

Monetizing Public Assets: Government's Next Frontier



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Columbia Capital is an independent financial and investment advisor serving municipal bond issuers. The firm is registered as a "municipal advisor" with the US Securities and Exchange Commission.

Monetization? Huh?

- The premise of today's conversation:
 - You're struggling to balance the budget. You've squeezed the proverbial turnip. You've held citizen budget sessions. You've done strategic cuts. You've done across-the-board cuts. You've done RIFs or right-sizing or whatever the latest euphemism is for "layoffs." You've even—heaven forbid—cut the fire department budget. You've recommended mill levy increases. You've tripled pet licensing fees. We're not going to talk about this stuff.
 - What we are going to talk about is turning public assets into immediate cash and/or long-term revenue streams (that is, "monetizing" them), as well as using risk-transfer to third parties to produce on-going cost savings.

Disclaimer

- **No Advocacy Intended**
 - Some of the approaches I'll talk about make a lot of sense. Some are more than a bit desperate. Some might make sense if they were implemented just right (which is often impossible legally, politically or financially).
- **No Legal Advice Provided**
 - Some of these approaches may not be achievable under Kansas law
- **Your Mileage May Vary**

P3—The New Sliced Bread

- P3
 - “Public-Private Partnerships”
 - An broad term covering a wide gamut of activities undertaken by public agencies to shift risk, and thereby cost, to third-parties (typically for-profit businesses)
- What’s Old is New Again
 - I started in the city government business in 1990 and “privatization” was the hot trend and a constant topic at ICMA conferences, NLC, GFOA, etc.

Global Trends, Local Uses

- P3s Have Been Used Around the Globe
 - US tax-exempt bond market is unique
 - Social democracies, especially in Europe, have increasingly looked for private sector alternatives to government-owned infrastructure and facilities
 - These moves have been driven by
 - Politics (conservative governments with free-market philosophies)
 - Budgets (crowding-out of infrastructure spending by other government-financed programs)
 - Availability of Capital (borrowing at the sub-sovereign and even sovereign levels is constrained)

P3 Experience, cont'd.

- P3 Undertakings
 - UK: hospitals, schools, rail, transportation
 - Australia: transit, technology, health, water
 - Ireland: transportation, rail management, water supply, waste management, education
 - Canada: sports complexes, transportation, health, courts
- 1,400 deals in the EU over the last 20 years

A European Definition of P3

- **Definitional characteristics**

- The relatively **long duration of the relationship**, involving cooperation between the public partner and the private partner on different aspects of a planned project.
- The method of funding the project, in part from the private sector, sometimes by means of **complex arrangements between the various players**. Nonetheless, public funds—in some cases rather substantial—may be added to the private funds.
- The important role of the economic operator, who participates at different stages in the project (design, completion, implementation, funding). The **public partner concentrates primarily on defining the objectives to be attained** in terms of public interest, quality of services provided and pricing policy, and it takes responsibility for monitoring compliance with these objectives.
- The **distribution of risks** between the public partner and the private partner, to whom the risks generally borne by the public sector are transferred. The precise distribution of risk is determined case by case.

Benefits of P3

- **British Columbia Provincial Government Report**
 - **Improve service delivery** by allowing both sectors to do what they do best. Government's core business is to set policy and serve the public. The private sector takes responsibility for non-core functions.
 - **Improve cost-effectiveness** by taking advantage of private sector innovation, experience and flexibility.
 - **Increase investment in public infrastructure.** P3s can reduce government's capital costs, helping to bridge the gap between the need for infrastructure and the Province's financial capacity.
 - **Reduce public sector risk** by transferring to the private partner those risks that can be better managed by the private partner.
 - **Deliver capital projects faster**, making use of the private partner's increased flexibility and access to resources.
 - **Improve budget certainty.** Reduce the potential for government cost overruns during project development or service delivery.
 - **Make better use of assets.** Private sector partners are motivated to use facilities fully, and to make the most of commercial opportunities to maximize returns on their investments.

