

Memo

To: Karen Skelton
From: Fred Salvucci
Date: March 7, 2000
Subject: "Big Dig" Finances Review

I assume that the freeze and review of "Big Dig" finances must review construction change orders and items like that which have been in the news, but I believe that a fair review will find nothing improper. Change orders are always difficult to explain publicly, because they involve acknowledgement that there are unforeseen factors which warrant a change, but especially in underground work, uncertainty of exact conditions is a fact of life, and properly managed change orders save money in comparison to litigation and delay. Since this phase of the project was reviewed by FHWA as the project has progressed, my hope and expectation is that you will find everything to be in order.

The fact that the State rushed items like the Ted Williams Tunnel opening, and advertising with not all elements pinned down, has probably led to increased cost, but the state could argue that staying closer to schedule saves money, and again FHWA approved all these actions, so cannot fairly fault these actions.

An area of cost growth that is more troublesome is right-of-way costs, in that real estate owners whose property is taken tend to argue for the market value of their land as enhanced by the project, a logically inconsistent standpoint, but with expert lawyers, they are often able to prevail in the courts. The negotiated settlements in this area involved settlements that the inspector general previously objected to (notably at North Station with the Boston Garden). In addition, the treatment of Massport as if it were a private owner, getting compensated for property taken when half of the project cost (the Seaport Access Road and Ted Williams Tunnel) is primarily to improve access to Massport facilities,

raises an important public policy question, but presumably a reasonable Massport contribution to the project will eventually outweigh any payments. Moreover, according to news accounts a few years ago, the State was to be responsible for 100% of real estate acquisitions in the future, to avoid any federal concerns in this area. Assuming that agreement was implemented, there should not be any major federal issues here, although obviously the cost of takings affect overall project finances and must be reviewed, whether or not there is Federal participation.

I believe the major area of Federal concern should be the adequacy of the financial plan in terms of public disclosure, and the federal "fiscally constrained planning" requirements. These requirements represent a careful balance between respect for the local decision-making and priority-setting process, and the Federal responsibility for proper stewardship and maintenance of good state of repair of highway and transit systems which have been recipients of massive amounts of Federal money, and protection of fair treatment of cities and towns, geographical distribution of benefits, civil rights and environmental protection. The fundamental building block of proper fiscally-constrained planning processes is accurate public information, so that local officials and citizens can participate with the State in setting priorities. An important element in that process is, obviously, an accurate cost estimate. Once a project is underway, the real market costs will be incurred, and if these are higher than the cost estimate, other highway or transit projects or environmental mitigation will be displaced, creating an *ex post facto* flaw in the "fiscal constraint" process. An additional factor in the Big Dig case is the "Grant Anticipation Notes" which pledge about 50% of expected federal transportation funds for the next 15 years, thus depriving other state projects of access to these funds, far in advance of the normal decision-making process.

In short, a reasonable argument could be made that FHWA should not have agreed to the GANs, because they constrain the resources available to future generations. An even stronger case can be made that the "new" \$1.4 billion should be financed by the State with cash so that non-Boston road and MBTA projects which were in approved fiscally-controlled plans can proceed. This suggests a parameter for what FHWA will find acceptable that might require cash, or at least not involve any further GANs.

It may be worth a brief summary of the cost estimates of the Big Dig, particularly since 1991, to get a sense of what is happening:

