Alternative Financing Structures

Public-Private Partnerships

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I. Overview of Public-Private Partnerships

Public-Private Partnerships provide a new source of capital for state and local governments

Historical Option #1
Raise taxes

- More taxpayer burden immediately

Historical Option #2
Issue tax-exempt bonds

- Allows conservative amount of debt to fund projects

New Option
Public-Private Partnership

- Can be structured to avoid impact on taxpayers
- More capital for give project (debt and equity)
- Operating risk shifted to private party

While several strategies exist to implement and finance infrastructure assets, PPPs offer a unique alternative

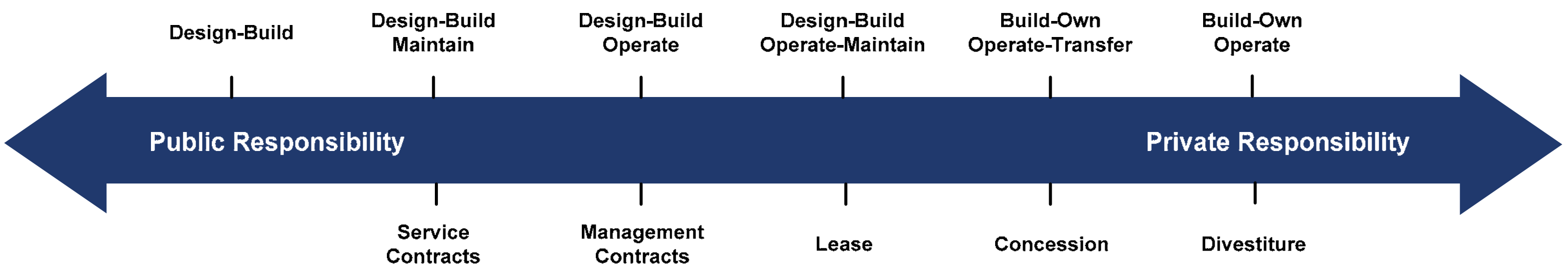
Strategy	Description
1) Public Ownership	Traditional toll/revenue system – design, construction, O&M, governance, etc., remain with municipality
2) Public Ownership/Private Contracting	Same as above except certain activities may be contracted for – i.e., design/construction, etc.
3) Public-Private Parternship	Public owns facilities and maintains governance, enters into lease agreement with a private entity that is responsible for operations, maintenance, construction
4) Private Ownership	All activities, including the setting of rates, are controlled by a private entity

Public Private Partnerships (PPP or P3)

- A Public-Private Partnership (PPP or P3), refers to a contractual agreement formed between a government agency and a private sector entity that allows for greater private sector participation in the delivery of public infrastructure projects
- In some countries involvement of private financing is what makes a project a PPP
- PPPs are used around the world to build and upgrade existing public facilities such as roads, airports, maritime ports, schools, hospitals, waste and water treatment plants and prisons
- Compared with traditional procurement models, the private sector assumes a greater role in the planning, financing, design, construction, operation, and maintenance of public facilities. Risk associated with the project is transferred to the party best positioned to manage it

Common PPP Models

NEW PROJECTS



EXISTING SERVICES AND FACILITIES

New Projects

Design-Build (DB)	The government contracts with a private partner to design and build a facility in accordance with the requirements set by the government. After completing the facility, the government assumes responsibility for operations and maintenance
Design-Build-Maintain (DBM)	This model is similar to Design-Build except that the private sector also maintains the facility. The public sector retains responsibility for operations
Design-Build-Operate (DBO)	Under this model, the private sector designs and builds a facility. Once the facility is completed, the title for the new facility is transferred to the public sector, while the private sector operates the facility for a specified period
Design-Build-Operate-Maintain (DBOM)	Combines the responsibilities of design-build procurements with the operations and maintenance of a facility for a specified period by a private sector partner. At the end of that period, the operation is transferred back to the public sector
Build-Own-Operate-Transfer (BOOT)	The government grants a franchise to a private partner to finance, design, build and operate a facility for a specific period of time. Ownership of the facility is transferred back to the public sector at the end of that period
Build-Own-Operate (BOO)	The government grants the right to finance, design, build, operate and maintain a project to a private entity, which retains ownership of the project. The private entity is not required to transfer the facility back to the government
Design-Build-Finance-Operate / Maintain	Under this model, the private sector designs, builds, finances, operates and/or maintains a new facility under a long-term lease. At the end of the lease term, the facility is transferred to the public sector

