

Another Year, Another Hike in Turnpike Tolls

Another year and another toll increase for users of Pennsylvania's Turnpike system. For the sixth consecutive year, tolls will rise for travelers paying with cash (E-Z Pass fares were not raised in 2012). Turnpike tolls have been boosted to cover the cost of rising bond obligations incurred to satisfy 2007's Act 44 requirement that the Turnpike contribute \$450 million to PennDOT annually.

As we had written in past *Briefs* (*Volume 12, Number 5* and *Volume 13, Number 3*) the Turnpike will need some legislative help to lighten this debt burden as the cycle of issuing debt and raising tolls cannot continue for the fifty years outlined in Act 44. In late 2013 that help arrived with the passing of Act 89 of 2013 which reduces the amount owed by the Turnpike from \$450 million to \$50 million—in the fiscal year (FY) ending in 2022. While any help is welcome, the damage may already have been done.

For FY 2004 the amount of mainline bonds outstanding (those issued against toll revenue) was just over \$1.13 billion¹. In May 2007, before Act 44 was passed, that debt total climbed by 46 percent to reach \$1.7 billion. By May 2013 the amount had jumped above \$7.5 billion—an increase of more than 560 percent over 2004 levels and 350 percent higher than in 2007. With a strategy of borrowing to satisfy Act 44 requirements and using toll revenues to pay them off, the amount of mainline debt will continue to rise dramatically for the foreseeable future. An official from the Turnpike Commission was quoted in news reports that their bond ratings have been solid, so there appears to be little outward worry.

However there are two main reasons to worry. First, interest rates for the past few years have been very low, making borrowing cheap and offering extraordinarily favorable refinancing opportunities. Through its quantitative easing policy, the Federal Reserve has kept interest rates historically quite low purportedly to promote the national economic recovery. This has kept the growth in debt service on these bonds from rising as rapidly as the debt growth itself. In 2004 the debt service on the mainline bonds stood at \$81.1 million before rising to \$111.5 million in 2007 (38 percent). In 2013 that amount swelled

¹ All financial data from 2013 Turnpike Comprehensive Annual Financial Report: http://www.paturndpike.com/geninfo/PTC_CAFR_13-12_final.pdf. The Turnpike Commission's fiscal year ends on May 31.

by 185 percent to \$318.9 million. Thus, the increase to the debt service of these bonds grew by a slower rate than the amount of debt issued. Even though debt service is currently manageable, debt service will inevitably rise as more borrowing is incurred, even with low interest rates, and to make matters worse it is a virtual certainty that interest rates will eventually move higher.

The second reason to worry is that Turnpike traffic levels have been flat over the past decade or so. The mainline Turnpike offers the best route to traverse the southern part of the state, connecting west to east from border to border. Customer demand is highly inelastic in the short run and usage levels do not drop appreciably in the face of price hikes. This is borne out by the data. Since FY 2008 (before the first hike) to FY 2013 there were the six consecutive cash toll increases and yet gross toll revenue increased nearly 33 percent with the total number of vehicles using the Turnpike virtually unchanged (down less than one percent) over the period. To be sure, there must have been some effect on traffic over the period in light of the improvement in the state's economy and the very modest upturn in national economic activity. One would have expected some significant pickup in traffic absent the toll increases. Indeed, the traffic did rise to recover to the 2008 level in 2011 and 2012 but dropped back to 2004 readings in 2013.

But within the years we can see that the growth in gross toll revenue was rising at a decreasing rate. From FY 2009 to FY 2010 gross revenues increased 12.5 percent. Then from FY 2010 to FY 2011 growth was less than 6.5 percent and the increases got smaller from 2011 to 2012 (4.4 percent) and again from 2012 to 2013 (3 percent) despite the constant toll hikes.

Are motorists starting to react negatively to the toll hikes by finding alternative routes to travel? While the number of vehicles has not changed much since FY 2009, within the last three fiscal years the change to the number of passenger vehicles on the Turnpike's roads have been decreasing (up one percent, down 0.16 percent and down 0.77 percent). The number of commercial vehicles using the toll roads over the last three fiscal years has been increasing, albeit at a decreasing rate (3.8 percent, 1.3 percent, and 0.33 percent respectively).

However, a more telling indicator kept by the Turnpike is revenue miles. From FY 2008 to FY 2013, this measure had fallen by 4.5 percent. FY 2009 had the largest fall of nearly 3.75 percent, but FYs 2010 (-0.69), 2012 (-1.19), and 2013 (-0.03) all had setbacks as well. Only 2011 had a modest one percent uptick.

But revenue miles per vehicle points to a possible reduction in usage. FY 2007 represents the high-water mark for both revenue miles per passenger vehicle (27.69) and per commercial vehicle (51.84) for the last ten years. In FY 2013 the average passenger vehicle using the Turnpike traveled 26.81 revenue miles—about three percent lower than in 2007. However, commercial vehicles on average traveled 46.17 revenue miles—nearly eleven percent fewer miles than they did in 2007. In fact, commercial revenue miles per vehicle had been steadily declining since that peak. This measure shows that

commercial customers may be more sensitive to the fare increases than originally thought as they have shaved more than 5.5 miles off an average trip. This could eventually be problematic for the Turnpike as commercial vehicles pay more per mile than passenger vehicles. It could also cause problems for municipal and state roads as this measure suggests that commercial vehicles are substituting state or local roads for the Turnpike. Of course commercial vehicles do far more damage to roadways and bridges and that may translate into higher costs for those entities.

All told, the continual borrowing by the Turnpike and the raising of tolls has not produced a crisis as yet but there is every reason to be concerned as the debt piles up and tolls reach levels that begin to drive significant traffic off the Turnpike. Once the toll reaches a level that leads to stagnation or decline in revenue, the financial situation will become extremely problematic. As it stands, the annual \$450 million contribution to PennDOT is scheduled under the recent transportation bill to continue through FY 2020-21. The reliance on permanent historically low interest rates is not a prudent strategy.

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