Evaluating Public-Private Partnerships for State Transportation Projects

Final Presentation to JTC

December 7, 2011

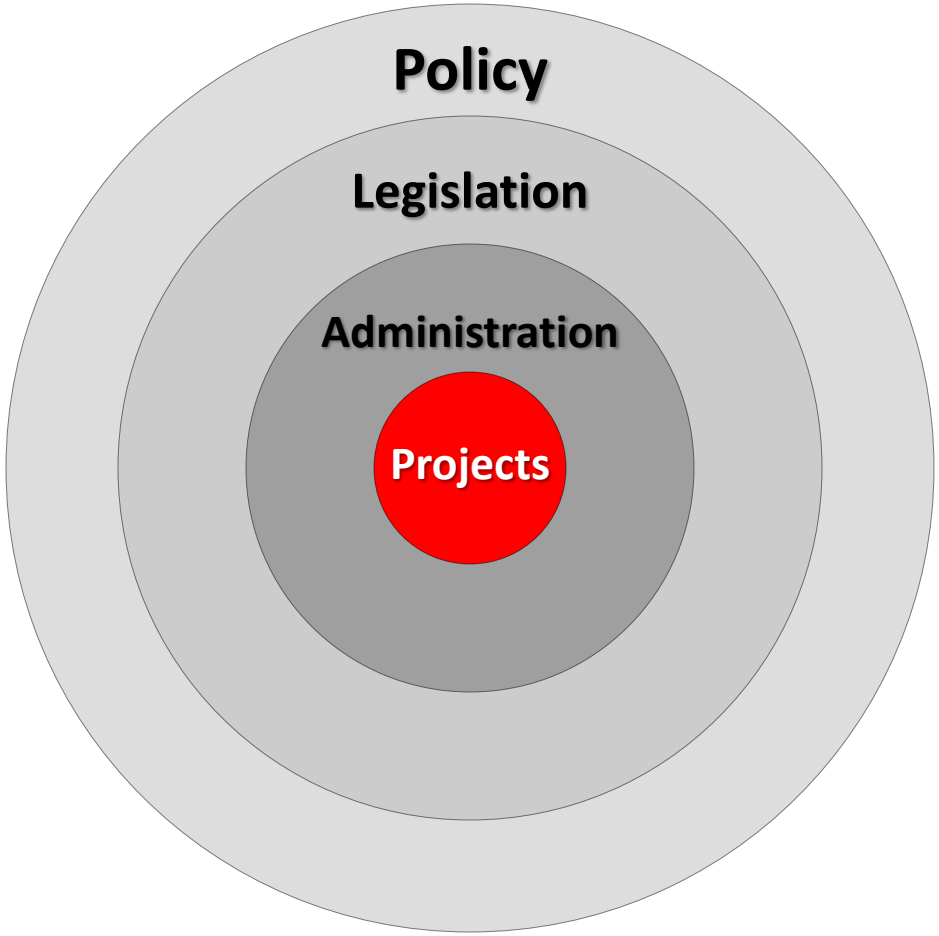
Overview

- 30 minute presentation followed by 15 minute Q&A
- Summary of study scope and milestones
- Presentation of findings and recommendations
  - Screening assessment of the five candidate projects
  - Strategic recommendations for:
    - Policy
    - Legislation
    - Administration
    - Next Steps

Study Outline: Milestones and Deliverables

	Educational Process	Screening Tool		Financial Model		Report	
Date (2011)	Presentations and Public Meetings	Develop Tool	Assess Projects	Develop Inputs	Develop Models	Run Model Scenarios	Draft and Final
July	July 12 Staff Workgroup kickoff meeting July 13 presentation to JTC						
August	August 2-3 2-day educational workshop with Policy Workgroup						
September	Sep 15 SWG meeting Sep 29 PWG meeting and table top dry run						
October	Oct 13 SWG meeting Oct 24 Table Top exercise with PWG						
November	Nov 9 SWG Meeting Draft Report due Nov 28						
December	Dec 6 PWG meeting and presentation of findings Dec 7 Final presentation to JTC						
January	Presentation of findings to House and Senate						

Overview



In developing recommendations it is critical to understand the ideal relationship between Policy, Legislation and Administration:

- *Policy is all encompassing and defines the needs, preferences and objectives of the State as concisely as possible*
- *Legislation should be designed to fully reflect the State's policy objectives – and in its purest form is simply a tool for implementing such policy*
- *The State's Administration is tailored to empower the Policy objectives of the State, within its legislative architecture*
- *Projects should only be attempted within this framework*

Policy Recommendations

1. Adopt a policy framework that identifies a number of minimum public interest protections that must be assumed to be binding requirements of all future P3 projects, implementable and enforceable through statutes and/or mandatory guidelines.

2. Utilize the two-step screening tool developed by the JTC to determine if a project is suitable, from an initial qualitative perspective, to be advanced as a P3.

3. Employ the financial model developed by the JTC study to determine whether Value for Money is greater in a P3 approach compared to a traditional delivery method.

