Public-Private Partnerships: The Big Picture

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Leveraging Private Capital for Public Infrastructure: The Big Picture

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Institute for Emerging Issues

North Carolina State University

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The U.S. is on the verge of a "perfect storm" in funding its civil infrastructure

Infrastructure badly in need of reinvestment

New Orleans 2005

Minneapolis 2007

?

2009

Financial needs are huge

Aviation	D
Bridges	C
Dams	D
Drinking Water	D-
Energy	D+
Hazardous Waste	D
Inland Waterways	D-
Levees	D-
Public Parks and Recreation	C-
Rail	C-
Roads	D-
Schools	D
Solid Waste	C+
Transit	D
Wastewater	D-

AMERICA'S INFRASTRUCTURE G.P.A. **D**

ESTIMATED 5 YEAR INVESTMENT NEED **$2.2 TRILLION**

CATEGORY	5-YEAR NEED (BILLIONS)	ESTIMATED ACTUAL SPENDING*	AMERICAN RECOVERY AND REINVESTMENT ACT (P.L. 111-005)	FIVE-YEAR INVESTMENT SHORTFALL
Aviation	87	45	1.3	(40.7)
Dams	12.5	5	0.05	(7.45)
Drinking Water and Wastewater	255	140	6.4	(108.6)
Energy	75	34.5	11	(29.5)
Hazardous Waste and Solid Waste	77	32.5	1.1	(43.4)
Inland Waterways	50	25	4.475	(20.5)
Levees	50	1.13	0	(1.13)
Public Parks and Recreation	85	36	0.835	(48.17)
Rail	63	42	9.3	(11.7)
Roads and Bridges	930	351.5	27.5	(549.5)
Discretionary grants for surface transportation			1.5	
Schools	160	125	0**	(35)
Transit	265	66.5	8.4	(190.1)
	2.122 trillion***	903 billion	71.76 billion	(1.176 trillion)
Total Need**	**$2.2 trillion**			

