibid*, p. vi.

proposed that a citywide building tax be earmarked for subway station improvements.<sup>52</sup> This tax could be specified for developments which benefit by being located near public transportation stations, like benefit assessment districts.

### *Assessments and Taxes*

Special tax districts, or benefit assessment districts, are specially defined areas where properties are determined to benefit from proximity to transportation development. Additional assessments are levied on property owners to pay for the transit development. This type of financing has been used successfully in Los Angeles and Miami. In Los Angeles, special legislation was passed to create a Southern California Rapid Transit District. In this district, assessments are levied on property owners in direct proportion to the benefits their properties gain from proximity to Metro Rail.<sup>53</sup> The Southern California Rapid Transit District estimates that it will collect \$38.9 million from 1994 to 2003. In Florida, Metropolitan Dade County assesses and collects fees from about 700 properties, which are located near public transportation development. The assessments are adjusted annually to account for new development. These fees have paid for \$7 million of debt service and \$20 million for capital construction.<sup>54</sup> The City of San Francisco imposed a one-time fee of \$5 per square foot for new office developments. This fee funds capital and operating costs. This example of financing is similar to an impact fee exaction.

Tax increment financing districts are districts where taxes are earmarked for transportation development. Tax increment financing, otherwise known as value capture, looks to glean part of the financial benefit of an increase in the property tax base as a result of the transportation development. Tax increment financing monies are used to pay back the capital loans used to pay for the project.

The MTA has looked at value capture mechanisms for Metro-North. Metro-North has opportunities to extend its lines north and build new services. One extension is already under construction. The Harlem Line is growing north to the towns of Amenia and Wassaic in Dutchess County. The MTA commissioned a study of possible value capture opportunities for the properties surrounding the extension. The Regional Plan Association (RPA) was contracted for the study. It is the RPA's responsibility to make suggestions to the MTA as to how the local governments might adopt land use regulations to capture incremental property value gained as a result of the line extension and station development. This study is currently under MTA review. Here, the MTA is aggressively looking to find opportunities for private contribution to its projects, although these contributions are less direct than private participation or public private developments.

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<sup>52</sup> Ibid, p. 47

<sup>53</sup> National Council for Urban Economic Development, Urban Mass Transit Administration, "Moving Towards Joint Development: The Economic Development - Transit Partnership," (August 1989), p. 16.

<sup>54</sup> Ibid.



Also, tax increment financing is a weak financing tool because it is dependent on the real estate market.<sup>55</sup>

### **Private Participation in the Capital Construction Process**

One of the latest transportation-related procurement techniques to gain attention is the turnkey method. Also known as design, build, operate, and maintain (DBOM), the method is another form of public private partnership. With turnkey, the four separate aspects of public transportation development are packaged into a single group procurement. It is the responsibility of the private sector to form teams to design, build, operate, and maintain an entire project. Again, the Federal government has paid attention to this development method. According to the Federal Transportation Administration, "Turnkey is a promising project delivery system to help expedite schedule, control cost, and better allocate and manage implementation risks."<sup>56</sup>

The private sector teams collect revenue from the facility for operating costs and, after the predetermined period of the contract expires, the facility is transferred to the contracting agency. The bundling of procurements is a time saving method which reduces redundant contracting and decreases risk to the agency. Because terms of operation and maintenance are fixed, there are strong incentives for cost-effective development. Each private partner in the development team is pressured by the other to deliver the promised services on time and on budget.

The turnkey procurement method creates a fast development schedule. The shortening of the construction schedule has implications for the cost of the project by simply reducing the consequences of inflation on financing. For example, the FTA estimates that for a \$600 million project, with an additional \$180 million for construction management, \$65 million can be saved. This scenario assumes a construction completion of three years rather than six years and a five percent annual inflation rate.<sup>57</sup> Also, what the following examples illustrate is that soft costs, or administrative costs, are reduced by creating one point of contact for four procurements. The turnkey method benefits riders and municipalities by providing system improvements expeditiously.