Development of Legislation: Context

Legislation must address all phases and facets of P3 projects:

- Phases of P3 Projects
  - Project identification and screening (for P3), planning of funding sources
  - Procurement including the development of tender process and documents, project agreements, bid conditions (bid bonds etc); and the management of Best and Final Offer (BAFO) and Financial Closing periods
  - Construction and Operating Periods
  - Handback or Termination
- Facets of P3 Projects
  - Relationship and interaction between the public and private sector
  - Project related stakeholder outreach (PR)
  - Tolling and operations by private and public parties
  - Public and private funding and execution of construction and operations
  - Solicited and/or unsolicited proposals
  - Ownership and tax treatments
  - Approval and enforcement of binding project agreements, control and oversight

Legislative Recommendations

Washington State should revise current P3 legislation to encompass public interest protections, ensuring that for every project advanced key policy goals are upheld. These protections include:

1. The State should maintain control and/or ownership of assets involved in P3 projects.
2. Value for Money must be assessed and show a positive value before the State pursues a P3 project.
3. Upfront payments generated by P3 projects to the State by the private partner should be used only to address transportation needs, and not diverted to pay for other government costs.
4. The long-term quality of service delivered in a P3 project must be ensured through stringent contract provisions and ongoing oversight.
5. The State must safeguard against private partners realizing excessive returns.
6. P3 projects should possess the same State apprenticeship requirements as any other public works project.
7. P3 projects should conform to the State's toll setting policy, rather than allowing the private sector to change toll rates.

Legislative Recommendations - Continued

Washington State should revise current P3 legislation to encompass public interest protections, ensuring that for every project advanced key policy goals are upheld. These protections include:

8. Through contractual and legislative provisions, the State must ensure that the private partner selected will be solvent and able to deliver over the long-term.
9. The State should maintain the ability to terminate a P3 contract, or concession agreement, if the private partner is not able to deliver according to the performance specifications of the contract.
10. The P3 contract should clearly specify the condition the asset must be in when the long-term lease concludes.
11. Prevailing wage laws should be adhered to for all P3 projects.
12. Minority and Women-Owned Business Enterprises (MWBEs) should be encouraged to participate in P3 initiatives.

Legislative Recommendations - Continued

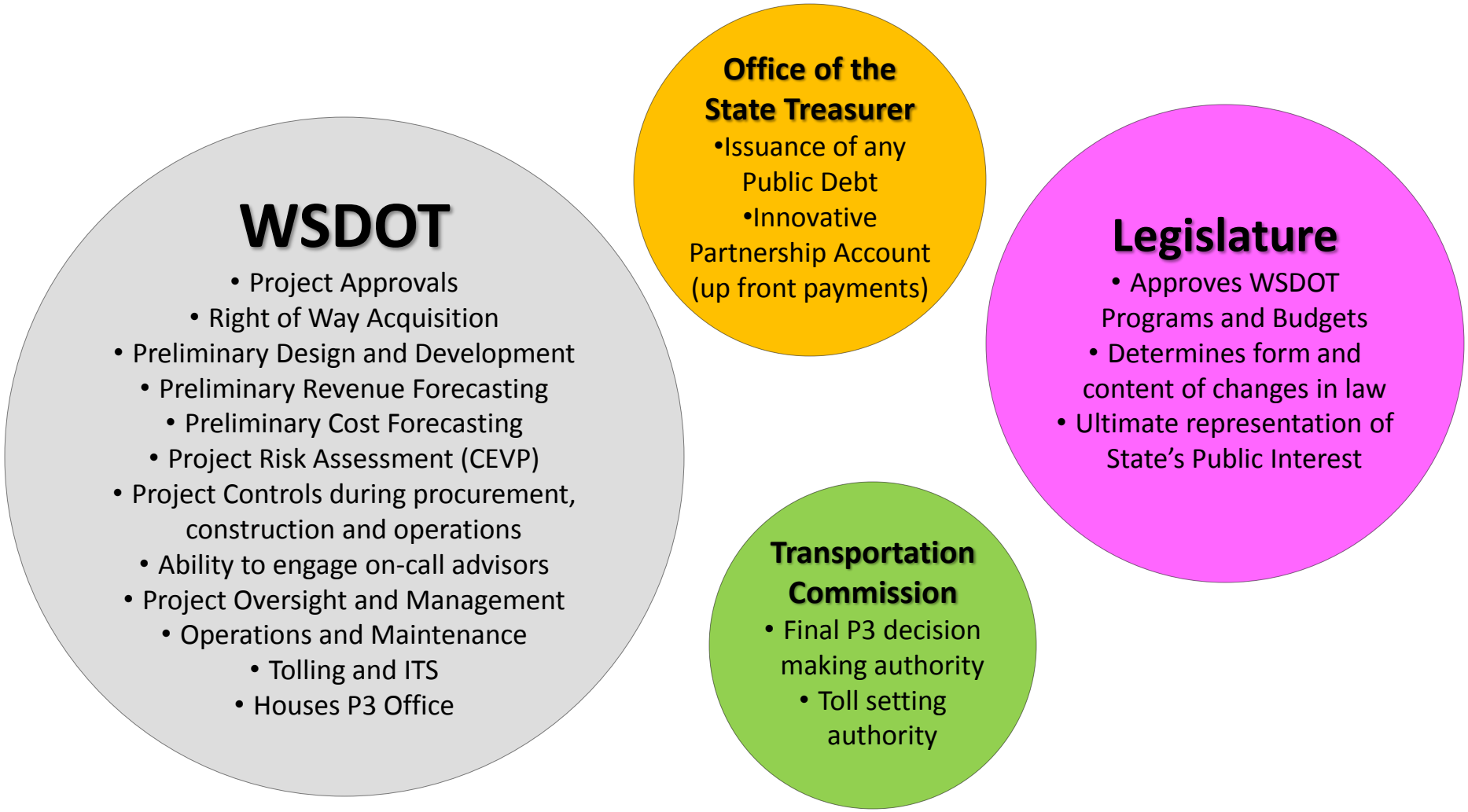
- Washington State Should
  - Draft new legislation that eliminates provisions in existing P3 law that prohibit innovatively financed projects
  - Encompass public interest protections in new law, ensuring that for every project advanced key policy goals are upheld.
  - Take a programmatic approach to P3 project delivery by authorizing the creation of a centrally located oversight office within the Department of Transportation that is responsible for upholding public interest concerns and facilitating projects in the best interest of the public and private sector. The legislature should adequately fund this P3 office.
  - Clearly authorize a full range of procurement structures and tolls, such as two-step procurements (Request for Qualifications (RFQ)/shortlisting and Request for Proposals (RFP)), and a period for dialogue with proposers.
  - Remove the post-procurement discretionary action by the State Transportation Commission and other post-procurement, pre-execution processes. Such existing requirements will preclude the State from undertaking any major P3 projects.
  - Enable the use of privately arranged or issued debt financing, and allow the private partner to realize a return on equity.