The Highway Trust Fund is broke

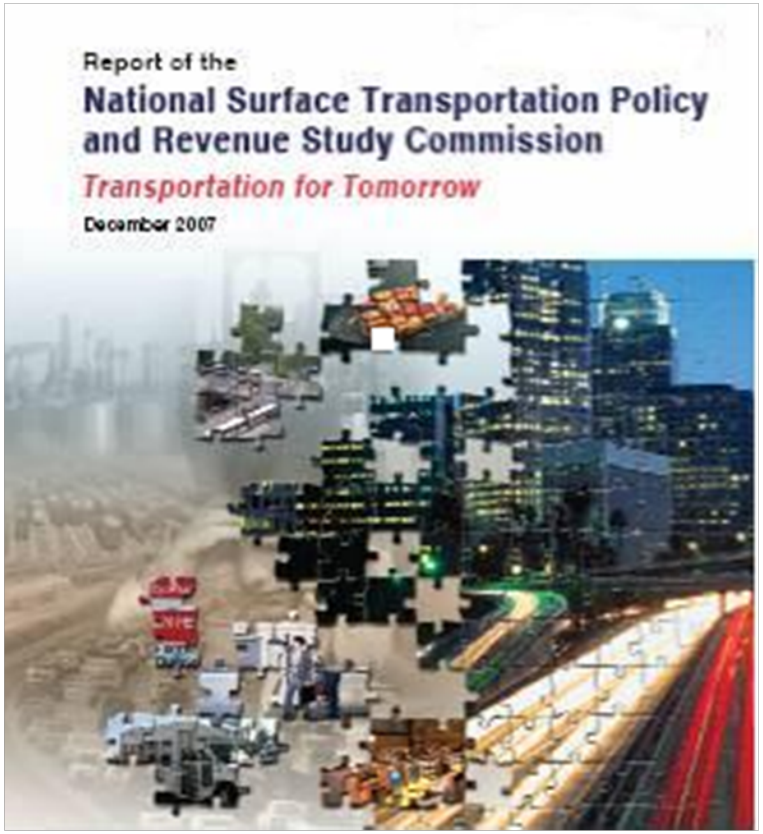
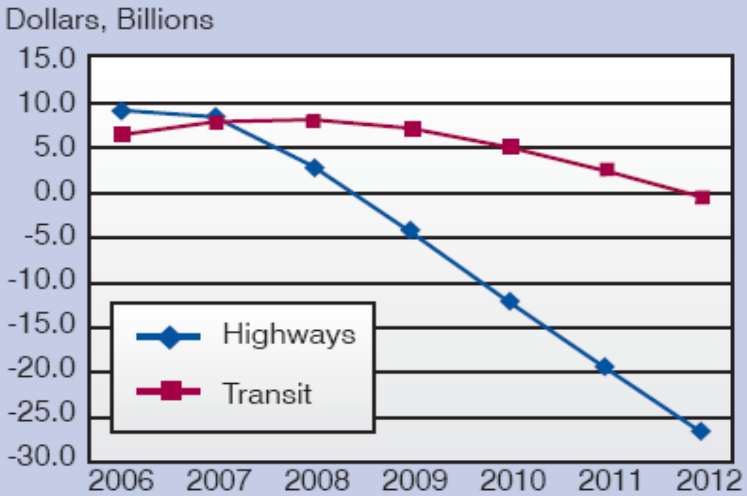
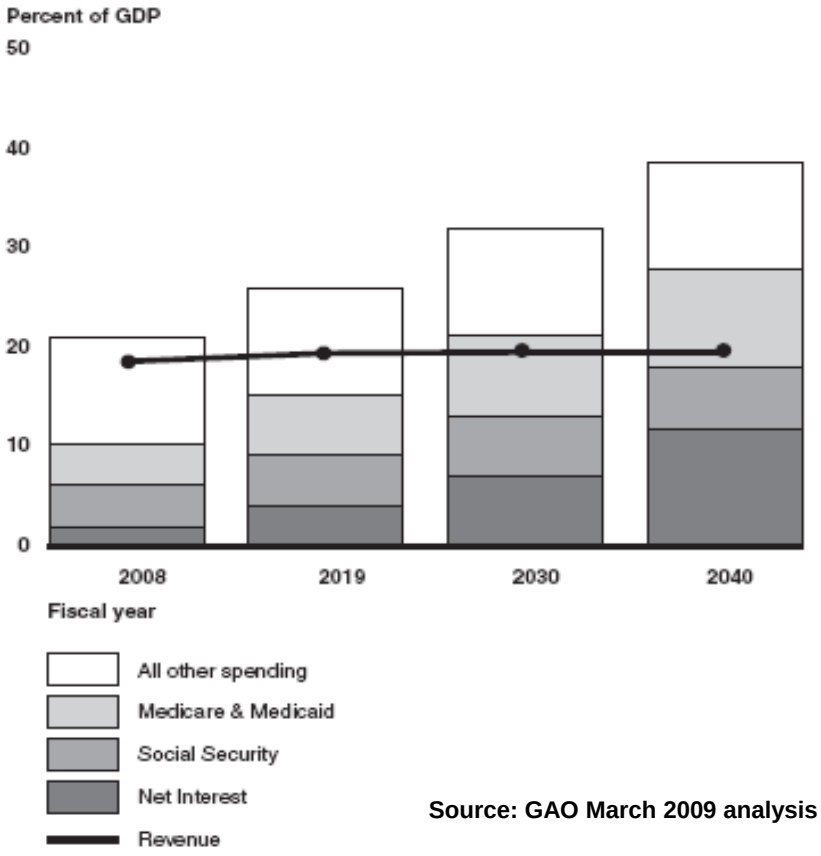


