P3s In The US: Is There A Role and Future?

What Works? What Doesn't for the 21st Century?

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- Director, two terms at Power Generating, Inc. renewable energy company and other company advisory boards; Director and Chairman, Sphere E, Inc. (2011 -).
- Just rated in 2012 Top Rated Lawyers Guide to Energy/Environmental/Natural Resources Law, and rated in 2013 Euromoney LMG Clean Tech Top 100 in US; 2013 American Lawyer and Martindale Hubbell "Top Rated Lawyer in Energy/Environment Land Use"
- Former Co-Chair, American Bar Association ("ABA") Renewable and Distributed Energy Resources Committee (2008-10).
- Former Co-Chair ABA Energy and Environmental Markets and Finance Committee (2010-12), currently in ABA SEER Section capacities on book publishing and annual Fall meeting (2012-13).
- Legal Advisor, Capital Markets Partnership for U.S. green building finance (2008-11), Americans for Community Development (2009-), and Washington Counsel, The Microgrid Institute.
- Member, USGBC Energy Atmospheric TAG Committee (2005-09); ASTM BEPA Legal Subcommittee (2009-10) on green buildings.
- Best rating in nation for *Martindale & Hubbell* (1989-2012) - highest rated for 20 years for legal quality and ethics.
- Member, Strategic Advisory Committee American Council on Renewable Energy (ACORE); former Vice-Chair, ACORE Biomass Coordinating Council.
- *Public Utilities Fortnightly,* Ground Breaking Lawyers Award (2009) for renewables and cogeneration work; 2013 Who's Who of Procurement Lawyers; Martindale Hubbell Washington, DC and Baltimore's Top Rated Lawyers
- Rated in Who's Who in International Project Finance Law.
- Moderator and Co-Editor or Contributor, *Ohio Energy Report (2006), Ohio Advanced Manufacturing (2011), Ohio Climate Change (2010-11)* and *Ohio Shale Energy Supply Chain (2012)*, Voinovich School for Leadership and Public Affairs, Ohio University.
- Chapter author with Matthew Bender, Inc., Urban Land Institute, Government Institutes and ABA publication on various clean tech, energy, cogeneration and green building topics.

Overview

- What are P3s – and what they cover and offer?
- Why are P3s game changers? The magnitude of the prize
- What makes a P3 work? What are the problems?
- Why do some P3s fail?
- Future in U.S.

What are P3s – Partnerships with Common Goals

- A collaborative venture between the public and private sectors, built on the leadership and strengths of each partner, that best meets clearly defined, validated public needs, risks properly allocated – and makes money!
- “P3s that rely on contracts to solve problems, and not its leaders, are doomed to fail.” Mahlon Agpar IV
- Cooperation with constructive solutions grounded in problem solving and not litigation
- Flexibility with adaptation as over 33% of P3 projects are restructured

P3s – Roles

- Federal
- State/County or City Agencies
- Business/Developers
- Operating Managers
- Investors
- Lenders
- Consultants

Funding Challenges - Public

- Major economic/environmental/resource issues
- Staggering budget deficits; funding vs. financing
- Declining revenues, bankruptcy and bond defaults in government units
- Struggling to maintain necessary & basic services; redefinition
- More responsibility on the backs of the citizens/taxpayers
- Downsizing and outsourcing
- Lack of political or public will; but politicians seek to control public assets
- Old traditional methods of financing are limiting
- Lack of innovation, deferred maintenance growing

Funding Alternatives to P3 Option

- Direct fees, tolls
- Debt, and sovereign debt
- Credit assistance/support, TIFIA, WIFIA (pending) and others
- Equity – funds, private equity, pensions
- Value extrapolation, developer fees, special districts, tax increment financing, joint development authorities
- New tools, land bank, national infrastructure banks
- Loan guarantees
- Efficacy insurance
- Grants, philanthropy, social enterprise, L3C's and dream contracting