Legislative Recommendations - Continued

- Washington State Should
  - Eliminate provisions directing toll revenues into the transportation innovative partnership account and making expenditures from toll revenues subject to appropriation.
    - These provisions should not adversely affect private sector financing of eligible projects.
    - Toll revenue expenditures should be freed from legislative appropriation.
  - If lawful, Washington State should enable the use of continuing appropriations that would allow for availability payment contracts to be advanced.
  - Expand the scope of eligible transportation projects.
  - Enable conduit issuance of private activity bonds.
  - Improve control over unsolicited proposals.
  - If necessary, Washington State should rectify any insurmountable barrier to the use of P3s created by existing provisions concerning the state personnel system reform act.
  - New legislation should address its relationship to other state laws.

Current Administration: Internal Resources

Recommendation: maximize use of existing internal capabilities



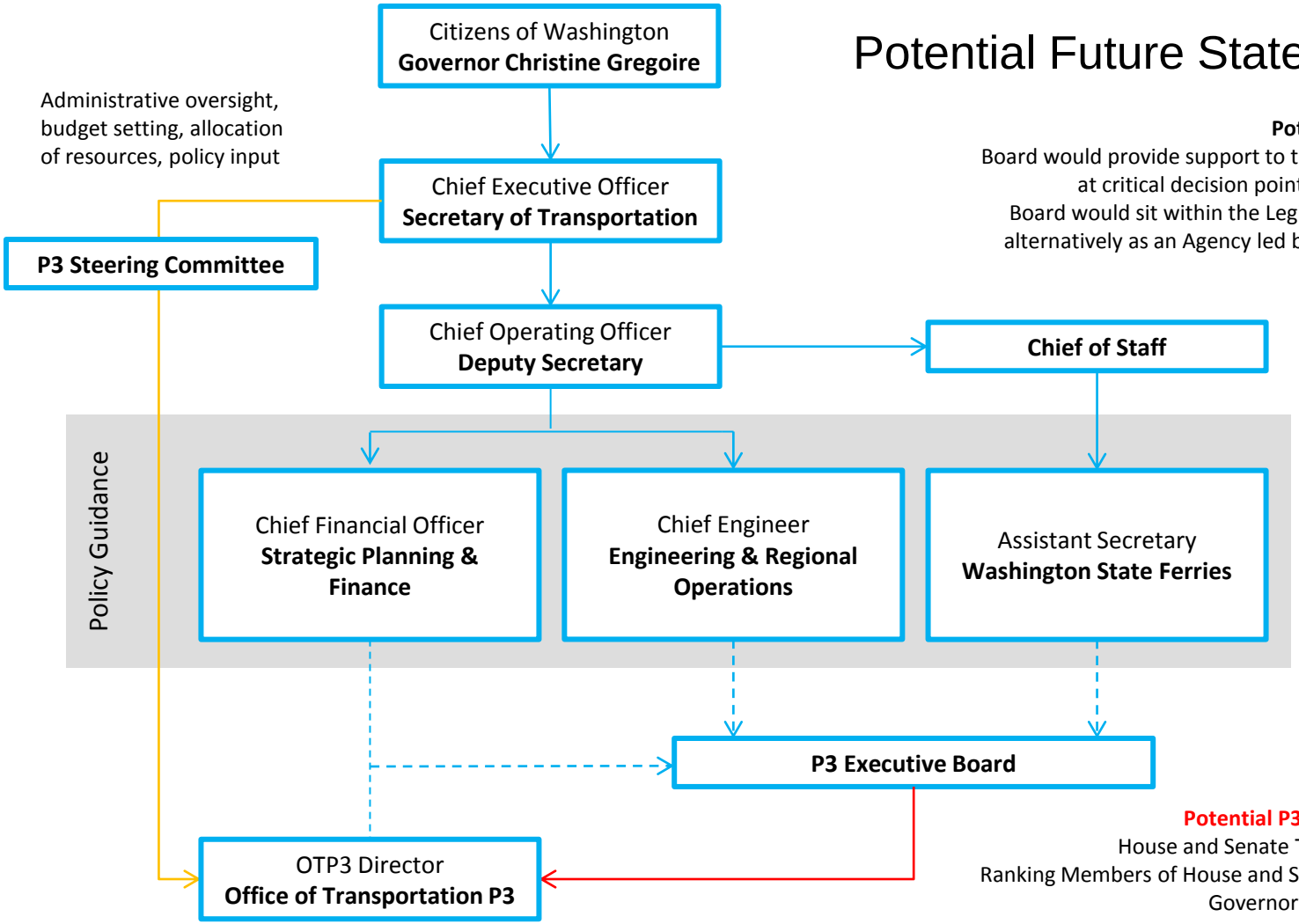
Administration: Recommended Resources

The following table provides recommendations on which internal and external resources should be engaged at each identified Phase. Recommendations are based on the current function and resources of relevant internal bodies, and industry standard use of advisors