Exhibit 5-13. Projections of Highway and Transit Account Balances Through 2012



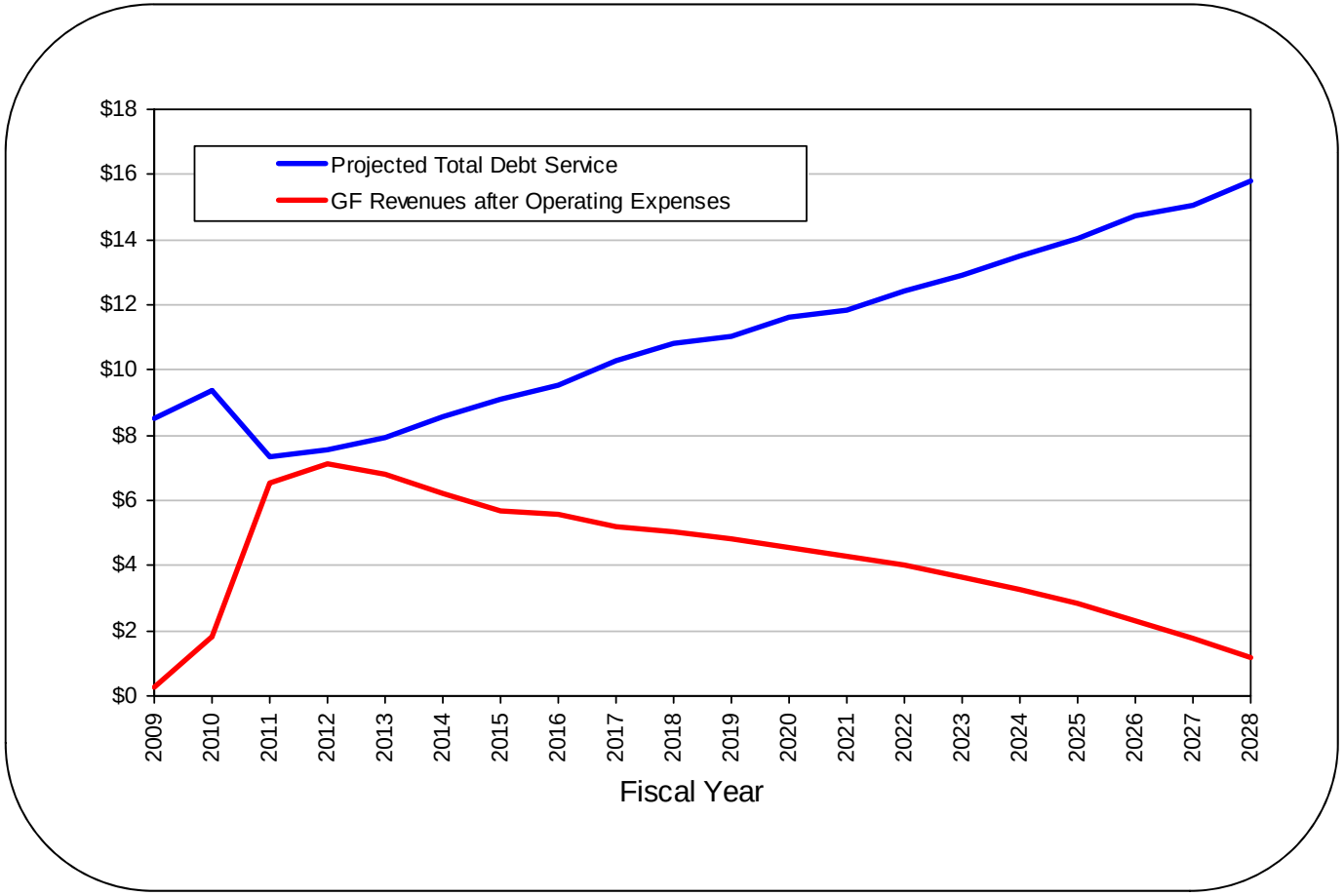
This exhibit shows projected balances in the Highway and Transit Accounts of the Highway Trust Fund through 2012 assuming no change in revenues or program levels.

Barring drastic changes in revenue and expenditure policy, the Federal Government will be insolvent



Source: GAO March 2009 analysis

In California, debt service on GO Bonds already exceeds available revenue



So, what should we do and where will we find the money to do it?

Before we answer that question, we first need to address a basic public policy issue

Are infrastructure services a public good, a market commodity, or something in between?

The answer to this question has profound implications for how we should fund and finance infrastructure.

First, we need to address the harsh reality of infrastructure finance

There are two ways to pay for infrastructure, taxes or fees

Public Good

Market Commodity

If we will not support increased taxes to pay for infrastructure, we will need to charge user fees!

This is not a simple binary decision!