The traditional form of development and procurement at the MTA is piecemeal. Each aspect of development is contracted separately: first for design, then construction, with the MTA operating and maintaining the transit developments. Turnkey projects in which the sponsoring agency provides all funding are discussed first and opportunities for private financing follow.

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<sup>55</sup> "Lessons Learned, Turnkey Applications in the Transit Industry," *Federal Transit Administration, U.S. Department of Transportation*, (October 1997), p. 1-21.

<sup>56</sup> *Ibid*, Executive Summary.

<sup>57</sup> *Ibid*, p. 1-8.

### *Hudson-Bergen Light Rail Transit - Public Financing*

The New Jersey Transit (NJ Transit) Hudson-Bergen Light Rail Transit project is the first U.S. example of a turnkey project. The contract uses the design, build, operate, and maintain procurement method. The turnkey consortium method was chosen over traditional contracting for promised time and cost savings.

The planning of the light rail line began in the early 1990s and a solicitation for proposals was issued in 1995. The \$1.1 billion, 10-mile initial phase of the light rail project is financed through the NJ Transit capital program and an FTA Full Funding Grant. The contract, awarded to the 21<sup>st</sup> Century Rail Corporation, includes the private operation and maintenance of the line for 15 years.

The 21<sup>st</sup> Century Rail Corporation is a consortium of engineering, rail, and construction groups, led by Raytheon Infrastructure, Inc. By including the operation and maintenance of the completed line in the contract, the 21<sup>st</sup> Century Rail Corporation is compelled to design and build an excellent system. This works as a check on the construction process, because the 21<sup>st</sup> Century Rail Corporation will be operating its own trains on the tracks. Also, the price of the project has been predetermined. The 21<sup>st</sup> Century Rail Corporation will not be allocated extra costs for overruns. It benefits the company to complete the project on time or early.

Working with one contractor, the 21<sup>st</sup> Century Rail Corporation, for administrative and engineering services is more efficient than traditional procurement for NJ Transit. Simplifying the administration and engineering aspects of the contracts by bundling the procurements saved NJ Transit from three to five percent of the total cost.<sup>58</sup> In real numbers, the estimated savings are \$35 million to \$55 million.

Optimizing the construction schedule for the project has created more savings. Another estimate of the cost savings of the turnkey method over traditional procurements methods for the Hudson-Bergen Light Rail Transit project is savings in excess of \$150 million.<sup>59</sup> Because of its success with the turnkey method on the Hudson-Bergen project, NJ Transit put another turnkey project out to bid, the South Jersey Corridor, in August of 1998. The South Jersey Corridor is to be a light rail system, linking Trenton with Camden.

### *JFK Air Train - Fee Financing*

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<sup>58</sup> Richard Herson, Interview with Author, New York, NY, (July 1998).

<sup>59</sup> Jim Duffy, "Inside New Jersey's \$1.1 Billion Hudson-Bergen DBOM Light Rail Project," *Mass Transit*, (September/October 1998), p. 16.

The Port Authority of New York and New Jersey (Port Authority) chose the turnkey application for development of the John F. Kennedy (JFK) Airport Access rail project. The rail line will be designed, built, operated, and maintained by a group of private developers. The line will run from the Jamaica, Queens, Long Island Rail Road and NYC Transit E, J, Z subway station to JFK International Airport. The rail line will be 8.4 miles with a two-mile loop connecting JFK airline terminals and an extension to the NYC Transit Howard Beach Station on the A line.

The Port Authority set up a think tank of national and international experts to debate the issue of creating a rail system for the airports. Using the turnkey application for rail development was one of the group's suggestions because of the time savings of the procurement method. Another incorporated suggestion was to use similar technology to the pre-existing rail network of the New York City area, as opposed to a monorail.<sup>60</sup>

The entire project cost for the rail and stations is \$1.6 billion. The Airport Passenger Facilities Charge (PFC) fees, the use of which is being contested by the airlines, will pay for the majority of the project and the Port Authority will make up the difference. The PFC is a \$3 fee charged to users of the airport to be used for airport improvements. Some airlines are contesting its use for the project, saying the connections to the transit stations are not airport improvements. (The Port Authority broke ground on the on-airport aspect of the project on September 16, 1998.) The financing not covered by the PFC funds will come from the Port Authority's capital budget. This figure is \$300 million from monies collected from the entire Port Authority system. About \$100 million will come from the two New York Airports. If construction is kept on schedule, the project is expected to come in on budget. Financial incentives and penalties are built into the contract.