Development Phase	WSDOT	Transportation Commission	Legislature	Financial Advisor	Legal Advisor	Tech Advisor / IE
Phase 1 – Initial	P3 Office	Information Only	Approval Required	Recommended (or on call)	Required	Optional
Phase 2 – Minimum Steady State	P3 Office	Information Only	Input through P3 Exec Board	Optional	Optional	Optional
Phase 3 – Preliminary Project Development	P3 Office Project Staff		Input through P3 Exec Board	Recommended (or on call)	Recommended (or on call)	Recommended (or on call)
Phase 4 – Project Development	P3 Office Project Staff		Input through P3 Exec Board	Required	Required	Required
Phase 5 - Construction	P3 Office Project Staff		Input through P3 Exec Board	Recommended (or on call)	Recommended (or on call)	Required
Phase 6 – Operations	P3 Office	Information Only	Input through P3 Exec Board	Recommended (or on call)	Recommended (or on call)	Required

Administration: Organizational Context

Potential Future State P3 Structure



Potential P3 Executive Board Remit:
Board would provide support to the P3 office on behalf of the State at critical decision points – refer following slide for detail.
Board would sit within the Legislative Branch (recommended) or alternatively as an Agency led by Governor-Appointed Executives

Potential P3 Steering Committee representation:
WSDOT Capital Program Development and Management
WSDOT Chief Operating Officer
WSDOT head of the Toll Division
WSDOT Operations Manager

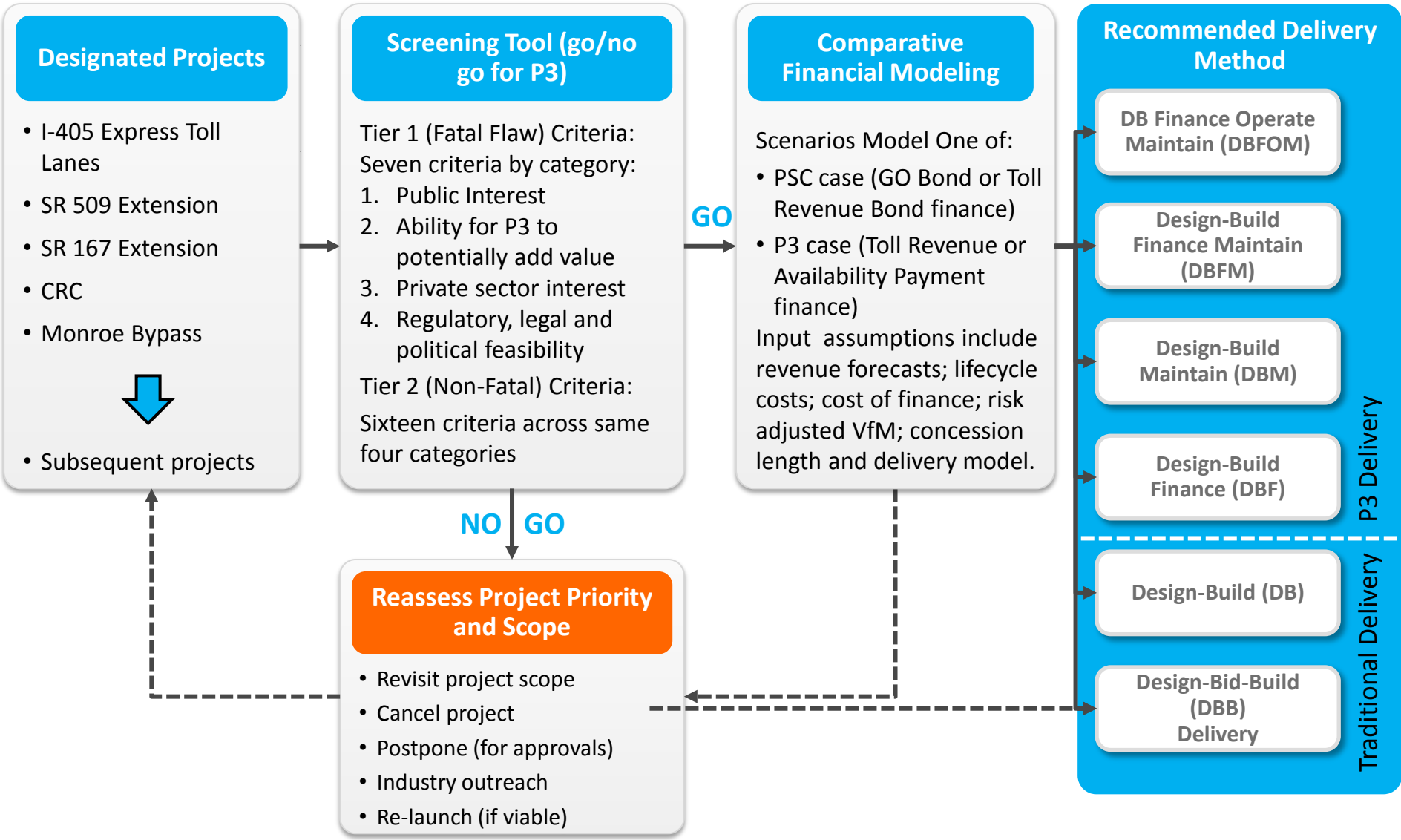
Potential P3 Executive Board representation:
House and Senate Transportation Committees Chairs
Ranking Members of House and Senate Transportation Committees
Governor's Office of Financial Management
State Treasurer's office
Transportation Commission

