

FUNDAMENTALS OF PUBLIC PRIVATE PARTNERSHIPS - PPPs

- PPPs usually are either public/private joint ventures or long-term, up to 50 year, concessions.
- Governments guarantee public service delivery instead of providing it as well.
- Used for highways, mass transit, water treatment/transmission, schools, waste treatment, airports, and other sectors.
- Deal sizes range from \$50 million - \$2 billion. Smaller transactions occur based on special circumstances.
- A pre-set defined basket of money invested up-front relies only on user charges for repayment.
- 1,300 PPPs have been financed globally with only about 20 in the U.S.
- PPPs arrived late in the U.S. due to readily available tax-exempt financing that bonds taxation streams.
- Project Finance debt and equity for a PPP rely **only** on project cash flow with no outside recourse.
- Project Finance debt + equity = an **after-tax** financing cost equal to Public Sector tax-exempt financing.
- PPPs are easy to understand but documentation and paperwork is complex because the documentation determines how risks are shared between the parties with little consequent scope for ambiguity.

ADVANTAGES TO THE PUBLIC SECTOR

- Delivery of projects on time and to budget with no change orders because private companies view risk differently and, as a result, typically manage "construction chaos" better. Contractors know there is a capped basket of money available up-front with no more to fund change orders.
- Some early U.S. private power projects were completed at about 40% less than their public counterparts.
- It's easier to differentiate "*spending*" and "*investment*" because PPPs do not finance operating deficits.
- PPPs benefit from smart design and technology if output (rather than design) specifications are set.
- Governments do not have to "bank" annual budget allocations until funds are all in hand. They can build immediately what makes sense rather than what they can

afford or be forced to break projects into ultimately more expensive pieces.

- PPPs reduce real estate developer influence.
- The Private Sector must plan maintenance with a 30-50 year "*life cycle*" in mind.
- Project Financiers will not lend to PPP projects unless everything is transparent because they are at risk!
- Managing the ups and downs of construction cycles becomes a Private Sector labor/pension problem.
- Government is less involved day-to-day, so can focus on ensuring a PPP meets its contractual obligations.
- Private companies often typically understand better that users are also "customers."
- PPP users can choose to pay user charges, whereas taxes are mandatory.
- PPPs attract private equity which means less government debt and improved municipal bond ratings.

CHALLENGES, OBJECTIONS, PERCEPTIONS AND MISPERCEPTIONS

- Public "*crown jewels*" are not lost to private operators; they return at some point per the concession.
- A PPP "*bundling*" everything together simply means government has to be on its toes to avoid gouging by PPP promoters.
- Well-structured PPPs rarely default and create moral hazard because the financiers require 20% down and good old-fashioned cash flows.
- User charges for previously free services can be avoided by government paying in lieu of users.
- PPPs create local jobs. They do not export Public Sector or construction jobs out of state.
- European banks are the main Project Finance lenders to PPPs. A serious challenge exists in getting U.S. banking institutions back into this business, diversifying away from real estate, and ensuring that Arizona and U.S. contractors have a level playing field in rebuilding the nation's infrastructure.
- PPPs, however, are not a panacea because excess government debt and user charges must still compete for disposable income from taxpayers' pockets.