The Port Authority issued a Request for Statement of Interest and Qualifications in May 1996. Five teams responded and their plans underwent considerable review. Financial resources and price of product were among the considerations for selecting a turnkey team. The Air Rail Transit Team was selected. The team is made up of Skanska (U.S.A.), Bombardier Transit Corporation, and Perini Corporation. A Port Authority advisory board oversees the development of the project.

The Port Authority has contracted the Air Rail Transit Team to operate the line for 15 years. The Port Authority does not anticipate that it will need to subsidize service operations. Funds for current bus lines to and from JFK parking lots will be given to the rail's operating budget. With these funds and farebox income, the Port Authority expects to generate a profit. The fare will be a premium fare. Tentative discussions have focused on \$2 for airport employees, \$5 for other passengers. Any operating surplus will be used for maintenance. It is estimated that 34,000 passengers per day will use the train.

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<sup>60</sup> Patty Clark, Interview with Author, New York, NY, (July 1998).

There are considerable time savings in using the turnkey method over traditional procurements. Time savings equal cost savings. There are also soft savings in administrative overhead. One important aspect of the organization of the turnkey team structure is that there is one point of contact for communication and accountability.<sup>61</sup>

### **Private Financing and Turnkey**

Private financing for turnkey projects may also be an option for public transportation agencies. Opportunities for increased revenue, outside of toll collection, should be available for the project to be attractive to private financiers. For example, revenue collected from real estate developments, such as the WMATA station developments, off-set the developer's contribution to the capital construction aspect of the station and ensure reimbursement. The method of including private financing in turnkey development is called Super Turnkey. The Federal Transit Administration (FTA) advises public transportation agencies to offer non-transit elements of projects in soliciting private financial support.<sup>62</sup>

#### *Florida High Speed Rail - Partial Private Funding*

The Florida Department of Transportation (FDOT) embarked on a private partnership to build a high speed rail system as one way to meet its public transportation needs. The plan was to build a new high speed rail line which would run from Tampa to Orlando and on to Miami. The system was to be 320 miles long and connect with many tourist attractions and serve airports. The high speed rail plan was in the preliminary phase in January of 1999 when the new Governor of Florida, Jeb Bush, announced that the state would no longer financially support the rail plan. Governor Bush pointed to financial risk to the taxpayers for the project. For now, at least, the Florida high speed rail will not become a reality.

Like the JFK Rail Link and the Hudson-Bergen Light Rail Transit, the Florida high speed rail was to be constructed using the turnkey application. In 1995, a request for proposals was published for a group to design, build, operate, and maintain the high-speed rail system, as well as contribute to financing the project. In 1996, the Florida Overland eXpress (FOX) group was chosen because of its experience with high speed rail technology and financial commitment plan.<sup>63</sup> The FOX Group was led by Fluor Daniel, Inc., an engineering and construction company, and also included Bombardier and GEC Alstom. The contract, still to be negotiated, would have been a standard turnkey, for a

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<sup>61</sup> Ibid.

<sup>62</sup> "Lessons Learned," p. I-7.

<sup>63</sup> Smith, Charles, Manager, High Speed Transportation Program, "Developing Florida's High Speed Rail System: Transportation for the Future," <http://www.dot.state.fl.us/hsrail.overview.htm> (August 31, 1998), p. 1.

fixed price, with penalties built into the contract for delays. The expected date of completion of construction was 2006.

What is remarkable about the FDOT and FOX contract was the private financial participation. The private development consortium, Florida Overland eXpress group, had pledged \$349 million in equity contribution bonds to the project. The total price for the project was \$6.3 billion. The FOX group would have contributed to the purchase of vehicles and paid for design and environmental certification. The state of Florida promised \$70 million per year in infrastructure bonds from 2001 to 2038. The remaining financing was to come from TIFIA Federal credit enhancement, revenue bonds, and infrastructure bonds. Over the life of the project, the \$359 million private investment would have been returned with interest through farebox collection.