or

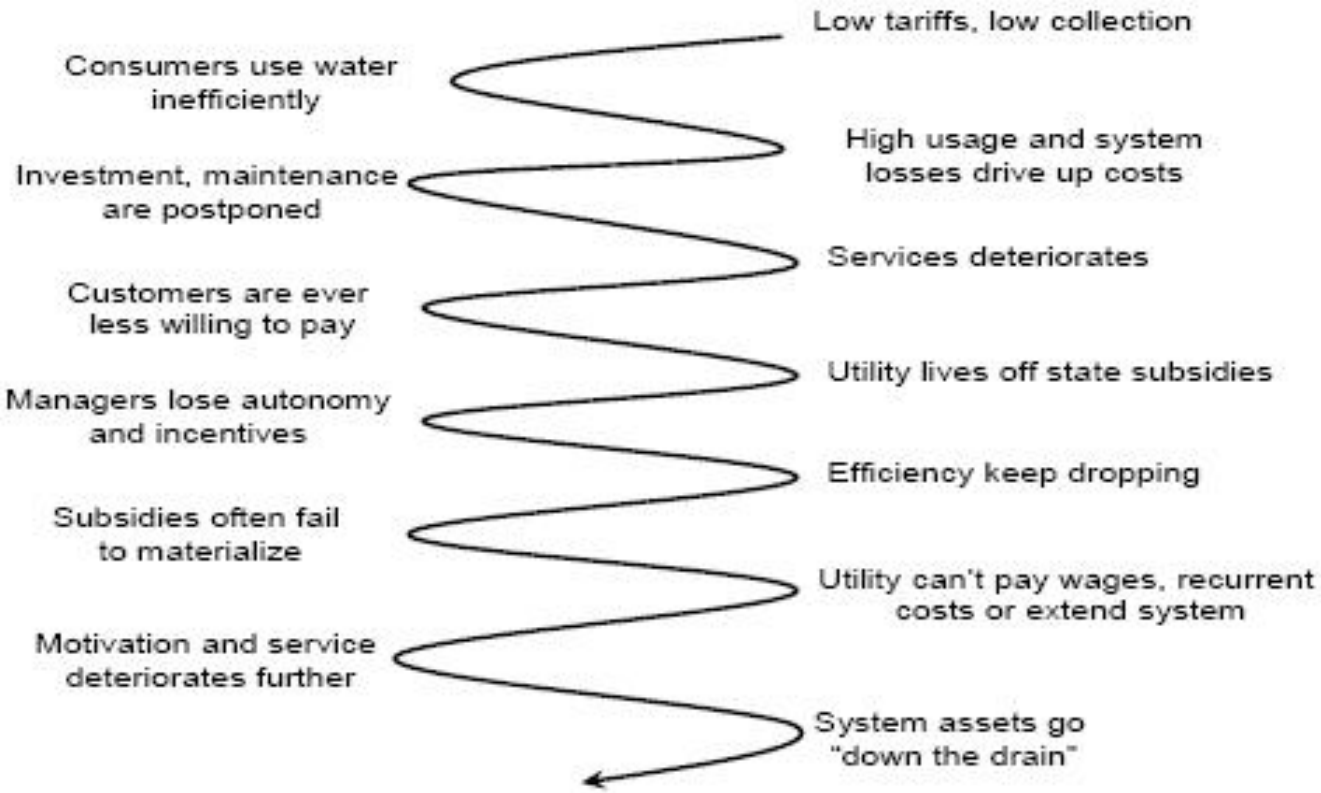
But it does come with its own mythology

Myth 1:additional taxes will cripple the economy

- 1¢/gal of fuel tax ≈ $53,000,000*
- 10¢/gal ≈ $500 Million/year or the debt service for a $1.0 Billion bond
- If you drive 20,000 mpy in a vehicle that gets 20 mpg this will cost you ≈ 23¢ per day.

*North Carolina data

Myth 2: keeping utility rates as low as possible is the best public policy



There are a range of funding and financing options available

- Management strategies to reduce demand and the need for physical infrastructure
- Increase taxes
- More user fees (TOLLS!!!) where the beneficiary pays for services received
- Non-enterprise resource streams outside of general revenues
- Increased reliance on innovative procurement and financing (PPP or P3 arrangements)

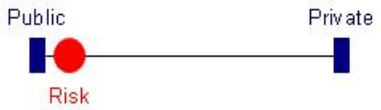
New ways of thinking about what we do, how we do it, and how it's paid for.

PPPs—when public funding isn't enough

Public Private Partnerships (PPPs) are **CONTRACTUAL AGREEMENTS** between the public and private sectors wherein the private sector agrees to **DELIVER SERVICES** in exchange **FOR A FEE**.

The private sector typically agrees to finance, build, operate, and maintain the infrastructure assets (frequently, but not exclusively, transportation) necessary to deliver the services.

How do they work?

