Joint Development Strategy for Honolulu's Fixed Guideway

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Honolulu has been planning a rapid transit project for more than 25 years. This capital city of Hawaii has a resident population of more than 850,000 and a de facto population (residents plus military and visitors) of more than a million each day. The population is primarily contained in a dense corridor on the leeward side of the island of Oahu stretching approximately 40 mi. The business and economic centers are even more condensed within the corridor, consisting primarily of Waikiki, Kakaako, downtown, Iwilei, airport, and Pearl Harbor.

As now proposed, Honolulu's rapid transit line will stretch 15.7 mi from Waiawa, where H-1 and H-2 (Central Oahu) freeways meet, to the University of Hawaii campus in Manoa to serve the popular athletic facilities there. The transit line will be part of an integrated islandwide transportation system with bus routes reconfigured as feeder lines. In November 1990 the city and county of Honolulu issued a request for proposals (RFP) to procure its system. The procurement was unique in several ways:

- Technology was not preselected but the system had to be automatic (driverless);
- Turnkey operation would include design, build, operate, transfer (DBOT);
- Fixed-price bids with a very detailed cost proposal were required; and
- Joint development proposals were strongly encouraged but would be evaluated separately.

After a spirited and competitive process, the team selected was a consortium called Oahu Transit Group (OTG). Its joint venture partners include Morrison-Knudsen (managing partners), AEG Westinghouse Transportation Systems, EE Black, and SCI Contractors & Engineers. OTG bid a 208-passenger articulated vehicle. The vehicle will ride on an innovative elevated concrete guideway designed to have maximum span lengths of 180 ft, walls and an emergency guideway that double as noise barriers, and extensively landscaped exterior planters.

Since Phase 1 of the project was awarded December 3, 1991, OTG and the city have been completing route selection and station locations as well as a supplemental draft environmental impact statement (EIS) and a final EIS for the project. The Honolulu City Council is scheduled to take a crucial vote to raise the current 4-cent general excise tax by an additional half cent to fund Phase 2 construction. Of the total $1.7 billion costs, one-third (or $618 million) will come from the federal government. The local share will come from the half-cent excise tax cushioned by a partial state rebate to resident taxpayers.

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JOINT DEVELOPMENT AS FINANCING MECHANISM

In recent years Honolulu has had a very active real estate market, fueled in part by heavy Japanese investment. At the market's peak (1988–1989), some land costs along Kapiolani Boulevard (a major city artery that runs parallel to the transit route) were running \$500 to \$600/ft² of frontage. During this time the city was putting together its initial cost estimates and financial plans for the transit line.

The Urban Mass Transit Administration [now Federal Transit Administration (FTA)] enthusiastically committed a 30 percent share in return for promises that the city would attempt to involve the private sector to the greatest extent possible. Next the state legislature, meeting to consider the project financing, permitted two alternative plans:

- Plan A: If 35 percent financing were received from the private sector, the state would contribute $50 million a year for 17 years; or
- Plan B: If 35 percent private financing were not received, the city was authorized to raise the general excise tax by a half cent for a 10-year period. In this case the state would provide partial rebates to resident taxpayers to offset their burden.

At the time this legislation was approved, it was believed by many that Plan A could be achieved through the provision or sale of development rights along the line or elsewhere. This impression was fueled by an interested party who circulated stories widely in the legislature that the line's expenses could be fully covered by the sale of development rights. Unfortunately, as it turned out, none of the bidders was even able to achieve the 35 percent goal with up-front money (roughly $600 to $700 million). What happened?

JOINT DEVELOPMENT'S ROLE IN EVALUATION CRITERIA

To understand what happened, one needs to begin with the RFP evaluation criteria. There were four major criteria, each with a set of subcriteria listed in order of importance. The major criteria were as follows:

- Technical and management expertise,
- Cost proposal,
- Benefits to the city, and
- Joint development options.

Five teams chose to submit draft proposals and all five were eventually invited to submit a best and final offer (BAFO). A considerable amount of variation appeared among the teams' proposals. Each, for example, selected a different technology: magnetic levitation (maglev), rubber tires, monorail, and steel-on-steel (proposed by two bidders).

Although the teams initially formulated their proposals around the technologies, as the process moved along the proposals became more and more dominated by the construction element. This was in part because of the stiff requirements for bid and performance bonds—requirements that could only be met by the deep pockets of a major construction company partner. It is noteworthy that all of the teams were highly qualified in a technical sense and that the three lowest bids were within $100,000 of each other on a $1.17 billion job.

It is also noteworthy that the RFP was extremely well written and the evaluation and selection process were fair and smoothly run. Only a single challenge to the selection was made, and after two rounds had been lost in court, that suit was dropped.

The Group IV privatization and joint development criteria described in the RFP included the following points:

- Whether the city considered the option appropriate;
- Whether the option was likely to be approved by the jurisdictional authority;
- Depth, quality, and financial feasibility of the plan;
- Degree of commitment; and
- Potential value to the city net any costs or disbenefits.

JOINT DEVELOPMENT PROPOSAL BY THE WINNING BIDDER

Very little is known about the joint development proposals of the losing bidders because each chose to classify these volumes as proprietary. It is rumored that they varied considerably, ranging from no submittals to a series of alternate alignments and extensions coupled with a franchise proposal. Competition in the area of joint development was especially fierce between the draft and BAFO submittals as rumors flew around town about the content of competitors' proposals. In retrospect much of this was probably speculation fueled by competitive fears because the city's security was airtight.