Existing Services and Facilities

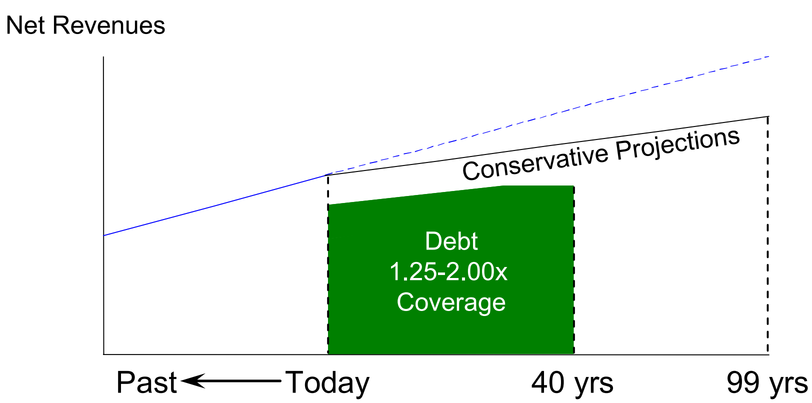
Service Contract	■ The government contracts with a private entity to provide services the government previously performed
Management Contract	■ A management contract differs from a service contract in that the private entity is responsible for all aspects of operations and maintenance of the facility under contract
Lease	■ The government grants a private entity a leasehold interest in an asset. The private partner operates and maintains the asset in accordance with the terms of the lease
Concession	■ Grants a private entity exclusive right to provide operate and maintain an asset over a long period of time in accordance with performance requirements set forth by the government. The public sector retains ownership of the original asset
Divestiture	■ The government transfers an asset, either in part or in full, to the private sector. Generally the government will include certain conditions with the sale of the asset to ensure that improvements are made and citizens continue to be served

II. Structuring Considerations

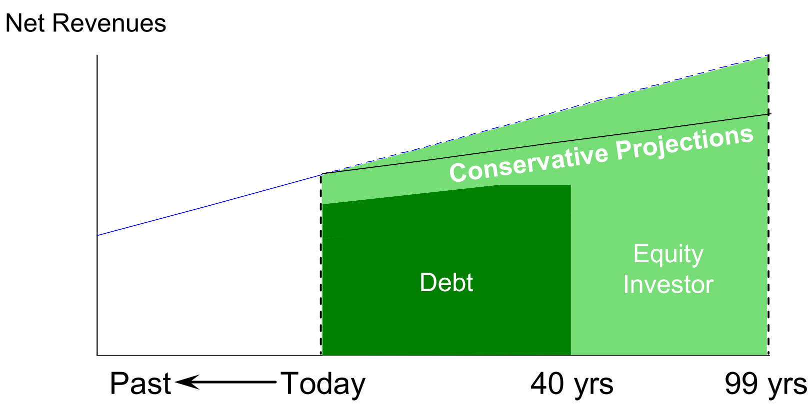
Concession leases provide an opportunity to capture the "growth wedge" in volume and revenue increases

- Municipal bond investors rely on historical revenues to determine the leverage levels which constrains total value for the owner
- Equity investors look for future returns based on growth
- Debt + Equity = Greater Proceeds for Owner of Asset

Municipal Bond Market



Concession Sale



Structuring a Concession Agreement

- **Concession Agreement** – A legal document that evidences a long-term lease of a public asset by a private operator.