Other Financial Instruments

- P3, P4 & P5 (Pro-Poor, Public-Private Partnerships)
- Social Impact Bonds
- Bonds, BABs redux, Covered Bonds
- Master Limited Partnerships (MLP) for Infrastructure
- State Clean Tech Funds (19 in review)
- Infrastructure Development Banks
- Trading systems (carbon, emissions, water, conservation, nutrients)
- Conservation and Land Trusts
- User, tipping, and impact fees
- Loans and loan gurantees (federal and states) – EPA, USDA, Cobank, Commerce, North American Development Bank
- Brownfields Development
- Local government as center for DG, distributed water, efficiency, PACE model, SIDs
- Natural Resource TIF's

P3s – Often Center On Big Complex Problems

P’3s often address political and physical facilities concerns:

- Unmet needs that are important, urgent and not satisfied in community
- Unfunded or underfunded public priorities, budget shortfalls and programs foster need for “on cost” delivery
- Needs for innovation/technology as part of solution
- Negative signs about facilities condition and delivery, deferred maintenance and upkeep
- Excess costs, low value for money, inefficiency, cost overruns
- Failures of governance, procurement process by public
- Consumer (constituent) complaints and/or bad publicity, infrastructure shortfalls
- Process improvement, timelines, cost savings
- Jobs creation, trade unions solution to a problem

P3s – Public Process

The “public agency” sets the environment and ground rules. Public criteria in U.S. for success are:

- A positive P3 environment
- P3 legislation and authorities
- Competent P3 office with experience, right staff
- Business-like conditons in the P3 government office
- Evaluation of market interest
- Pre-qualification principles
- Established a RFQ process, then LOI, RFP‘s with enhanced pre-qualification
- Panel with business advisory experience; balance on control issues
- Nature of project for P3 success; not for all public projects
- Wide/narrow scope for project
- Project timeline realistic
- Project risk-reward clear / fair / shared; not merely transferred or hidden in complexity
- Land ownership/treatment
- O&M value
- Nature of innovation, technology risk
- Risk transfer vs. control of public assets

Process

- Best Practices; Worst Practices
- Standard Agreements
- Data/Analysis
- Alternative Scenarios
  - With 55% of US infrastructure requirements unbudgeted in future
  - Requirements for sustainable economic growth
- Comparison of Service Contract, P3's, Design-Build, Bonds with Leasing and experiences in other countries
- To succeed, the P3 process must address:
  - not serving public interest
  - corruption and incentives for abuse w/DCF of rents transfers
  - maintenance of independence, with checks and balances over controls of assets
  - transfer of public policy with power to private sector for enhanced economic efficiency
  - control issues
  - role of competition
  - impacts on labor, collective bargaining deals

Oversight

Lessons from P3 experience in U.S., UK, Australia, Canada:

Oversight is critical and grounded in fairness, quality and independence to:

- Inform budgetary process, reduced bureaucracy
- Partners – public and private – comply with spirit as well as rules; a balanced process
- Impose discipline and caution, efficiency
- Constructive and practical, improved results
- Mission and project first

P3 Documentation

More recent experience and norms may be valuable:

- Original business cases
- Contracts, concessions and agreements
- Schedules
- Payments, subcontractors
- Performance targets set
- Qualitative intent of “value for money”
- 20-25 years LCA cost analysis
- Land management. agreements
- Construction, risk management or mitigation; not merely transfer

P3s – Wrong Tools

Differentiate established, well-understood tools from P3s and improper structures for risk management and transfer.

- Outsourcing: Contracting for services, staff or facilities. Outsourcing can lead to a P3 if the contractor becomes a "partner" in providing the service.
- Disposition: Sale of assets to transfer responsibility, control, costs, risks for a government function to business. Once the asset or function is gone, it's not likely to return to government.
- Sale-leaseback: Leaseback of government building as a condition of sale. Established practice which does not require P3 organization and oversight; watch accounting rules.
- Design/Build: Services to save time and cost in typical construction project. Established practice which does not require P3 organization and oversight.

Source: Mahlon Apgar, IV, 2013

P3s – What Doesn’t Work?