OTG's winning joint development proposal was presented to the City Council and the media immediately following selection. OTG offered seven basic proposals, four of which were as follows:

- Prepare a master plan for joint development along the entire line;
- Contribute $100 million for the development rights at eight stations, specific plans to be consistent with an approved master plan;
- Revenue sharing at a major proposed mixed-use development to be called Concert Galleria (Concert Galleria would include a 1.8-million-ft^2 retail mall, 1,440 units of market-priced housing, and 1.25 million ft^2 of office space; the city would share 20 percent of net revenues); and
- Master concessionaire plan with revenue sharing at 60:40.

These four proposer options were offered by a separate joint venture formed by Morrison-Knudsen and The Myers Corporation, a major Honolulu developer with a successful development portfolio in residential, office, and hotel projects. In addition, OTG offered three other options:

- Dillingham Plaza, a mixed-use project at a station site, proposed by Bedford Properties, a respected developer in Honolulu and California;
- Newtown Industrial Park, which offered a financial contribution to the transit project; and
- Pearl Highlands, which offered to build an extra transit station at its power mall then under construction.

This set of proposer options represents a range of opportunities although hardly a comprehensive set of the possibilities inherent along the line. It would have been impossible to do that during the relatively short period of time available and within the resource confines of what was required for the rest of the transit proposal. Meanwhile the city has a 1-year period in which to exercise the above options.

EVALUATION OF THE JOINT DEVELOPMENT PROPOSALS

Although several of the proposers offered privatized financing techniques (for example, benefit assessment and tax increment financing, cross border leasing, or leveraging of federal and state money), none were qualified in the evaluation as a private source within the proposers' authority, and therefore they were not given any points. Franchise proposals from two of the bidders were not awarded points for failure to provide sufficient information, including monetary data.

The seven options offered by OTG, the winning bidder, were initially valued at approximately $487 million, or slightly more than half the amount required to initiate Plan A financing. This amount was heavily discounted. In a state analysis for the legislature the value of the private offer was reduced to $347 million by eliminating some of the proposals as outside city authority or current zoning policy. Furthermore, and perhaps most significantly, the OTG proposal and the city analysis showed that most of the private-source revenue would come by sharing future year revenue streams. Net present value analysis substantially reduced the value of the income stream.

Moreover, even had everything gone according to plan, much of the revenue would have come in the future; only $65 million would have been received from private sources by 1998, the year in which the construction would be completed. This amount represents only 8 percent of the total costs.

City and state officials recognized that, given the overall size and nature of the rapid transit project, some private revenues could be expected. However, these revenues were considered to be too unreliable or unpredictable a source to use in a financial plan. The conclusion therefore was to focus on Plan B, the half-cent excise tax as the major (70 percent) financing source for the capital costs of the project. This fall-back position has not been without its political ramifications in that raising taxes in Hawaii is as unpopular as anywhere.

JOINT DEVELOPMENT IN PHASE 1

The role for joint development has taken a dramatically different course than initially anticipated. Instead of financing a major portion of the capital cost, joint development is viewed as a supplemental source for operational and maintenance costs and as a resource for implementing land planning objectives. Joint development has for the moment taken a back seat to the more urgent tasks of completing the final environmental work and mustering the political will for the financial package and the half-cent tax increase.

This is not to imply that nothing is proceeding—quite the contrary. Both the city and OTG are progressing with their plans for development. The city has taken two steps. First, the city has selected an independent consultant to prepare a master plan for land use along the entire alignment. OTG options, city joint development options, and other private development proposals will all be evaluated against the work of the master plan consultant. The city has formed eight citizen advisory committees (CACs) for different segments of the alignment. The CACs, which have already been involved in station location and design, will next work with the master plan consultant to define station area character and land uses.

Second, the city has advanced its own joint development program by identifying selected city-owned sites and in certain instances negotiating to acquire sites. These sites will be awarded through an RFP process to interested developers who are willing to provide city amenities or share the revenue stream with the city. The City Council is deliberating a proposal to dedicate such revenues to operations and maintenance of the transit line.

The state legislature has not lost interest in the concept of using private development revenues for the capital costs. A proposal under consideration would permit this option. The objective of this legislation is to reduce the number of years during which the excise tax would have to be levied.

As for the OTG options, none has been selected at this time, most likely because the city is awaiting the outcome of the master plan process. Meanwhile Myers/Mk Partners has proceeded with landowner, community, and agency negotiations on Concert Galleria, the major mixed-use development. As the development plans progress a significant amount of redesign can be expected before the project takes its final shape.

Myers-Mk is also working on a series of transit-based housing proposals along the route. Affordable housing is a major problem in Hawaii with its high land prices. Shortages have been estimated at 20,000 to 40,000 affordable units and including a portion of affordable housing is a common condition of most rezoning actions. Myers-Mk is looking to provide a major demonstration of how housing and transit can work together by working through a nonprofit development fund.

CONCLUSION

Joint development in the Honolulu rapid transit project has evolved from viewing it as a major financing mechanism for the capital costs to viewing it as a supplemental resource and revenue stream for operations. Most recently the view of joint development is focused on its potential for integrating land use and transit and for building communities. The transit project is still in its infancy. In the next several years it can be expected that real estate and joint development will become recognized contributors to both good land use and sound financial planning.