The system would have paid back the capital costs through farebox revenue. It is estimated that the debt would have been paid within 20 years of operations. Ridership studies and financing studies estimated that at 8.5 million riders per year, the system would have broken even in 20 years. After the debt was paid and operating revenue exceeded costs, the surplus would have been put into expansion of the system.<sup>64</sup> The operating contract was 40 years with an option to extend the contract.

In this example, the private financing participation was secured through operating revenue. The participation benefits FDOT through transfer of risk to the private consortium. By involving the private developers in the financing of the rail line, an incentive to produce the product on time and on budget is built into the relationship. Also, the private consortium's commitment to the project was secured by the investment.

Unlike traditional commuter rail or bus systems, the Florida high speed rail was to be marketed and operated in a manner similar to air travel. With only seven stations, the rail line would have served intercity trips, not daily commutes. Plans to team with airlines to sell joint tickets were being discussed.<sup>65</sup> Fares would have been competitive with air travel and would have offered premier class, reserved seating.

The Florida high speed rail may, someday, become a reality. Demand for alternatives to highway construction may grow and the high speed rail project may be revisited. Perhaps the rail plan would have been more successful had the private financial commitment been larger and secured by revenues outside of fare collection, like real estate at or near stations.

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<sup>64</sup> Charles Smith, Interview with Author, (January 1999).

<sup>65</sup> Ibid.

## Conclusions and Recommendations

Several opportunities exist for incorporating the private sector into the MTA's capital program. The MTA and its operating agencies can work directly with developers, as the Washington Metropolitan Area Transit Authority has done with its joint development program. In this case, builders fund transit station construction and, or pay annual rent in exchange for obtaining land that they then develop. The retail aspect of the Pennsylvania Station redevelopment project is another example. Here, retailers are financing the costs of constructing and maintaining their space.

Indirect participation from the private sector is another possible approach. Real estate values, for example, generally increase following a transit improvement, and local governments in the MTA service area can use the additional property tax revenue to help pay for the project. Turnkey procurement is also a possibility for the MTA. Many of the agency's prospective projects could use one of these three methods, and given the constrained nature of capital funding, the agency should make as much use of the private sector as possible.

Partnering with private developers would not be new for the MTA. As discussed above, Metro-North is seeking to use private money for improvements at its Harrison and Peekskill Stations. Part of the cost for redeveloping Grand Central Terminal is being paid through rental payments from the expanded retail space. Through its Adopt-A-Station program, NYC Transit has sought to supplement its resources with funding from corporate sponsors. NYC Transit has also exacted payments from developers who plan to construct new buildings near subway stations. As part of the approval for Riverside South, a large-scale development on the Upper West Side of Manhattan, builder Donald Trump agreed to give NYC Transit a maximum of \$12 million to help pay for the reconstruction of the 72<sup>nd</sup> Street/Broadway subway station.

It is encouraging that the MTA agencies are being creative in finding ways to support their capital activities. They have not been as aggressive as they should be. As they seek to rebuild and expand their systems, they should examine both new opportunities and ask more from their private partners.

Developers who want to build near commuter rail and subway stations are one resource that the MTA has not used to its full advantage. For example, accepting \$12 million from Donald Trump for the 72<sup>nd</sup> Street station is not sufficient. His complex will contain several residential buildings and bring thousands of new riders to the already overwhelmed station. Under an earlier plan for the Riverside South site, the MTA would have received approximately \$40 million. The additional money, as well as contributions from other developers who have recently built in the area, could have been used for a more ambitious reconstruction project. Instead of widening the southbound platform at the station, NYC Transit intends only to construct a new entrance north of 72<sup>nd</sup> Street and extend the platforms. Community leaders are not satisfied with this plan, asserting that it will not do nearly enough to address the overcrowding at the station.