Administration: P3 Office Staffing and Funding Recommendations

- Washington's P3 office will need initial seed capital to fund organizational costs such as staff, normal administrative expenses, and outside technical, legal and financial advisors (which vary over time per slide 23)
  - We recommend initially, a core staff of 1 or 2 Full Time Employees (FTEs) supplemented by WSDOT Project Staff and potentially staff from other agencies as required based on skill sets
  - New hire FTEs must have first-hand experience executing P3 projects and be capable of building institutional knowledge across financial, commercial, legal, technical and process issues
  - In house staff should be sought with an understanding of project delivery, project planning, State finance and procurement, along with private sector individuals that bring a mix of project finance, project management, legal, market awareness, and other relevant skill sets required to adequately and expeditiously fulfill the P3 Office's charge.
- The State should permit and encourage the P3 office to pursue cost recovery through application fees, transaction fees and periodic/ongoing service fees

Assessment of Projects

Screening Process



Screening Tool Findings

Project	Tier 1 (Fatal Flaw) Criteria			Tier 2 (Non-Fatal) Criteria		Overall Result
	Fatal Flaw Triggered?	Pass with limitations scores		Pass with limitations scores		
		Score Result	Failing Score	Score Result	Failing Score	Pass / Fail
I-405 / SR 167 Express Toll Lanes	No	5	11	13	24	Pass
I-5/SR 509 Extension	No	0	11	10	24	Pass
SR 167 Extension	No	10	11	12	24	Pass
Columbia River Crossing (CRC)	No	4	11	13	24	Pass
Monroe Bypass	**Yes**	**17**	11	20	24	**Fail**

- All projects passed assessment other than Monroe bypass, which failed due to two fatal flaw criteria
  - Criterion 1.02.01: Financial Feasibility – Due to the lack of a viable revenue stream, the project is not financially self supporting and no additional sources of funding have been identified. The project can therefore not be considered affordable to the public until this assessment improves
  - Criterion 1.04.01: Environmental approvals expected within three years – This will not be possible until the project EIS is recompleted, submitted and nearing approval

General Financing Assumptions: All Projects

General Assumptions	
Term	• Availability payment: 35 years + construction period • Toll concession: 50 years
Taxation	• Federal: 35% corporate tax • State: .05% state gross receipts tax
Discount rate	• Project and debt cash flow: 7% • Excess cash flow / equity: 11%
Development costs	Publicly funded under all scenarios, not included in project financing
Inflation	• Inputs include inflation (2.5% per annum) • Availability payments: 20% inflated at 2.5%
Sensitivities	• Traditional delivery model: - 10% decrease to T&R • P3 delivery model: + 25% increase to T&R

- Sensitivities seek to reflect equity view of T&R for P3 delivery model and more conservative lender/rating agency view for traditional delivery model
- Availability payment models normally include an escalation factor that is applied to a portion of the availability payment to account for inflation-indexed costs (e.g., routine operations and maintenance)

Financial Model Results

I-405	**Project is fully funded under all delivery models** ■ P3 delivery model offers approximately $403M - $440M in additional Value for Money compared to GO and Toll Revenue bond financing, respectively ■ Key generators of VfM are accelerated project delivery schedule, cost savings, and risk transfer
SR 509	**Construction is fully funded under P3 model and may not require any public funds for all-in delivery** ■ P3 delivery model may generate a concession payment of $76M - $189M and has the potential to cover all project delivery costs including retained State risks and pre-development costs ■ Toll revenue bond generates $165M - $190M in excess cash flow to State over project term; however, up-front funding gap of $200M - $225M exists
SR 167	**Project economics are weak and require a public contribution under all delivery models** ■ While the P3 delivery model delivers $350M in additional Value for Money and leverages greater amount of financing, it requires a $74M availability payment beginning in FY 2018 ■ Annual toll revenue does not cover availability payments until FY 2033
CRC	**Significant construction costs are main contributor to funding gap under all delivery models** ■ Project still has negative $1,243M - $1,479M net project value ■ Availability payment P3 model offers marginal Value for Money when compared to traditional delivery model using GO bond financing and requires a $243M availability payment beginning in FY 2016. Annual toll revenue is unable to cover availability payments until FY 2044.

Next Steps

1. In this context, development includes preliminary design and ROW acquisition, in addition to all pre-procurement and procurement activities

Schedule: Milestone Recommendations

The State must reach political consensus that its policy is sufficiently well defined to pursue changes in legislation and administration. We recommend this be targeted for 2012 based on the findings of this study and ensuing debate

