PUBLIC INTEREST PARAMETERS FOR PUBLIC PRIVATE PARTNERSHIPS

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Commission staff have been requested to develop a list of parameters, as initiated by Commissioner Heminger and discussed at its June meeting. Commissioner Heminger's list of "Principles" was offered in the context of long-term concession agreements with equity participation, one form of PPP's. **This white paper is a synopsis of a recent paper by Buxbaum and Ortiz for the Keston Institute for Public Finance and Infrastructure Policy, "Protecting the Public Interest: The Role of Long-Term Concession Agreements for Providing Transportation Infrastructure," offers a range of strategies are provided that could address those concerns. Illustrative requirements have been added by Commission staff and are arrayed in conjunction with the many of the options in the above paper. Please note that this paper does not address which of these public interest concerns extend to the Federal government as opposed to State and local entities as that is linked to the intergovernmental and institutional responsibilities that the Commission has yet to determine.**

Public Interest Issues Associated with Public-Private Partnerships

As described on the FHWA PPP website, over the last year or so, PPP has typically referred to these concessions, but PPP refers to any contractual agreements between the public sector and a private entity that allow for private sector participation in the delivery of transportation projects. The project sponsor should seek competing public sector bids to test the viability of traditional tax-exempt financing methods. Commissioner Heminger offered the following aspects as protecting the public interest; Commission staff note that rather than "principles," these could be characterized as strategies to address public interest concerns. As such the short list below are strategies that were offered as options for incorporation into Federal law and actions.

"Prior to U.S. DOT approval of a public-private partnership (PPP) project on the
federal aid system, the following criteria should be satisfied:

1. The project agreement should ensure the funding of major reconstruction or replacement of the new or existing asset over the life of the lease.

2. Revenue generated from the asset or its lease should be used only for eligible Title 23 (highway) or Title 49 (transit) purposes, and not diverted to non-transportation uses.

3. The project sponsor should ensure adequate public participation and review of all transactions and compliance with applicable planning and environmental requirements for projects involving new construction.

4. The project sponsor should document consideration of alternative financial arrangements in any proposed lease, i.e. long-term equity participation vs. up-front cash payments."

This synopsis of a recent paper by Buxbaum and Ortiz for the Keston Institute for Public Finance and Infrastructure Policy, "Protecting the Public Interest: The Role of Long-Term Concession Agreements for Providing Transportation Infrastructure," offers a range of strategies are provided that could address those concerns. In that paper, Buxbaum and Ortiz, identified three areas of "public concerns about long-term concession agreements, specifically related to long-term leases and DBFO contracts involving private investors who would either collect toll revenues or receive state payments to recoup their investment."

1. Aspects of public sector decision-making
    - Lack of public sector (particularly State DOTs) experience to avoid conflicts of interest in the negotiation and management of these types of contracts
    - Valuation of the facility as a critical component of the arrangement
    - Use of upfront payments and equity issues associated with the distribution of the payment
    - Perception that the Public Sector could raise as much money as the private concession but for debt limits and political constraints on setting tolls that keep pace with inflation
    - Transparency in the development, negotiation, and implementation processes
2. Conflicts of private sector interest with public sector interests
    - Business interests may not align well with the public interest as the scope of its revenue maximization goals are for the particular assets versus the system effectiveness concerns of the traveling public.
    - Unsolicited proposals and "cherry-picking" of profitable projects may set priorities for developing facilities in conflict with priorities reflected in fully consultative planning processes.
    - Public resources devoted to the review of proposals may divert resources from higher agency priorities.
3. Contract terms and how they affect price and public control
    - Tolling Policy, i.e., the authority to change rates over time.
    - Allocation of Toll Revenues, including profit sharing and windfall revenues
    - Length of leases that extend beyond the accountability of the electorate and the public officials involved
    - Extent of "noncompete" clauses or "monopoly" authority conferred on the concessionaire as a result of provisions that prevent the state and local governments from adding capacity within a specific distance from the facility or require the public sector to pay the concessionaire for "lost revenues"
    - Default or Renegotiation
    - Facility operating and maintenance requirements and environmental standards.
    - Consideration of the transportation system as a whole, i.e. creation of a fragmented system with localized concerns that do not consider interoperability of the entire highway network.

- Elimination of labor protections often required for the construction and operation of public projects
- Providing the benefits of eminent domain to a private party

The following potential strategies to address public concerns were offered as "strategies to lead elected official to the best decisions regarding development and preservation of transportation assets?" Brief statements of possible strategies are arrayed by the above concerns. In the same vein as Commissioner Heminger's listing, some options for requirements are shown that are more directive in tone, and might be adopted by a unit of government in statute or regulation to address these concerns. No comment is made as to the appropriate level of government to take these actions.

Concern	Strategy	Illustrative Requirements
Public sector inexperience	Contract for expertise where in-house in unavailable but be cognizant of conflicts of interest	
	Build in-house competencies	
	Develop comparators	
	Create independent commission to advise	
Undervaluation of assets	Estimate the value under government ownership, and set a confidential, minimum value	
	Encourage participation of public toll authorities to submit competitive proposals	
	Account for and publicly disclose supplementary resources	
Uses of Upfront Payments and Equity	Allocate funding to projects that benefit the users	The project sponsor should document consideration of alternative financial arrangements in any proposed lease, i.e. long-term equity participation vs. up-front cash payments.
	Set up an annuity for projects over the life of the lease.	The project agreement should ensure the funding of major reconstruction or replacement of the new or existing asset over the life of the lease.