The MTA acted similarly when it allowed the Rudin Organization out of an agreement to provide escalators in a building that it is constructing over the Times Square station. As part of agreements reached in 1994, the MTA had the right to require the developer to install and maintain two escalators at the station. In lieu of exercising this requirement, the MTA accepted a \$1.3 million payment, compared to the \$10 million compensation payment that transit staff recommended the agency seek.<sup>66</sup>

In both this case and the Trump example, the MTA was too lenient, illustrating that the situation today is not much different than it was when the PCAC released its 1989 report, "The Subway vs. the Sky." Developers should be required to contribute more to the MTA if their projects affect commuter rail or subway stations. Mandating greater compensation is not inappropriate. Projects such as Riverside South bring many new riders to a facility that may already be inadequate to handle the flow of people who use it. In addition, given the profits that new buildings generate and the amount of money that developers invest in them, exacting higher fees would not be a financial hardship. An additional \$30 million from Donald Trump or \$9 million from the Rudin Organization is a fraction of the overall project cost and is a small price to do business.

The MTA should be aggressive in its dealings with developers and New York City or New York State should consider a legislative solution. One approach could be to require minimum payments from developers who build around commuter rail and subway stations. The amount of the fee could be based on several factors, including the size and value of the project as well as the number of new riders the project would bring to the station. Alternatively, legislation could authorize the creation of transit improvement districts that include all properties within a certain radius of a station. Any new development in this area would be assessed a fee. The revenue collected could be put towards station maintenance, or if it is substantial enough, it could be put into a fund that would be used for station reconstruction.

Tax increment financing is another mechanism that the MTA could use to access private monies. In this case, though, the developers would not pay the MTA directly. Instead, the revenue would come from increases in property tax collections that usually occur after a transit improvement. New Jersey offers an example. In 1996, NJ Transit completed a project that connected its Morris and Essex Line directly into Penn Station, giving riders on this branch a one-seat ride to Manhattan. Property values in the communities near the line rose, augmenting property tax collections without an increase in the tax rates.

The MTA is studying projects that likely would have a similar effect. For example, it plans to bring the LIRR into Grand Central Terminal. Doing so would ease the commute for approximately 50,000 daily riders who work in East Midtown Manhattan but who today cannot directly reach this area. The MTA is also considering constructing a new east

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<sup>66</sup> Press Release, *New York State Senator Franz. S. Leichter*, (May 14, 1998).

side subway that would run under Second Avenue from 125<sup>th</sup> to 63<sup>rd</sup> Streets and then connect into the express tracks of the Broadway line. Again, the gains would be substantial, alleviating the overcrowding on the Lexington Avenue subway line and providing easier access to the subway for tens of thousands of Upper East Side residents.

Both projects would have a dramatic impact on property values in the benefiting communities. Property tax receipts would increase as well. The additional revenue would not be sufficient to pay for the expected twenty percent local share of the projects. The estimated local share for both *East Side Access*, which is the LIRR Grand Central connection, and for the Second Avenue subway project is \$800 million (in 1997 dollars). The MTA should still consider using whatever new collections occur as one funding source. The agency could use the New Jersey example as a guide for estimating the potential increase in property tax revenue. The amount may be substantial, and at a minimum, it would ease the financing pressure such projects pose.

In addition to using the financing mechanisms discussed above, the MTA and its agencies should build on their existing efforts to team directly with developers. Costing out smaller aspects of subway station rehabilitation and maintenance is a good step by NYC Transit towards determining whether it can make its corporate Adopt-A-Station program more successful. The LIRR and Metro-North should consider expanding their adopt-a-station programs as well.

Another example of a partnership that resulted in private contribution to station rehabilitation is the NYC Transit Franklin Street Station. Private contribution to the station was managed by the New York City Economic Development Corporation (EDC). Private developers were requested to make a community contribution in relation to their building deal with New York City. MTA should team with the EDC and other development groups to encourage similar projects.

If Metro-North eventually succeeds with its Harrison Station project, it and the other MTA agencies should explore using this approach more extensively. The agencies could team with New York City and local municipalities served by the railroads to identify prospective sites for development or redevelopment of stations. The goal of inviting private developers to construct stations is to save capital money for other projects and increase property revenue for local areas. Another important goal of any public transportation development should be to bring better services to the public. The Secaucus Transfer station represents the ideal realization of both of these goals as private financial participation has contributed to the construction funding, property revenues will increase with the construction of the new complex, and riders will be better served by a decrease in commuting time of 30 minutes each day.