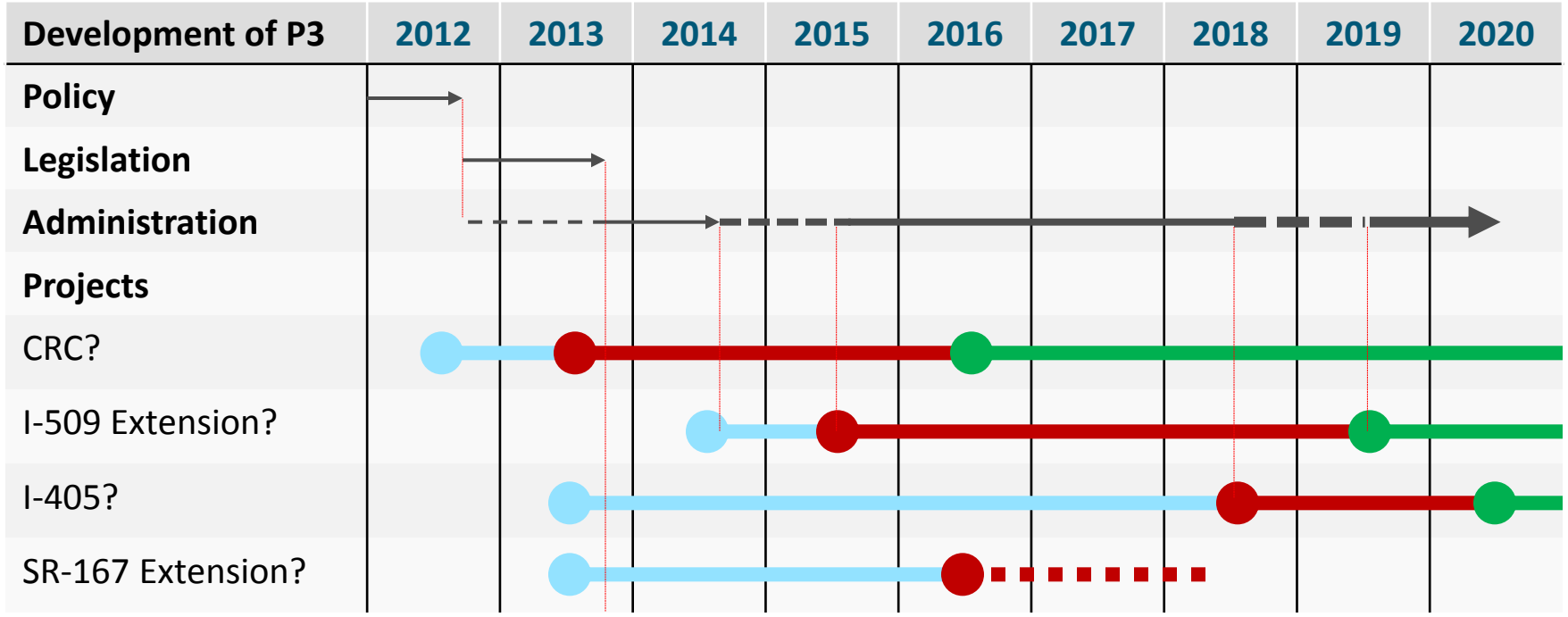
The effort to modify the State's P3 legislation could then start during 2012. The new legislation must be signed into law before the first P3 project enters procurement, and before initial P3 administrative changes are finalized

The State's P3 Administration must ramp up over time, initially to cover pre-procurement activities such as screening. Initial changes must take P3 legislation into account, and at a minimum be capable of supporting 1 procurement process

Project milestones for development[1] construction and operations phases (blue, red, green respectively) are shown below

This indicates that CRC procurement is probably too advanced for a P3 approach; while the 509 and 405 may be viable.

P3 Administration must continue to evolve over time in line with project needs (through development, procurement, negotiation, construction and operation phases); and with the number of P3 projects in process (see following slide)



Appendix

Administration: Organizational Considerations

Existing WSDOT Office of P3 Structure

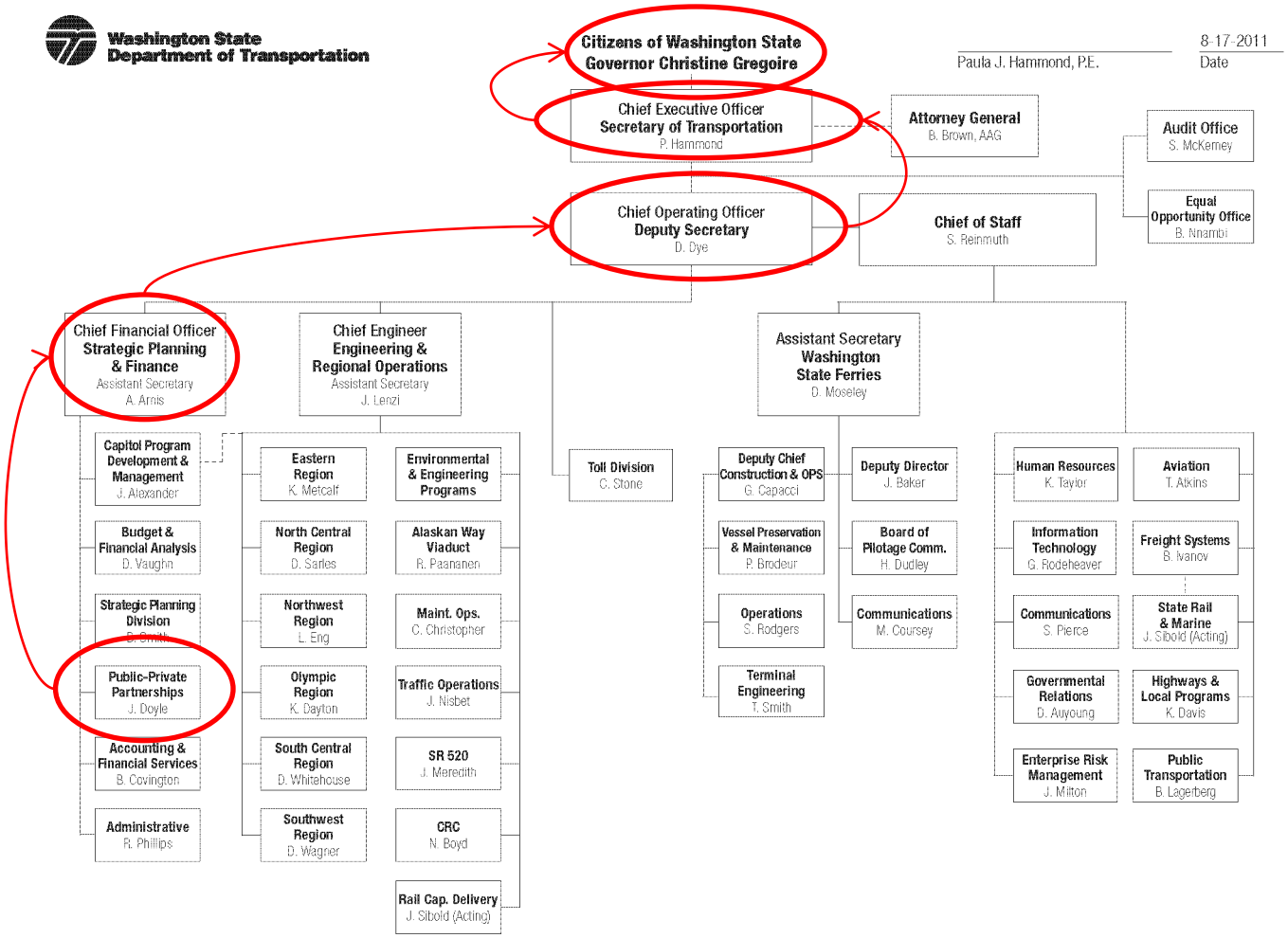
Citizens of Washington State
Governor Christine Gregoire