P3s fail to meet their goals if they do not:

- Engage all major stakeholders and constituents
- Provide “level playing field” for private partners, proper risk management
- Defuse political risk to a public/business/stakeholder outcome orientation
- Build revenues / value / risk into business models
- Define desired outcomes / ensure progress; not merely financial returns
- Drive actions to protect mission, and not just contracts
- Educate their public constituencies and stakeholders
- Provide transparency with abundant communication

Streamline Government First

Local/state governments need talents and tools to design, structure and manage P3s for this to work properly:

- Reform procurement – first use RFQ … then RFP to remove lowball pricing
- Install metrics for management and oversight
- Adopt pilots and prototypes to solve problems; experiments
- Infuse “best business practices” – and foster innovation
- Standardize procedures and contracting
- Educate public; financial community for establishing new “asset class”
- Value adds specified/quantified
- Know when to say “No”
- Land use policies must be integrated
- Changes/post operations data and analytics

Targeted Funding Approaches

- Public-Private Partnerships
  - A contractual arrangement whereby the resources, risks and rewards of both the public agency and private company are combined to provide greater effiency, better access to capital.
  - Can come in a variety of forms or delivery methods tailored to the partnership's needs.
- Benefits
  - Have been tested and used in the U.S.A. for over 200 years primarily for infrastructure projects. Would be unique but a form of conscious public capitalism
  - Valuable tool during challenging economic conditions of low revenues/slow growth.
  - Allows the private sector & investors to take the risks the community is not able to take to provide valuable real services which are appropriately rewarded in return.
  - Assembling of sufficient resources and technical expertise at a scale to do enough of the right things to produce the desired results, and to do the right things right. Mission and people, solutions.

P3 Innovation

- Efficiency for results
- Technology access
- O&M support, infrastructure improvements, better maintenance options
- Processes methods, techniques
- Better O&M results without annual appropriations
- Discipline in execution
- Forced integration of weighing upfront costs vs. long-term operating costs
- Design for durability, quality

P3s – The New State Models?

- Will P3 bills make a difference?
- Creates a predictable, fair, transparent road map for structuring and approving future P3 projects
- Balance risks and potential revenues between public and private sectors; outputs v. outcomes means public may have to give up more to secure benefits
- Requires open, competitive solicitations for all future P3 projects; some projects are better than others
- Allows private sector to propose ideas and solutions in the form of unsolicited proposals
- Updates procurement processes in states, federal government
- “Value for money” baseline for comparison
- Offers on alternative to service contracts, complexity, with limits on owner, use of property, transparency

Canada's P3 Model

This model should be studied, has performance and data for past decade:

- Structure
- Sufficiency
- Scope
- Savings
- Speed

- Company/board/professional management
- Talents/tools BUT no bureaucracy, self-sufficiency
- Full assets/functions/services/O&M
- 10% savings on - $400M budget, 30 year life cycle budgets
- Projects ahead of schedule / operations catch up?

Savings of P3's come over time, not up front. Cashflows match with patient sources of capital – bonds, SWF's, insurance, pension investors

Specialty funds and some private equity interests.

Pricing of risk transfer as private sector risk aversion escalates. Federal risk is effectively self-insured

Risk = Control, not necessarily monies

Quantification of risk – subjective

Education, standardization

Modeling – best in Canada

Match risks with party's ability best to assume and manage such risks

Funding Challenges – Non-Profits

- Skyrocketing operating costs
- Scaling back needed services is rising; stuck at 2% of GDP for decades
- Grants have been cut back and are more competitive; no leveraging
- Charitable giving significantly down (9.5% in 2009)
- At risk with current budget & tax reform talks in Congress
- Mission creep; leadership transformation