P3 Policy Guidelines

- **BC Government P3 Report**
 - **The Public Interest is Paramount.** All P3s protect and enhance the public interest by addressing such factors as public health, safety, environmental protection, accessibility, equity, privacy, security and reliability.
 - **Processes are Fair and Open.** This allows taxpayers to see for themselves where P3 solutions deliver tangible benefits.
 - **The Focus is on Results.** P3 proposals are judged on the basis of what they deliver (in terms of assets, services, cost-effectiveness, innovation, etc.), rather than how assets or services are delivered. Public sector agencies only choose a P3 where it is the best option available.
 - **The Public Agency is Accountable.** P3s are only developed where they are supported by a thorough and rigorous business case analysis. In other words, the partnership has to offer clear and tangible benefits to both the public and private sectors.

When P3s Make Sense

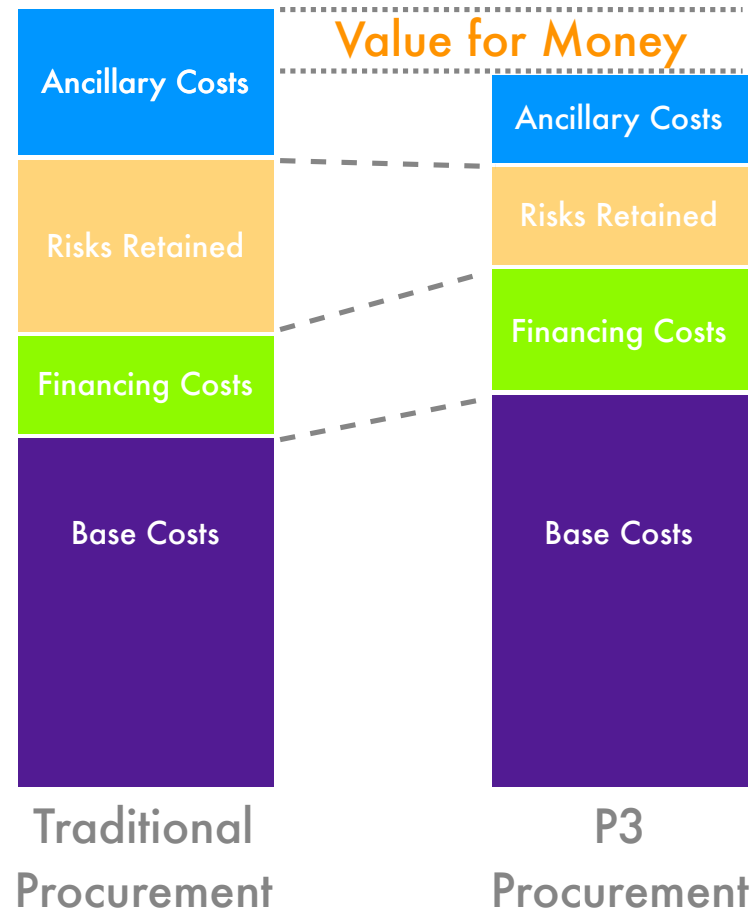
- **BC Government P3 Report**

- There is a **significant opportunity for private sector innovation** in design, construction, service delivery, or use of an asset
- **Clearly definable and measurable output specifications** can be established suitable for payment on a services delivered basis
- An opportunity exists for the private sector partner to generate **non-government streams of revenue, to help offset public sector costs**
- Some **risks can be transferred** to the private sector
- **Projects of a similar nature** have been successfully developed using a similar method, and
- The **private sector has sufficient P3 capacity** (expertise and availability) to successfully deliver project objectives.