Public sector capability	Evaluate revenue potential including nonfinancial measures	
Transparency	Public participation and outreach, sharing information as to the criteria and the participants	The project sponsor should ensure public participation and review of all transactions and compliance with applicable planning and environmental requirements for projects involving new construction.
	All equity holders in the transaction should be publicly disclosed.	The agreement should ensure that the private party procures services in a fair and transparent procurement process and that the private party is prohibited from engaging in any form of discrimination.
Concern	**Strategy**	**Illustrative Requirements**
Revenue Maximization vs. System Effectiveness	Revenue sharing, to address any off-highway impacts.	The agreement should ensure that the public agency has the right to assume appropriate control over the operation of the facility during emergencies.
	Use of availability payments to motivate the concessionaire to maximize traffic use of the road.	The agreement should ensure that the facility's technology continues to comply with regional architecture and is interoperable with other regional/national systems (communication equipment, electronic toll collection equipment, etc).
	Requirements to provide free service for transit vehicles and emergency vehicles.	
Unsolicited proposals and "cherry-picking" of profitable projects	PPP legislation designed to regulate or even prohibit unsolicited proposals.	The project proposal, even if unsolicited, should be subject to a fair and open competition process that ensures the public that it is getting the best bid.

	Incorporate competition into the public processes, solicited or unsolicited.	
Public resources divert resources from higher agency priorities	Require unsolicited proposals and counter-proposals to be accompanied by application fees to offset the cost of reviewing the proposals by the public sector.	
Concern	**Strategy**	**Illustrative Requirements**
Tolling Policy, i.e., the authority to change rates over time.	Public sector establishes frequency of toll rate adjustments with formulas in the contract. Consider congestion pricing if that is the objective of the project.	The agreement should include a toll rate structure that protects the public from excessive increases in tolls.
	Include toll policy within enabling PPP legislation with opportunity for public input.	
Allocation of Toll Revenues, profit sharing and windfall revenues	Include revenue sharing provisions within the contract.	Revenue generated from the asset or its lease should be used only for eligible Title 23 (highway) or Title 49 (transit) purposes, and not diverted to non-transportation uses.
	Conduct a careful selection of growth indices; assure that various income groups are not disproportionately affected.	The agreement should include a revenue sharing provision in which the public agency receives a share of the profits if the profits exceed a certain threshold.
	Provide for a “shadow toll” and/or nonstandard rates for certain users.	

	Refinancing can be regulated as part of the lease contract with provision for revenue sharing of gains from the refinancing transaction.	
	If a TIFIA loan is used in a long-term concession agreement, the TIFIA program allows the TIFIA debt to be refinanced as long as the proceeds are used to complete, expand, or upgrade the project.	
	Include rebalancing provisions in the contract to bring the contract terms back into financial balance based on changes in the underlying economic conditions.	
Concern	**Strategy**	**Illustrative Requirements**
Length of leases	Maximum length of lease/concession agreements can be established through State legislation.	The agreement should include appropriate provisions ensuring that the facility is returned to the public agency at the end of the lease term in good condition.
	Alternatively, a clause in the agreement can end the lease when the private investor has reached a specified rate of return.	The agreement should structure the length of the lease term so that it is renewable at certain set intervals and milestones, such as when a certain rate of return is realized by the private party.
	Public outreach to explain lease period rationale.	
"Noncompete" clauses	Lease agreement can include provisions that allow planned construction; could exclude other "modes" from noncompete clauses such as arterial improvements, public transportation, Interstate	The agreement should not include any non-compete agreements in which the public agency agrees not to improve the infrastructure on competing facilities.

	expansion or safety purposes.	
		The agreement should include appropriate termination provisions ensuring that fair, but not excessive, compensation is paid to the private party.
Default or Renegotiation	Specify that the facility reverts to the public sector at no cost in the case of default or bankruptcy.	The performance measure could include liquidated damages provision upon failure to meet the performance measure either in terms of payment to the public agency or reimbursement of tolls to users.
	Ensure that if default occurs, operations will not be interrupted (tied up in bankruptcy proceedings) and that financial liability will not be transferred to the public sector.	The agreement should ensure that the public agency reserves a right of reentry to assume operations and undertake necessary repairs if private party is neglecting responsibilities. Agreement should include assign appropriate liability in the form of damages on the part of the private party for these situations.
	The lease should specify the level of compensation to the private investors If terminated for “convenience.”	
Concern	**Strategy**	**Illustrative Requirements**
Facility Operating and Maintenance Requirements and Environmental Standards	Include in clauses in concession agreement that specify any major capital investments (construction or reconstruction) to be performed over the length of the lease, such as future widening, extensions.	The agreement should include appropriate facility performance measures on certain key operating elements, such as: pavement condition, maintenance, safety, level of service/congestion, capacity, snow/ice removal, environmental mitigation, emission levels, etc.

	Agreement may include penalties for not meeting standards based on periodic inspections by an independent party. Public sector should conduct an assessment of the current state of the asset prior to lease.	
Labor protections	Explicitly address the performance with respect to employment and benefits; address transfer of public employees.	The agreement should ensure that that laborers working on facility are paid prevailing minimum wage.
	Long-term concession projects receiving state or Federal funds subject to state or Federal labor regulations.	
Providing the benefits of eminent domain to a private party	Private investors may choose to acquire land through negotiation.	The agreement should ensure that the facility remains dedicated and open to public use.
	Eminent domain authority is not transferred to the private sector; it remains in public sector hands.	The agreement should ensure there are clear land acquisition policies inserted and make clear that eminent domain power not transferred to private party.