In an area as densely populated as the tri-state area with a long history of extensive public transportation services, it is difficult to find many new build situations like the Secaucus Transfer Station and Wassauc Extension. New build sites are more attractive to developers than sites with existing properties, because it is more expensive to raze existing



properties than it is to build new. The Secaucus Transfer project and many of the WMATA partnerships are new build opportunities. The MTA may find that attracting developers to built areas located above or near its subway stations and commuter rail stations is difficult. However, there are some opportunities for a project similar to the Secaucus Transfer or the WMATA joint-development program.

One area that is a suitable candidate is the Sunnyside Rail Yard in the Long Island City section of Queens. Sunnyside is a network of rail tracks that are used for train storage and for Amtrak, LIRR, and NJ Transit operations. In the last few years, Long Island City has enjoyed a renaissance, as both commercial and residential developers have sought to take advantage of its central location and proximity to midtown Manhattan. A new complex of residential buildings is being built on the East River, numerous large-scale retail stores have opened in the area recently, and in the 1980s, Citicorp constructed a major office tower that is home to many of its operations.

Developers have turned their attention to the air rights over Sunnyside as a site for a major, mixed-use complex. As part of this complex, a new transportation hub could be built, serving all three MTA agencies, NJ Transit, Amtrak, and trains to both LaGuardia and Kennedy Airports. Such a hub has been discussed and would be a natural extension of a Sunnyside Station that the LIRR plans to build as part of its Grand Central connection. Given the developer interest in the air rights over Sunnyside and in Long Island City as a whole, the station could be financed in a similar fashion to the Secaucus Transfer: largely through private contributions.

Joint development is possible for other projects as well. Metro-North, for example, is considering an extension of its Hudson Line north of Poughkeepsie to the Rhinebeck area. Public private partnerships could be used to build the new stations for this extension. The new station buildings could accommodate other uses, including commercial office space or retail space beyond the typical newsstands or food concessions. In this case, the developer could incorporate Metro-North's facilities into the building at little or no cost to the railroad. As the LIRR and Metro-North look to rebuild or improve their existing stations, they could explore this approach as well. Another option may be to copy the example set by the redevelopment of Pennsylvania Station, in which the retailers and not the sponsoring agency pay for the construction and maintenance of retail space. Using this and the other joint-development techniques discussed would greatly benefit the MTA and its agencies. They would enable the agencies to access private resources to help fund much-needed capital improvements and to free up money for other projects.

The turnkey procurement method would also benefit the MTA and its agencies. As discussed, this approach saves time and money in constructing new rail lines. Several projects under consideration in the MTA region are candidates for this technique. The Second Avenue subway could make use of the design-build aspect of turnkey development.<sup>67</sup> Unlike the Port Authority and NJ Transit, the MTA should not use the

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<sup>67</sup> In 1996, the PCAC explored design, build practices at the MTA and recommended that the MTA consider using the technique in certain situations and avoid using the technique on projects where the

design, build, operate, and maintain (DBOM) method for the Second Avenue subway project. It should operate and maintain the line itself since doing otherwise would fragment its network. The agency probably would still realize some time and cost savings by bundling the design and build aspects of the job, making it worthwhile to examine using this approach. New build projects, which would not share current rights of way – like the JFK Air Rail, are the best candidates for the turnkey procurement method at the MTA. Projects that would be integrated with the current system would not be well-suited to turnkey, because the MTA operates and maintains all of its systems.

Design and build would also be appropriate for a proposed rail link to LaGuardia Airport. This line would operate along the express tracks of the Broadway subway line in Manhattan. It would start at a station below the existing City Hall subway station and run to the Queensboro Plaza N line station. From Queensboro Plaza it would follow one of two routes to the airport. In one alignment, the system would continue along the N line to its terminus at the Ditmars Boulevard station in Astoria. At this point, the system would diverge on separate tracks to the airport. Alternatively, the system would diverge immediately at Queensboro Plaza and run along independent tracks to LaGuardia.