Chief Executive Officer
Secretary of Transportation
P. Hammond

Chief Operating Officer
Deputy Secretary
D. Dye

Chief Financial Officer
Strategic Planning & Finance
Assistant Secretary
A. Arnis

Public-Private Partnerships
J. Doyle



Administration: P3 Executive Board Approval Milestones

Project Phases and Primary Activities

- Projects screened for potential usage of PPP delivery model
- Where government elects to use PPP procurement method, project mandate assigned

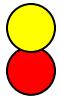
- P3 Executive Board must approve Request for Qualifications (RFQ) drafted by the P3 Office before it is issued to market
- If RFQ is approved by the Board the project is readied for the market and the RFP documentation prepared
- Initial Value-for-Money ("VFM") assessment prepared

- P3 Executive Board must approve Request for Proposals ("RFP") before it is issued
- Technical and commercial proposals of respondents evaluated
- Highest ranking proposals awarded right to finalize contract
- VFM assessment updated

- Potential negotiation and finalization of contract documentation
- VFM assessment finalized

- Construction progress monitored
- Initial operations monitored as required by project terms and stakeholder considerations

Governance Reporting

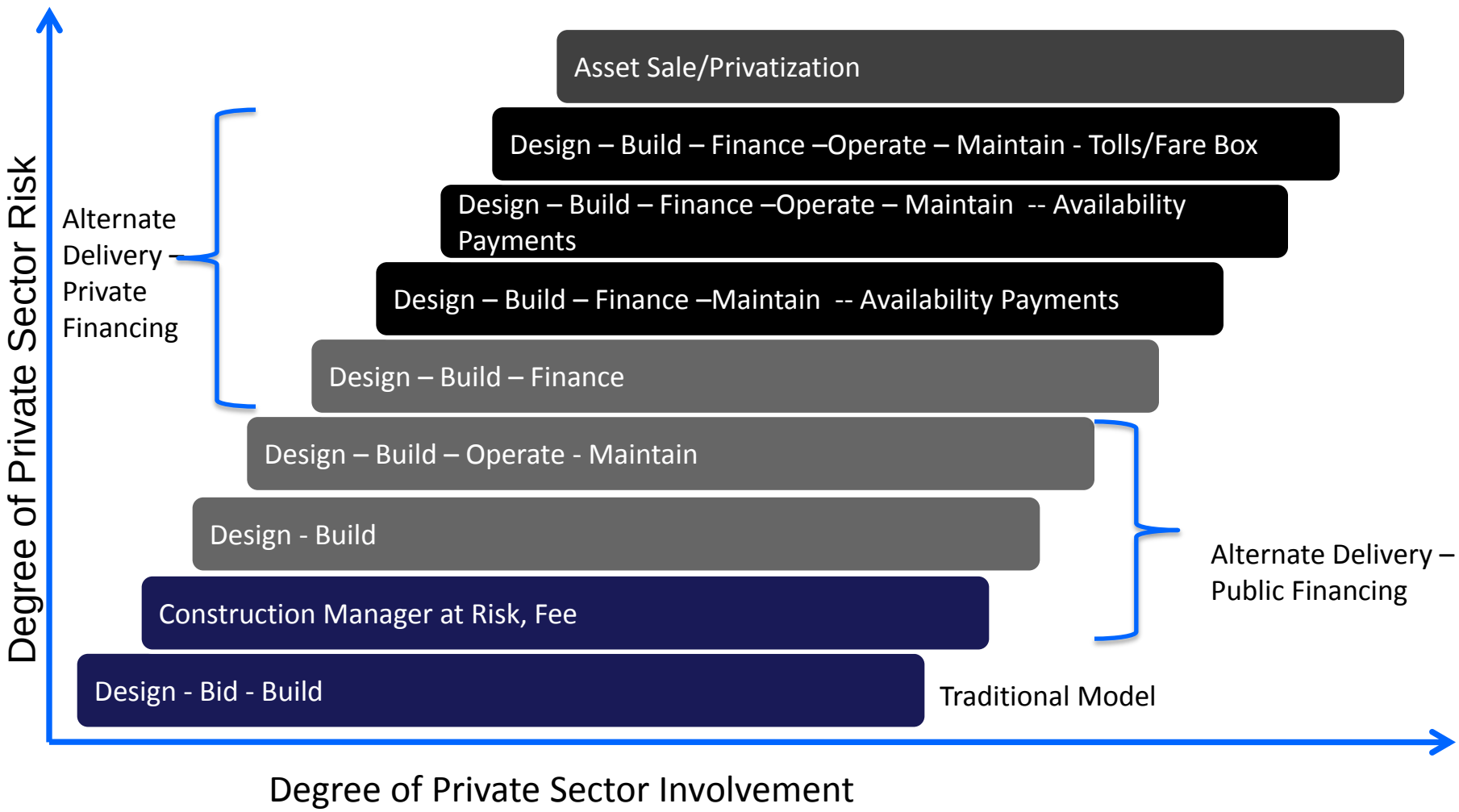


Board reporting provided at summary level, with detailed reporting on an exception basis, for the duration of the project phase