Type	Description	Risk Transfer
Design-Bid-Build (DBB)	Design and construction contracts awarded separately to private sector engineering and contracting firms	
Design-Build (DB)	Combines the design and construction phases into one fixed-fee contract	
Design-Build-Operate-Maintain (DBOM) Build-Operate-Transfer (BOT)	Selected contractor is responsible for the design, construction, operation, and maintenance of the facility for a specified time	
Design-Build-Finance-Operate (DBFO) Design-Build-Finance-Operate-Maintain (DBFMO)	Similar to DBOM, but contractor is also responsible for all or a major part of the project's financing	
Build-Own-Operate (BOO)	The private partner owns the facility and is assigned all operating revenue risk and any surplus revenues for the life of the facility.	

PPP can work for a range of infrastructures

- Transportation
- Water and sewer services
- Solid waste disposal
- Municipal parking
- "Social" infrastructure (schools, hospitals, other public buildings)

Can PPPs satisfy all the stakeholders?

Government wants:

- infrastructure to support economic growth and quality of life
- minimum life-cycle costs
- adequate & timely maintenance and repair
- "off budget" capital improvements

Investors want:

- steady, stable long-term return on capital
- opportunity to take advantage of value "locked" in public assets
- ability to use innovation to improve productivity and profitability

The Public wants:

- Good, reliable service at a fair price

Some of the concerns a PPP must address

Value for Money – making sure the desired services are provided at the same or less cost over the project lifecycle

Transparency – negotiating in open competition with details available for public scrutiny and accountability well defined

Workforce Issues – concern that any PPP will be viewed as a pretext to lay off public employees

Social Equity – making sure that all groups have equal access to basic services

Risk Management – ensure that all parties assume responsibility for the risks they are best prepared to manage

Accountability – holding both sides of the negotiation accountable for meeting contract provisions and pre-determined performance goals

Some common risks in a PPP

Political risks - unanticipated change in government, cancellation of a concession, unanticipated tax increases, arbitrary toll or fee imposition or increases, or new and unilateral regulatory policies

Construction risks – design flaws, delays in land acquisition or environmental clearance, project delays, unanticipated site conditions, or poor contractor performance

Operation and maintenance risks - physical condition of a concession facility, operator competence, poor construction quality

Legal and contractual risks - concession warranty or incomplete or inadequate contracts

Income risks - inaccurate estimates of traffic volume or revenue, construction of a competing facility that would reduce use or profitability

Project Finance – a key to PPPs and a barrier to their acceptance

Project finance makes use of highly leveraged, long-term commercial debt secured by the cash flows either generated by the project or guaranteed by the procuring agency and not the resources of the project entity.

It is generally not well understood by bureaucrats and elected officials!

Impact of the financial crisis on project finance and PPP

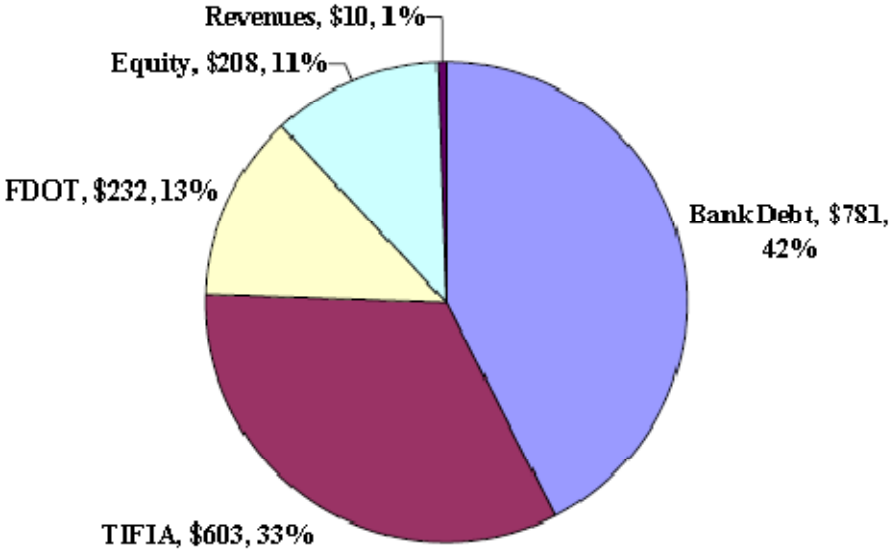
- Although the disarray is clearing, it will take more time for any sense of normalcy to return to project finance
- Leverage ratios are down (much more equity required)
- Liquidity is way down, commercial debt is expensive and not available for long term deals
- The U.S. market likely will be wary of nontraditional finance for some time to come. The presence of foreign players has been problematic in some cases.