Through a combination of indirect financial participation from private developers, and direct public private partnerships, the MTA and its agencies would be able to achieve more than it can today. It would stretch its capital dollars further, enabling it to undertake critical system rebuilding, maintenance, and expansion projects. In an era of constrained funding, the MTA should explore all opportunities for leveraging private resources, as well as public resources. The agency has had success with some partnerships and developer contributions and should look to repeat and increase those successes.

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construction begins before design is completed. "Contracting Practices at the MTA", *Permanent Citizens Advisory Committee*, (January 1996), p. 21.

## CONCLUSION

Privatization is not a panacea for the financial needs of the MTA. However, in certain circumstances, such as contracting out of non-transportation related operations and developing private partnerships in capital construction programs, private participation saves time and decreases costs. The MTA will have greater success with incorporating private partnership initiatives for its capital program than privatizing service operations on a large scale.

Contracting out service operations to private operators can be a cost savings alternative for inefficient public transportation agencies but can be complicated. Utilizing private service providers for bus services has worked well for Indianapolis. However, at London Bus, many difficulties have arisen with contracting out. Net cost contracting complications, decreasing competition, and increasing fares are problems at London Bus. Successfully contracting out operations is not an easy endeavor.

The greatest economic argument for contracting out services to private providers is the high cost of public employee salaries. Economists argue that public employee salaries are inflated, and unions stand in the way of decreasing public transportation operating costs. The political will of the transportation unions has already been exhibited in the New York State Senate in the form of a proposed privatization bill. This legislation would create a privatization board to oversee the MTA and ensure that any attempts at privatization are strictly scrutinized. Large scale privatization of service operations is not feasible for the MTA, because the transportation workers unions are powerful.

Private public partnerships and real estate value capture mechanisms are promising tools for raising private financing for MTA projects. Private developers are attracted to sites with public transportation access and are encouraged to contribute to station development and maintenance. Formal private partnerships for station development have worked well for the Washington Metropolitan Area Transit Authority (WMATA), and the MTA is working on developing partnerships for its commuter railroad stations. Real estate value capture mechanisms, such as benefit assessment districts and tax increment financing, should be developed for exacting fees from developers that impact MTA services. The MTA should look to partner with New York City or New York State to legislate mechanisms to extract fees from private developers for capital construction and service operations. Long Island Rail Road *East Side Access* is one project that is a good candidate for a benefit assessment district, because real estate on Long Island may become more valuable as a result of increased access to the central business district.

Greater private participation in the procurement method is also promising for time and cost savings. The turnkey method of procurement invites private firms to team for the design, build, operate, and maintenance aspects of transportation development. This method has been successfully implemented at New Jersey Transit and may prove to save costs at the MTA, in certain circumstances. With the turnkey procurement method, there are also opportunities for incorporating private financing, which the MTA should explore.

There are many opportunities for the MTA to generate private capital for construction projects and save costs in the construction process. In an era of constrained financing and great capital needs, the MTA can look to private participation in the development process to supplement public funds. By capitalizing on private partnerships and value capture mechanisms, the MTA can do more to meet its capital construction needs and better meet the needs of the riders.

## **Addendum**

Comments by the London Regional Passengers Committee

p. 14 – London Bus fare increases

“The DETR index used to compute this figure is based on standard single fares – but only a minority of users pay these. The increase in pence received per passenger mile is much less, because of the massive switch to period tickets which mean the marginal cost of each trip is zero.”

p. 14 – Bus service levels outside of London

“ . . . local authorities can (and do) contract for additional services additional to those operated commercially – and account for about 15% of the total . . . There are various factors which have helped LT to retain riders better than elsewhere, but the main one is the difficulty of using cars for many trips in London because of congestion levels and the lack of parking spaces.”

p. 15 – Subsidies to Railtrack

“Railtrack receives no direct subsidies – these are paid to the Train Operating Companies, which in turn rent track access rights from Railtrack.”

p. 15 – Punctuality is declining

“This is partly because of the number of speed restrictions where long-overdue track and infrastructure repairs are under way.”