P3's – Social Enterprise

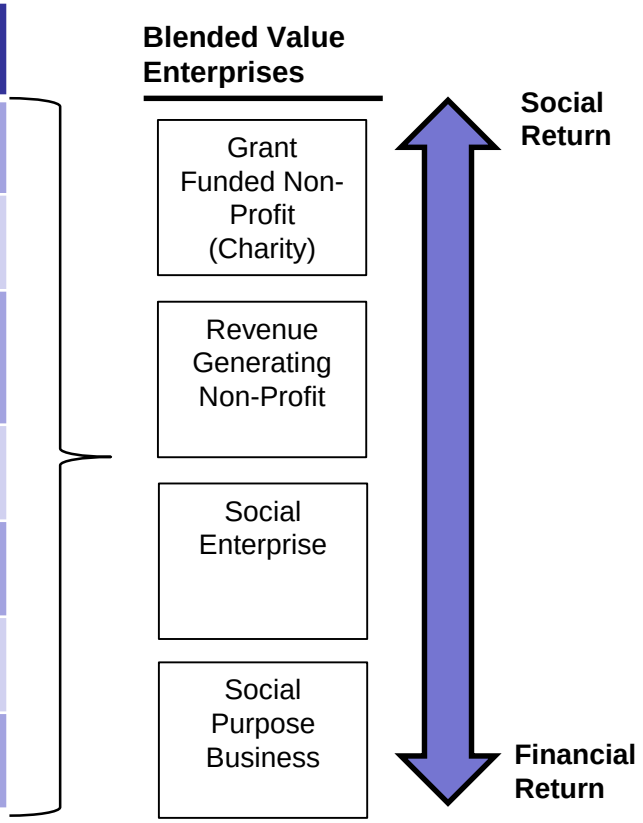
- The P3 model has a rich history for social enterprise investment in EU, Asia and Canada. Decades of examples include:
  - affordable housing
  - schools
  - social demand services
  - hospitals
  - prisons
  - colleges/food/energy efficiency/dormitories/campus hotels
- US state leadership here in MA, NY

Social Impact Contracts – What are they?

- A Social Impact Contract is a contract with the public sector in which it commits to pay for improved social outcomes. Payout only occurs based on performance.
- On the back of this contract, investment is raised from socially-motivated investors.
- This investment is used to pay for a range of interventions to improve the social outcomes.
- The financial returns investors receive are dependent on the degree to which outcomes improve. Performance is rewarded.
- Green bonds are new market phenomenon.