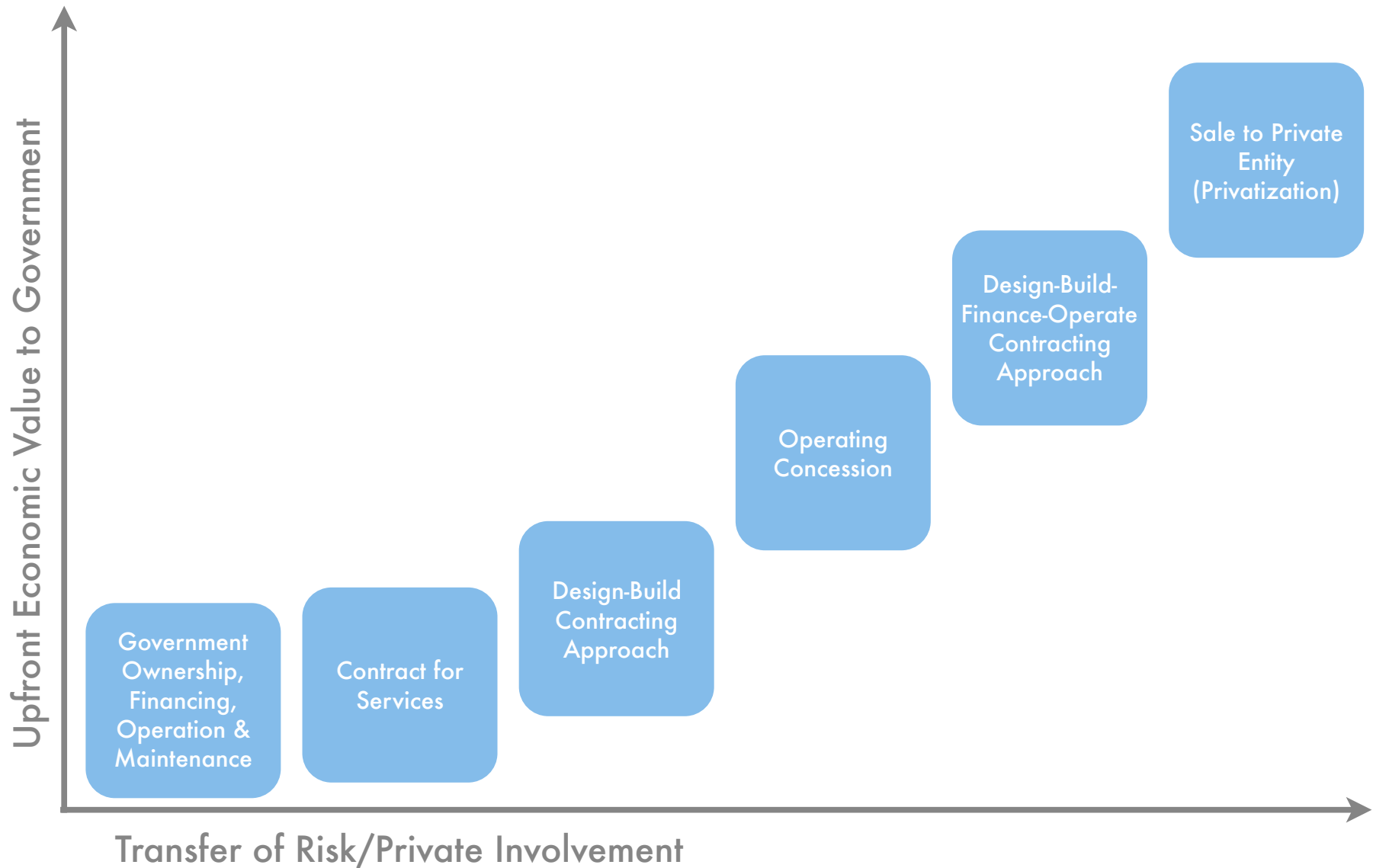
Measuring P3 Benefit

- “Value for Money” Concept
 - Value for Money (VfM) is the term used to assess whether or not an organization has obtained the maximum benefit from the goods and services it acquires and/or provides, within the resources available to it. It not only measures the cost of goods and services, but also takes account of the mix of quality, cost, resource use, fitness for purpose, timeliness and convenience to judge whether or not, when taken together, they constitute good value. Achieving VfM may be described in terms of the 'three Es' - economy, efficiency and effectiveness.
- VfM=getting a good deal
 - Much harder to measure than low bid

P3 Benefit Framework



P3 Continuum



Keys to Quality P3s

- **Statutory and political environment**
 - Authority to undertake the arrangement
- **Organized structure**
 - Public partner has internal capacity to lead the process
- **Detailed business plan**
 - Having a well-defined expectation of the outcome
- **Guaranteed revenue stream**
 - P3s generally won't work without guaranteed cashflow
- **Stakeholder support**
 - Governing bodies, labor organizations, etc.
- **Carefully chosen partner**
 - There is no "no-fault" divorce in P3

P3 Challenges

- **Information/Expertise Asymmetry**
 - Private P3 partners tend to be large, experienced multinational companies
 - Public agencies have limited expertise and resources to negotiate and complete the deal
- **Implications for Tax-Exempt Financing**
 - Maintenance of tax-exempt financing limits private use and repayment
 - “Qualified Management Contracts” may be too constraining for an effective P3
- **Limited Pricing Transparency**
 - A series of “one-off” transactions limits ability to benchmark pricing with previous transactions

P3 Challenges, cont'd.