Public Bond Retains		Private Operating Accepts
1) Up-front Payment by Private Operator	→	Construction duties and related construction risk
2) Oversight of Operation	→	All operating responsibilities and costs
3) Rights to mandate operating performance under the agreement	→	Requirements to expand/enhance the asset and related costs
4) Rights to expand/enhance asset beyond those specified in agreement	→	Reporting responsibilities to public body
5) Right to cancel agreement if Private Operator doesn't perform	→	Asset's revenues throughout life of agreement

Public policy decisions will have a substantial impact on the shape and form of the concession

Policy Decision	Description	Considerations
■ Term of Concession	■ Length of time that a concession partner will be allowed to lease and operate the asset	■ What is political sensitivity to 99-year concession? ■ What is value of incremental term length?
■ Fees	■ Fee limits will be mandated	■ Public appetite for future increases ■ What is the elasticity of demand?
■ Expansion/Enhancements	■ Will the municipal entity allow or mandate future expansion / enhancements to the asset	■ What enhancements are necessary ■ Future expansion if capacity constrained
■ Non-Compete	■ Potential commitment of the municipal entity to compensate if future development causes competition issues.	■ Is this good public policy? ■ What are future capital plans that could have an impact if any?
■ Construction Requirements	■ Capacity constraints if any and other requirements ■ Materials and methods	■ Allowance for phasing could enhance feasibility ■ What construction factors are important?
■ Operating and Maintenance Standards	■ Manual of specific operation conditions and rules to which a concession partner must adhere	■ What are operating and maintenance conditions that are most important?
■ Labor	■ Status of existing employees ■ Conditions for new concession company employees	■ Will the concessionaire be held to the municipal entity's employment standards?
■ Environmental	■ Responsibility for existing potential environmental liabilities (if any)	■ Are there any known environmental liabilities?

III. Availability Payment Models

Goldman Sachs

Public-Private Partnership Models

Full Concession Model versus Availability Payment Concession Model

Full Concession Model

Revenue Generating Assets

- Toll roads
- Maritime ports
- Airports

Premise: Concessionaire will typically pay an up-front amount in exchange for future revenues

Availability Payment Concession Model

Subsidized Assets

- Transit systems
- Non-tolled roads
- Hospitals

Premise: Concessionaire will build and / or operate an asset in exchange for a rent-like payment stream from the public sponsor

P3 availability concession structure can:

- Transfer risk (construction, financing, O&M)
- Reduce Costs
- Increase the certainty of execution
- Accelerate funding / project completion
- Provide for other construction benefits

Public-Private Partnership Models

Full Concession Model versus Availability Payment Concession Model (Continued)

Full Concession Model

- When assuming similar revenue projections, a concession financing may produce similar results to a traditional tax-exempt bond financing
- The State's goals with respect to project construction, operations, and maintenance are contained in the concession agreement
- Value can be gained when a concessionaire applies their own parameters for assessing the risks and revenues associated with the construction and operation of the asset
  - Concessionaire can take a more aggressive view on revenue growth and operating margins
  - Concessionaire may assume lower construction cost and on-going Capex and maintenance expense
  - In a typical concession, target return on equity ranges from 10-14% – however return on equity is not guaranteed as the concessionaire is assuming operating risk
  - Concessionaire will assemble competitive debt and equity capital structures to finance the project

Availability Payment Model

- The State makes ongoing rent-like payments to private concessionaire for ability to make the project "available"
  - As with the full concession model, the State's goals with respect to project construction, operations, and maintenance are contained in the concession agreement
  - Payments to concessionaire depend upon performance, with clear penalty system to ensure the concessionaire is bearing meaningful risk (e.g. construction completion risk or ongoing O&M risk)
  - Concessionaire has an incentive to manage maintenance programs efficiently in order to avoid disruption to users and maximize payments
- Structure allows for cost effective financing for the concessionaire
  - Typically concessionaire's debt viewed favorably by rating agencies, depending on the likelihood of breaching availability conditions and construction risks
  - Concessionaire uses the availability payments to pay for operations and maintenance, and to repay debt and equity
- State/sponsor payments to concessionaire
  - Are a binding obligation (subject to appropriations); not viewed as debt to the State