Florida I-595 – a successful U.S. PPP

The Florida I-595 PPP is a $1.8 billion, 35-year DBFOM concession on a 10.5 mile portion of the highway in Broward County, north of Miami. The deal reached financial close on March 3, 2009.

<u>Financing</u>

$800 million - Bank Debt
$600 million – TIFIA* Loan
$232 million – FDOT
$200 million – Equity
$ 10 million – Revenue



This is the first highway PPP in the US to use an availability payment scheme. The consortium will receive annual payments of $63.98 million mostly from tolls.

*Transportation Infrastructure Finance and Innovation Act

Some Canadian examples of PPP

Project	Description	Status	
Sierra Yoyo Desan Resource Road Operational	A 188-kilometre-long major upgrade of the Sierra Yoyo Desan (SYD) Road through a Design-Build-Finance-Operate-Maintain arrangement. **Client:** Ministry of Energy & Mines **Partnerships BC's role:** Procurement Manager	▪ Agreement announced: June 2004 ▪ Completed: 2005 ▪ Project Report: Achieving Value for Money released: Nov 2004 ▪ *CCPPP: Financing Award 2004	
Gordon & Leslie Diamond Health Care Centre Operational	A new facility that will support several hundred medical students, more than 580 medical and allied professionals, and an estimated 600,000 patient visits annually. **Client:** Vancouver Coastal Health **Partnerships BC's role:** Advisor	▪ Agreement announced: Sept 2004 ▪ Substantial completion: Aug 2006 ▪ Project Report: Achieving Value for Money released: Dec 2004	
Britannia Mine Water Treatment Plant Operational	A new acid-water treatment plant at the former Britannia Mine site near Squamish, B.C. **Client:** Ministry of Sustainable Resource Management **Partnerships BC's role:** Procurement Manager	▪ Agreement announced: Jan 2005 ▪ Substantial completion: Jan 2006 ▪ Project Report: Achieving Value for Money released: Feb 2005 ▪ *CCPPP: Infrastructure Gold Award 2006	

Some questions for the public sector to consider going forward

- What do we want to accomplish?
- What capabilities do we possess to achieve our objectives?
- What is the right mix of funding and financing approaches?
- What is reasonable and realistic to ensure efficiency and equity?
- Who controls the process; federal, state, local, or private interests?
- Who provides oversight?

Some questions for the private sector to consider going forward

- Will infrastructure meet investment objectives?
- Is there sustainable political commitment to the PPP process?
- Will commercial financing be available at a cost and for a duration to enable project success?
- Can the risks delegated to the private sector be managed successfully?
- Are the elements of a successful project team available?
- Is the public partner an "educated owner" that understands the PPP process?

Guiding principles for PPP

- Participation, by all involved parties, needs to be informed and organized.
- Fair and equitable legal frameworks are enforced impartially.
- All decisions and their implementation must be transparent to the public and abide by established rules and regulations.
- Information must be freely available and directly accessible to those who will be affected by the decisions.
- The process must be consensus oriented, responsive to the needs of all stakeholders, and equitable.
- The project should be effective and efficient, producing results that meet the needs of the local society
- All project participants must be accountable to those who will be affected by their decisions or actions.

What's the keys to making this work?

- Clear understanding and statement of objectives
- Mutual respect for the goals of each party
- Transparency
- Capable, knowledgeable people on both sides
- Realization that PPP are not free money; revenues must be available to pay the private sector for its efforts

Can PPPs help address the U.S. infrastructure deficit?

If the private sector can deliver reliable services faster and/or at less cost to the public at large and make a profit at the same time, why should we care?

This is what remains to be proven!

A closing caution!

"Let them innovate in nothing, but keep the traditions"

Pope Saint Stephen (254-257)

This mentality will not get us to where we need to go!

Sites for further research

Partnerships British Columbia
http://www.partnershipsbc.ca/

Infrastructure Ontario
http://www.infrastructureontario.ca/

Infrastructure Partnerships Australia
http://www.infrastructure.org.au/

Canadian Council on Public Private Partnerships
http://www.pppcouncil.ca/

The National Council for Public Private Partnerships
http://www.ncppp.org/

Thank you!

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