Lessons to be learned from the Australian “asset recycling” program

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As debate over President Donald Trump’s proposed $1 trillion infrastructure plan continues in Congress and the media, some are proposing that the U.S. look to Australia—specifically, that country’s “asset recycling” program—for a model of how to support a long-term program of badly needed infrastructure investment. While asset recycling may sound like a new invention, it’s simply privatization rebranded with a new name—selling off existing public infrastructure to pay for new infrastructure. In Australia, asset recycling schemes have amounted to expensive loans with long-term concession contracts that have had problematic features.

Introduced in 2014, the Australian asset recycling program ultimately crashed and burned, and the fund itself was formally ended in December 2016. The Tony Abbott government was unable to get enabling legislation and funding for the program through the Senate, which had held extensive hearings on the asset recycling program and raised multiple criticisms of its economics, administrative feasibility, transparency, conceptual soundness, riskiness, fairness, policy impact, and ability to deliver good and necessary public infrastructure.

Our own country’s experience shows that transferring control of public infrastructure to private interests is fraught with problems.

One such example is the privatization of Chicago’s parking meters. In 2009, Chicago signed a 75-year public-private partnership with a consortium of companies for the operation of the city’s 36,000 parking meters. Although the city received $1.15 billion in the deal, Chicago drivers will pay the consortium at least $11.6 billion to park at meters over the life of the contract.[1]

The contact required Chicago to raise parking meter fees by 200 to 800 percent, depending on the area of the city, from 2009 to 2013,[2] which raised parking rates to $7 for two hours of parking in some parts of the city.[3] The contract also requires Chicago to compensate the consortium whenever the city makes decisions that adversely impact the consortium’s ability to collect revenue, such as temporarily closing streets, even for community parades and street fairs.[4] The city is also restricted from making improvements to streets that have meters, such as adding bike lanes or expanding sidewalks, because these projects might “compete” with the meters and decrease corporate revenues. These restrictions severely limit the city’s future ability to accommodate residents, including bicyclists, pedestrians, and transit users.[5] Already, the city has had to pay the consortium $31 million due to these contract provisions.[6]

Another example is the Indiana Toll Road, one of the country’s first large public-private partnerships. The contract contained provisions that forced the state of Indiana to pay

the road's private operators nearly $450,000 in penalties after state officials waived tolls during a flood emergency to help evacuating residents.[7]

Given the troubles with privatization in the U.S., we should be wary of schemes that further embed private interests into plans to rebuild the country's infrastructure. Below are important problems with the Australian asset recycling program that should serve as lessons. Far from being a model to be followed, the Australian program is a model for what should not be done to promote badly needed infrastructure improvements in the U.S.

Asset recycling encourages flawed decision-making and distorts incentives

The Trump Administration has mentioned offering a "bonus" to incentivize state and local governments to sell their assets in order to generate money for new infrastructure. As Gary Cohn, director of Trump's National Economic Council and former president of Goldman Sachs, explained, "The bigger the thing you privatize, the more money we'll give you."[8]

The Australian asset recycling program offered a 15 percent federal subsidy for states and territories that sold existing assets. However, this subsidy encouraged flawed decision-making and distorted incentives. Decisions to privatize existing assets were heavily influenced by the presence of the subsidy.

In 2015, the Northern Territory government, in an attempt to access asset recycling funds, privatized two major public assets, including a lease of Darwin Port to a Chinese company for 99 years without an understanding of where the money would go.[9] Instead of encouraging thorough analysis of whether privatization is truly in the public's interest, the subsidy incentivizes states and local governments to rush and distort decisions with little transparency in an effort to get federal funding.

Asset recycling does long-term damage to public balance sheets

There have been concerns that the Australian asset recycling program has done long-term damage to the government's balance sheet by transferring income-producing assets to the private sector. After reviewing more than a decade of experience in Australia and the United Kingdom, Professor John Quiggin of the University of Queensland concluded: "In reality, most privatizations have reduced public sector net worth, either because the assets have been underpriced, or because the proceeds have been dissipated in current expenditure or economically unsound investment projects."[10]

This dynamic certainly has been true in the U.S. experience as well. As mentioned above, Chicago received $1.15 billion for its parking meters, but drivers will pay the private companies at least $11.6 billion to park over the life of the 75-year contract, revenues which the city will lose out on. Shortly after the deal was signed, Chicago's Inspector General concluded the city significantly undersold the asset.[11]

Asset recycling sets up the potential for unfairness and inequity between states and localities

As the Australian experience shows, there are several ways in which asset recycling sets up the potential for unfairness and inequity between states and localities.

First, the state of Victoria has recently clashed with the Australian federal government over what infrastructure investments qualify for the program. Victoria signed a 50-year lease for the Port of Melbourne but was denied the 15 percent subsidy by the federal government, which insisted that the bonus be used for the already-funded Melbourne Metro rail project rather than the removal of dangerous level crossings, for which the state wanted to use the bonus money.[12]

The federal subsidy can become a political football to incentivize projects that those with power want to build over projects that may be more critical but less popular. The subsidy can also become a valuable way to reward or punish particular states or localities. The Treasurer of Victoria has accused the federal government of withholding the bonus funds for politically motivated reasons.[13]

In the U.S., funds have been poured into pet projects without a careful analysis of actual community needs. In August 2010, Indianapolis leased its almost 3,700 city parking meters in the downtown and Broad Ripple areas to a consortium comprised of Xerox subsidiary Affiliated Computer Services (ACS) and several local companies. The city received a payment of $20 million up front for the 50-year lease. The city then basically engaged in asset recycling by using part of those proceeds to help build a pet project of the former mayor—a privatized $15 million three-story, 350-space garage, which opened in 2013. Five months after opening, the garage was just 5.5 percent full on average and only 20 percent full during weekend evenings, the busiest period. Even with changes in pricing and other factors, the garage still sits nearly empty.[14]

Asset recycling also runs the risk of favoring asset-rich states. In announcing the program he architected, then-federal Treasurer Joe Hockey conceded in 2014 that, as the Sydney Morning Herald put it, “some states would get more money from the [incentive] pool than others because some states had more public assets to sell.”[15] An asset recycling program sets up the very real possibility that states and localities that have assets to sell or assets in the pipeline ready to be sold will see more benefit than areas, such as rural areas, that don’t have as many assets to sell. As with the Trump Administration’s broader infrastructure plan, rural areas stand to lose out on infrastructure investment.

An asset recycling program can set up perverse incentives that can negatively impact cities and states

In 2015, the Australian Senate Economics References Committee conducted hearings around the asset recycling program and produced a report that included the below concerns:[16]

"The committee is concerned about the possibility that **incentives under the Asset Recycling Initiative may encourage privatization without effective public consultation and communication strategies, and without appropriate consideration or analysis of future costs.** The committee strongly encourages governments to conduct proper, **rigorous analysis of the all current and future costs associated with privatization projects.** In addition, **thorough and appropriate public consultation** should be always be undertaken, including consultation around transactions costs and the cost of creating **an appropriate regulatory environment and compliance with those arrangements.**"

The risks and costs that are inherent in any privatization deal are exacerbated by the incentives in an asset recycling program. Rushed decision-making to meet program deadlines, lack of transparency, and high transaction costs are important concerns that experts and lawmakers have expressed about the now-dormant Australian asset recycling program, and the U.S. should take those concerns very seriously before considering a similar program.

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Notes

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