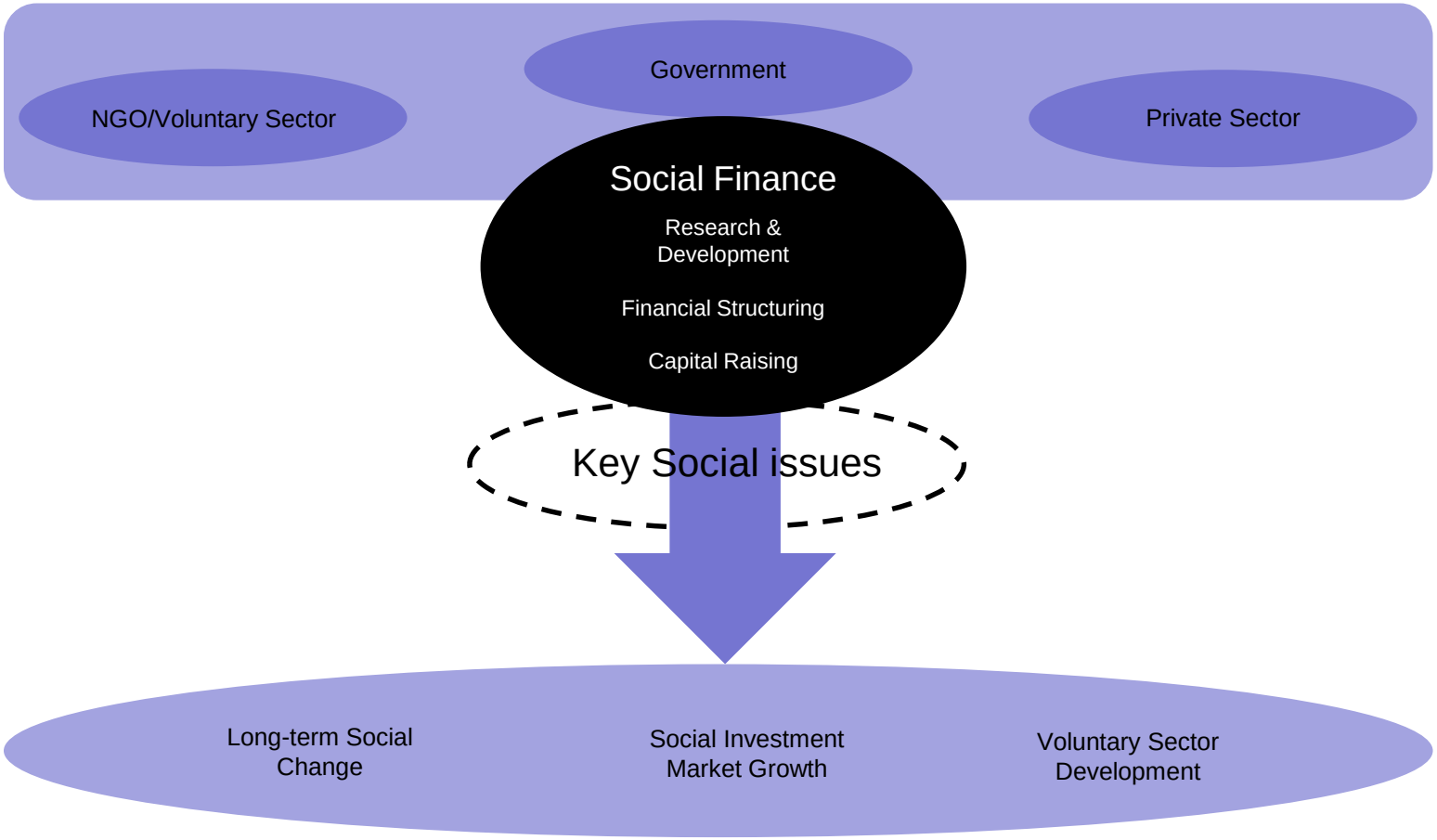
Emerging “Hybrid” Structures

Stakeholders	Enabler	Investor/ Funder	Financial Intermediary
Academics	✓		
Capacity Builder	✓		
Governments	✓	✓	✓
Grantors		✓	
Foundations	✓	✓	✓
Banks/Credit Unions		✓	✓
Investment Mgmt Firms			✓



Source: Cardno ENTRIX

Social Impact Performance Contracts



Source: © Social Finance

P3s – Federal Call to Action

- Federal policies and actions:
  - Congressional – TIFIA, WIFIA
  - White House / Agency – P3 Offices
  - OMB
  - DOT, DOD
  - Presidential P3 Commission
  - Construction, jobs and economic stimulus
- Less Federal support on non-profit, social funding; more on infrastructure replacement

P3s – What's Next?
Opportunities for States

- Best Practices in States – see PA, MI, CO, IL, VA, TX, FL, PR as successes
- Joint Program Examples – funding vs. financing, regional approaches in PAC NW
- States to Watch – see MD, NC, AK, CA, NY, AL
- States with Opportunities
  - Large transportation, water and energy infrastructure
  - Mega infrastructure – city redevelopment, St. Elizabeth's – Anacostia
  - Smaller municipal projects i.e street lighting, libraries, 911 systems, parking, dormitories, water restoration
  - Reinvestment in existing infrastructure
  - Federal limits may constrain taking on good deals
  - Bundling of projects to create scale
  - Water – caps on private activity bond financing; TIFIA structures for water
  - Other uses in social infrastructure, dream contracting

Conclusion

- The U.S. doesn't have a choice. With Federal support especially in transportation and water, and 34 states considering P3 legislation, market acceptance and barriers must be removed.
- P3 is the epicenter in U.S. of the next generation of infrastructure procurement/investment vehicles. Infrastructure debt is better spent than entitlement debt.
- Smart and effective implementation in the U.S. will lead to attracting pension, sourcing wealth fund, insurance and private equity to modernize U.S. capacity and infrastructure.
- U.S. must solve several P3 challenges to succeed in U.S.:
  - P3 must compete with $400 billion tax, exempt bond market
  - Lack of experience and education of stakeholders
  - Lack of investment review capacity and education needed
  - Increase adequacy of quality deal flow
  - Mismatch between development/investment objectives; resolve control and return issues
  - Politics and legislation intrusion and risk
  - Certainty for long term planning and execution
- Need for education – information – standards – and execution in the U.S.