In the 1983 FEIS, the cost of the project was estimated at \$2.5 billion in 1983 construction cost, consistent with the FHWA convention for interstate cost estimates. Between 1983 and 1990, completion of the supplemental EIS, costs rose to \$5.9 billion fully inflated. While that sounds like a large increase, it is important to realize that the project grew physically, expanding to include the contract 8A connection to Route 1A in East Boston, a major expansion to Southampton Street on the Southeast Expressway, plus the South Boston truck by-pass, and Spectacle Island. In short, the project in the 1991 Final Supplemental EIS was a different and bigger project than the 1983 project. Under the interstate rules of the time, 90% of costs were eligible for ~~90%~~ reimbursement from Interstate Completion Funds (with the exception of roughly \$1 billion of cost in the High Street to Causeway Street section). In addition, converting from current inflation index-based costs to fully-inflated cost, substantially exaggerates the apparent cost increase. The reason the 1991 cost estimate departed from FHWA tradition and is expressed in fully inflated nominal dollars is that 1991 was to be the last of the "old interstate" funding apportionments, and when President Bush signed the 1991 ISTEA legislation, it was clear that any additional cost above \$5.9 billion necessarily comes out of some other Massachusetts priority. Whether a shortfall is made up with Federal Formula Funds, gasoline taxes, tolls, or Massport contributions, given this reality, it is somewhat astonishing that the Weld administration reduced tolls and registration fees while they knew costs were rising well above \$5.9 billion. In 1994 when Kerasiotis ended the Scheme Z Review Committee, he announced that costs were up by \$1.2 billion in the area north of Causeway Street, and soil problems near Gillette were in the news during the same period. In about 1994 or 1995 the State announced that the project costs were \$7.7 billion, but now (I believe) they switched back to the current construction year cost estimate, reducing the apparent increase from \$5.9 billion. I believe the State ^{later} was justifying the \$10.7 billion simply as the "fully inflated" value of the 7.7 current construction index cost.

All of this confusion of numbers was used by the Weld administration to ignore the reality of the \$5.9 billion cap imposed by ISTEA, and pretend it was simply the job of the congressional

delegation to get 90% of whatever the cost is. At the same time, congressional critics took advantage of the confusion to argue for language freezing the ability of Massachusetts to use its Flexible Federal Funds on the Big Dig, an unfair position, but it required political energy to prevent it. In fact, the Massachusetts delegation did very well in the formula fight in 1998, getting approximately ^{53⁰} \$5.3 million per year for Massachusetts, substantially more than the \$350 to \$400 million the State contributes to the Federal Fund.

In all, the Big Dig has resulted in Massachusetts receiving about \$5 billion more than it has contributed to the Federal Transportation Funds over the past decade. Through the multiplier effect, this represents \$12 to \$15 billion in economic activity and probably accounts for about \$1.5 billion in Massachusetts tax receipts during the current boom, yet infrastructure projects at MBTA, environmental commitments of the Big Dig, and highway projects statewide have been deprived of funding in the midst of this boom because Massachusetts has withdrawn resources from transportation while the Federal contribution continues to represent a net benefit to the State. Yet as recently as last week Governor Cellucci was quoted as saying the problem of the \$1.4 billion is the failure of the congressional delegation to deliver enough Federal money.

While this is a complicated subject, I believe that the project is a good project, is currently reasonably well-managed as a construction project, and will generate major benefits. I believe the primary problem is the under-funding of other Massachusetts highway, transit, and Big Dig environmental commitments that should have been protected if a better public understanding of ISTEA and fiscal constraint had prevented the irresponsible lowering of tolls and registration fees by Massachusetts.

At this point in time, what is it reasonable for FHWA to do?

- (1) Freeze further construction contract awards until a value engineering process, with public participation, can review the current plans. It appears possible to save \$40 million in East Boston while improving environmental quality. It appears possible to save \$50 to \$100 million in the Dewey Square Tunnel, while reducing traffic disruption. A review of ventilation methods may indicate more savings. With a credibility crisis like this, the first obligation is to seek responsible cost savings.

- (2) Focus attention on the violation of fiscal constraint inherent in the State misrepresentation of cost, which have deprived the "rest of state" highway transit and Big Dig environmental commitments of support, and insist that the State revised financial plan identify funds not only to cover the \$1.4 billion (or larger shortfall) but FHWA substantially more to make up the MBTA and rest of State highway projects at a more reasonable level.
- (3) Refuse to cooperate in any further GANs or other excessive borrowing schemes by the State.
- (4) Require the Big Dig to shift to a State overmatch strategy, so that adequate Federal Formula Funds are available to honor the Big Dig environmental, MBTA, and rest of State priorities, while continuing to expeditiously complete the Big Dig.