

Trump’s infrastructure plan is not a simple public-private partnership plan, and won’t lead to much new investment

President-elect Donald Trump has indicated that one of his first priorities will be a plan to boost infrastructure investment. Normally, this would be welcome news for those of us who have been [arguing for years](#) that [increased public investment](#)—including [but not limited to](#) infrastructure investments—should be a top-tier economic priority. Further, it also seems like a rare opportunity for bipartisanship—after all, Hillary Clinton made infrastructure investment [a priority](#) of her campaign’s policy platform, as well.

The [still-sketchy details](#) of Trump’s plan, however, are a cause for concern. What we know is that the plan is to provide a tax credit equal to 82 percent of the equity amount that investors commit to financing infrastructure. In the coming days, this will invariably be described as creating *public-private partnerships* (P3s). P3s are a standard model for financing infrastructure that can *in theory* be used with little downside compared to direct public provision. However, this description of the Trump plan is both not that comforting and incorrect. It’s not comforting because the real-world record of P3s [is much spottier](#) than textbook models would suggest. And it’s not accurate because Trump’s plan isn’t as simple as encouraging new P3s. It is instead (at least in its embryonic form), simply a way to transfer money to developers *with no guarantee at all that net new investments are made*.

Let’s start with describing what a textbook P3 would look like and what the rationale for using it would be. P3s are long-term contracts between the state and private companies to build and maintain infrastructure. They can be thought of as sitting somewhere between standard public provision and full privatization of infrastructure. Say that a state or local government wants to build a new road, but is constrained for some reason (usually simpleminded anti-tax politics) from raising the money to publicly finance it. It’s important the democratically elected and accountable government ensure the project is in the public interest. Having done this, the government can then negotiate with private financiers and developers to get the project built. To reduce costs and provide incentives for development, [tax breaks](#) are sometimes provided to holders of bonds issued by the private entities, and the private entities also receive a revenue stream of some kind in exchange for their investment. Often this is an explicit user fee, like a toll for using a road.

P3s based on explicit user fees are clearly not useful for providing investments to underserved communities, who would likely not be able to provide profitable revenue streams. In theory, this can be addressed with clever “shadow user fees,” like minimum revenue streams guaranteed by the public partner. But such alternative mechanisms raise numerous new questions of corruption. For example, who makes sure that these minimum revenue streams are fair and only pay for the value of the infrastructure, as opposed to constituting pure rent-seeking that maximizes private profit?

P3s alleged benefit comes from the addition of profit incentives to infrastructure provision. Theoretically, this profit motive could filter out so-called [“bridges to nowhere”](#) that politicians approve for reasons of corruption or vote buying instead of broad economic benefits, as the private partner will demand a return on investment. In a well-managed P3 where infrastructure operators face some competition, the private partner is also expected to take into account the long-term costs of deferring maintenance, as fewer users will pay fees if the quality of the infrastructure deteriorates quickly. This could lead to better maintenance and repair than publicly financed infrastructure, since local political incentives lean more towards ribbon-cutting than pothole-filling. And to the extent that there is competition, more efficient pricing is possible as the infrastructure’s users pay the costs (though, as always, we would argue that simple efficiency should not be the sole criteria of policymakers).

It should be noted, however, that infrastructure investment is often characterized by economies of scale. The upfront cost is enormous, but the marginal cost of each new user is very, very low. These economies of scale in turn make it highly likely that the operators of the infrastructure will be a monopoly (it doesn’t make sense for

there to be two subway systems in New York City, for example). So, even “private” operators in P3s will likely have to be tightly managed and regulated, and the benefits of “competition” are unlikely to appear (monopoly is, by definition, absence of competition). In short, even textbook P3s are not some short cut around the need for government to be effective and well-run.

And in the real world, there are many ways [that P3s can go badly](#). For example, some P3s have included non-compete clauses that protect the private partner’s investment, which can hamstring the ability of the public sector to build future infrastructure projects, even those clearly in the public interest. For instance, there may be much more traffic than was anticipated when a P3 was used to build a toll road. The public partner might then wish to build more nontolled lanes to help alleviate the new traffic, but the private partner could file suit to protect the unexpectedly high profits on their tollroad. This is not an academic concern—exactly this happened with the P3 that provided [California’s State Route 91 Express Lanes](#). Or the private partner may ramp up prices (user fees) or reduce service quality in order to cut costs and maximize profits. Since much infrastructure has the character of a monopoly, customers are not free to just switch to other providers.

And then there’s the issue of renegotiation. Private companies have incentives to engage in opportunistic renegotiation. Such renegotiations reverse *all* of the benefits of ever engaging the private sector in infrastructure provision and financing. Take, for example, the case where a P3 toll-road is built, but traffic is lighter than forecast, so revenue disappoints. The private operator might try to renegotiate higher tolls or even minimum revenue guarantees from a public provider. [The international evidence](#) on P3s suggests that renegotiation is a major problem. Private partners tend to initiate renegotiations fairly quickly, and they tend to get bailed out when they run into financial problems. Most of the time, these bailouts occur because the private partner does a poor job of forecasting the revenue stream of a toll. In short, the use of P3s to make infrastructure investments without the whole endeavor turning into crony capitalism (exploiting the lack of competition to renege on implicit promises to undertake maintenance and repair or insisting on *ex post* renegotiation of terms if profit expectations disappoint, as we described above, among other things) depends heavily on strong regulation and the willingness to *not* renegotiate and bail out the private partner when they fail.

Frankly, this would raise alarm bells about the incoming Trump infrastructure plan even if it was a simple expansion of P3s. But [it’s not](#). Instead, it appears to be a plan to give tax credits to private financiers and developers, period. The lack of details here are daunting and incredibly important. For starters, we don’t know if the tax credit would be restricted to new investment, or if investors in *already existing* P3s are eligible for the credit. If private investors in already existing PPP arrangements are eligible, how do we ensure these tax credits actually induce net new investments rather than just transferring taxpayer largesse on operators of already-existing projects? Who decides which projects need to be built? How will the Trump administration provide needed infrastructure investments that are unlikely to be profitable for private providers (such as building lead-free water pipes in Flint, MI)? If we assume tax credits will be restricted (on paper, anyhow) to just *new* investment, how do we know the money is not just providing a windfall to already planned projects rather than inducing a net increase in how much infrastructure investment occurs?

To be fair, even well-planned infrastructure initiatives like the aid to state and local governments for infrastructure investment in the American Reinvestment and Recovery Act (ARRA) have to worry about simply crowding out already-planned investment instead of creating net new investment. For the record, research shows the ARRA investments worked very well, with substantial net new investment created. But a tax credit for private-sector provision introduces an additional complication. Instead of getting net new investment, states and localities may just change how the infrastructure investment they already had planned on are financed.

Trump’s plan frames the infrastructure problem as a lack of innovative financing options. This is nonsense. The problem is that politicians don’t want to ask taxpayers to pay for valued infrastructure. But, even in P3s, the taxpayers *do* pay. They just pay user fees or tolls to private entities rather than taxes to government. Thinking that the former is clearly superior is pure ideology. After all, nothing in theory really stops governments financing infrastructure directly and paying for it with their own tolls and user fees. In fact this happens all the time. But too often it is simply assumed that bringing in the private sector is always and everywhere more-

efficient and innovative. This is false. And it leads to flawed, ideological policies that will radically reduce—and may even totally erase—any net *new* investment actually induced by their plan.