- **Public Purchasing Regulations**
 - Traditional public sector purchasing regulations struggle to accommodate even relatively simple design-build structures
 - Purchasing codes may have to be ignored or reworked to permit more complex P3s; shift to life-cycle costing
- **Legal Authority**
 - In many cases, state legislation will be necessary to remove roadblocks or to allow P3 projects
- **Protecting Cash**
 - Making illiquid assets liquid exponentially increases the likelihood those assets won't benefit future generations
 - Chicago experience as case study

Local P3 Examples

- **Topeka “Optimization” Program**
 - Mock privatization bid provided motivation for policy makers, unions and management to enact significant cost-saving reforms
 - Life-cycle costing perspective to capital investment
- **Family Court Project**
 - Private group helped public agency define needs, selected site, aggregated land, selected design/build team, and will establish GMP, construct facility and potentially, manage it for the government
- **KTA Lawrence Service Island**
 - Private concession led to private investment

Major US P3s

- Chicago Parking Meters
- Indiana Toll Road
- Chicago Skyway



Chicago Parking Meters

- Concession to operate and maintain 36,000 metered parking stalls for 75 years
- \$1.2 billion payment to City of Chicago at closing
 - \$400 million to revenue replacement fund, interest earnings (pro forma \$20MM per year) transferred to General Fund
 - \$325 million used to help balance General Fund budgets 2009-2012
 - \$324 million to “stabilization” fund to be used at the discretion of the city council
 - March 2010 projection: only \$180MM left by end of 2010
- Many parking rates will increase 700% by 2013
- Study estimates City received only about 20% of the true value of the contract

Chicago Parking, cont'd.



Feed the Meter for Morgan Stanley

In 2008, Chicago struck a deal: The city pledged the revenue from its parking meters for the next 75 years in return for a lump-sum payment from an investment group that includes Morgan Stanley. **DARRELL PRESTON**

Amount Chicago got for leasing its 36,000 parking meters:

\$1.15 billion

Amount Chicago drivers are forecast to pay into those meters:

\$11.6 billion*

Year in which Chicago likely will spend the last of its proceeds:

2011

Year in which parking meter revenue reverts to the city:

2084

*According to papers filed this year for a planned sale of notes by the investment group.

Lessons Learned

- Incremental approaches provide incremental, not transformational, economic value
- Sales of assets or long-term concessions can be transformational, but
 - Extremely difficult to value the opportunity cost of a 75+ year stream of revenue
 - Much of the value of the concession comes from private operator rate increases (pricing model)
 - Pricing model can lead to public discontent
 - Governments have a hard time seeing large pools of money sitting around and not spending them in times of budget distress

Outlook

- Likely to see more P3s in transportation arena
 - Federal transportation agencies are amenable
 - Tolls provide long-term dedicated sources of revenues
 - Airports may be the next frontier
- Global credit crisis has significantly reduced the purchase price for long-term concessions
 - Private debt is expensive and hard to get
 - Ability for concessionaires to syndicate risk is diminished
- Persistence of recession will force P3s to be “on the table” for budget negotiation

Starting Your P3 Adventure

- Assess areas with established private sector service presence and capacity to perform
 - Water & wastewater, power, transportation, aviation
- Identify targets with recurring revenue streams
- Clearly identify your intended outcomes
 - Does it really make sense to give up 100 years of revenue?
- Recruit some help
 - Financial advisor, lawyers, consultants
- Consider “public monetization”
 - Can you adjust the pricing model to achieve your goals?
- Find a partner and document the deal

Questions & Comments

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 - Presentation Download
 - www.columbiacapital.com/images/ksgfoa2010.pdf