P3 Executive Board **approval** required to move into next project phase; Board reporting provided on a detailed project level

There are many different kinds of P3s

Project Delivery Options



Results Scenarios

Project	Public Sector			Private Sector	
	Public Sector Comparator (PSC)			Shadow Bid Model	
	Delivery Model	GO Bond	Toll Revenue Bond	Toll Concession	Availability Payment Model
I-405	DB	X	X	X	
SR 509	DB		X	X	
SR 167	DBB		X		X
CRC	DB	X	X	X	X
Monroe Bypass	NA	NA	NA	NA	NA

Results I-405

Type of Financing / Delivery Model	PSC	PSC	Shadow Bid Model
	GO Bond	Toll Revenue Bond	Toll Concession**
Concession Payment / (Public Contribution)	-	-	1,045,000
Excess Cash Flow	783,000	607,000 - 745,000	-
Retained Risks	(168,000)	(168,000)	(27,000)
Pre-Development Costs	(102,000)	(102,000)	(102,000)
Net Project Value	**513,000**	**337,000 - 475,000**	**916,000**
Value for Money	**—**	**—**	**579,000 (highest)**

$ '000s in Present Value (rounded)
** Represents debt service payments during construction, during operations paid from toll revenue*
*** Upside T&R revenue scenario not analyzed*

- **P3 toll concession has potential to generate better Value for Money to the State**
- **Under all delivery models, there is low/no funding gap and low/no requirement for additional public funds for delivery**
- **Accelerated delivery, cost savings, and risk transfer are key generators of VfM**

Results SR 509

Type of Financing / Delivery Model	PSC Toll Revenue Bond	Shadow Bid Model Toll Concession
Concession Payment / (Public Contribution)	(200,000) - (225,000)	76,000 - 189,000
Excess Cash Flow	165,000 - 190,000*	-
Retained Risks	(67,000)	(18,000)
Pre-Development Costs	(127,000)	(127,000)
Net Project Value	**(204,000) - (253,000)**	**(69,000) - 44,000**
Value for Money	**—**	**297,000 (highest)**

$ '000s in Present Value (rounded)
** Assumes funding gap can be filled to access these cash flows*

- **P3 toll concession has potential to generate better Value for Money for the State**
- **P3 toll concession is estimated to have low/no funding gap and may not require additional public funds for delivery**
- **Toll revenue bond has potential to generate $165M - $190M in excess cash flow to State; however, there is an estimated up-front funding gap of $200M - $225M**

Results SR 167

Type of Financing / Delivery Model	PSC Toll Revenue Bond	Shadow Bid Model Availability Payment
Concession Payment / (Public Contribution)	(478,000) - (491,000)	-
Excess Cash Flow	90,000 - 104,000 **	-
Availability Payments	-	(630,000)
Toll Revenue	-	518,000
Retained Risks	(116,000)	(41,000)
Pre-Development Costs	(244,000)	(224,000)*
Net Project Value	**(734,000) - (761,000)**	**(377,000)**
Value for Money	**—**	**384,000 (highest)**

$ '000s in Present Value (rounded)
** $20M in 'non-bid cost item' savings generated under P3 delivery model, **Assumes funding gap can be filled to access these cash flows*

- **P3 availability payment model has potential to generate greater Value for Money for the State**
- **P3 is estimated to require $74M AP beginning in FY 2018. Toll revenue does not cover APs until FY 2033.**

Results CRC

Type of Financing / Delivery Model	PSC Toll Revenue Bond	Shadow Bid Model Toll Concession
Concession Payment / (Public Contribution)	(1,722,000) - (1,746,000)	(865,000) - (1,101,000)
Excess Cash Flow	200,000 - 235,000*	-
Retained Risks	(124,000)	(47,000)
Pre-Development Costs	(331,000)	(331,000)
Net Project Value	**(1,942,000) - (2,001,000)**	**(1,243,000) - (1,479,000)**
Value for Money	**—**	**758,000 (highest)**

$ '000s in Present Value (rounded)
** Assumes funding gap can be filled to access these cash flows*

- **P3 toll concession has potential to generate better Value for Money for the State; however, both delivery models are estimated to require a large upfront public contribution**
- **Toll revenue bond model has potential to generate $200M - $235M in excess cash flow to State; however, it is estimated that a large upfront funding gap exists**

Results CRC

Type of Financing / Delivery Model	PSC GO Bond	Shadow Bid Model Availability Payment
Concession Payment (Public Contribution)	(1,120,000)	-
Excess Cash Flow	-	-
Availability Payments	-	(2,368,000)
Toll Revenue Offset (AP Only)	-	1,192,000
Retained Risks	(124,000)	(47,000)
Pre-Development Costs	(331,000)	(331,000)
Net Project Value	**(1,575,000)**	**(1,554,000)**
Value for Money	**—**	**21,000 (highest)**

$ '000s in Present Value (rounded)

- **P3 availability payment model has potential to deliver marginal Value for Money for the State**
- **It is estimated that P3 requires $243M AP beginning in FY 2016. Leverages greater amount of financing; however, toll revenue does not cover APs until FY 2044.**