IV. Public Relations and Key Issues for Private Investors

Key Considerations when Approaching the Public

Frame the Issue

- Solve a Problem: Use funds to solve a major problem. Lead with the solution
- Describe it as a “Partnership” or “Lease”, not a “Sale” or “Privatization”
- Emphasize Continuing Government Control
- Frame as a Non-Partisan Issue

Engage the Public

- Anticipate and engage key stakeholders – Lawmakers, Unions, Geographic Players
- Carefully construct proceeds distribution plan – spread the benefits
- Educate clearly – simplify a complicated issue

Use Effective Messaging – Indiana Case Study

What Works

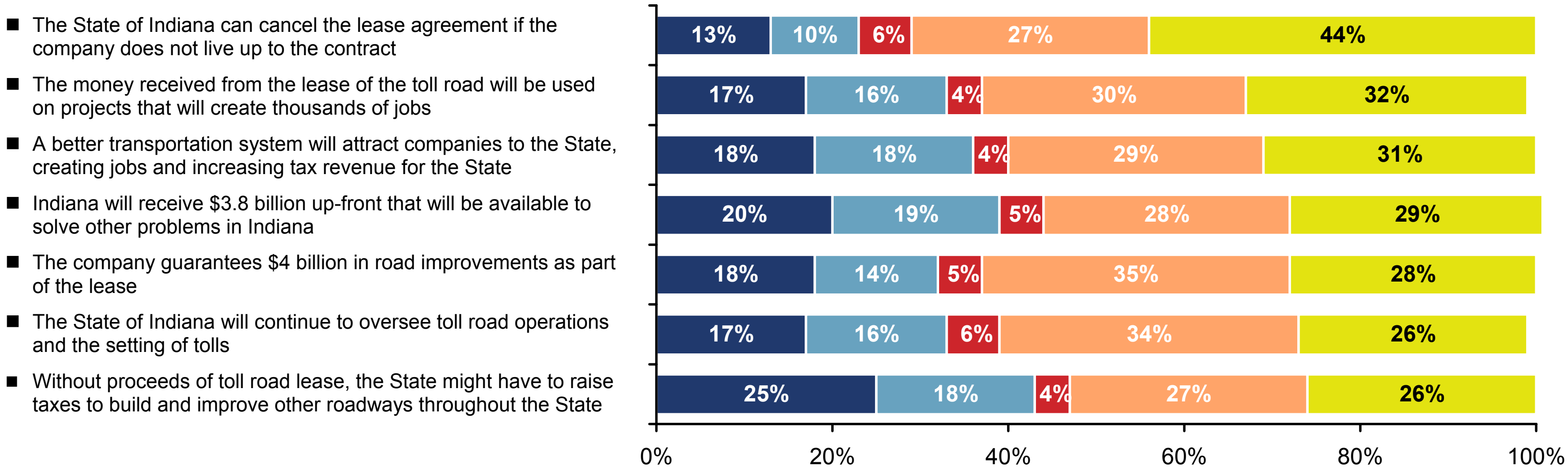
- Government Control
  - Cancellation Rights
  - Continuing Oversight
  - Ownership Remaining with Government
- Public Benefit
  - Jobs / Economic Development
- Proof of Success
  - Highlight successes at every step

What Doesn’t

- Focusing on Efficiencies of Private Sector over Public Sector Control
- Threatening tax increases or more debt without the transaction
- Being branded as a “sale”
- Foreign involvement without an explanation providing an easy target for opponents

Indiana Toll Road Support and Opposition Messaging

Please tell me how persuasive each statement is as a reason to *support* leasing the Indiana Toll Road to Statewide Mobility Partners



Please tell me how persuasive each statement is as a reason to *oppose* leasing the Indiana Toll Road to Statewide Mobility Partners