Virginia’s Public-Private Partnership Approach

Barbara W. Reese, Summer/Fall 2006
• Commonwealth responsible for maintaining the third largest highway system in country – more than 70,000 miles

• Last sustainable state revenue increase for transportation in 1986 – transportation user fee based
  – Gas tax is 17.5 cents per gallon
  – Increasing reliance on bonds and federal funding for any new capacity in mid-1990s
  – Federal highway funds now largest source
The Context, continued

• In 2004, a multimodal examination of capacity needs found a $108 billion gap between funding and needs in the next 20 years

• Since 2004, there has been incremental support of additional one-time funding for transportation along with changes to project delivery
  – Transportation Partnership Opportunity Fund
  – Incentives for takeover of local roads by localities
  – General Funds to offset impact of debt service
History of PPPs

• Late 1980’s, private franchise legislation governed like a utility – Dulles Greenway

• 1995 – Public Private Transportation Act (PPTA)
  – Unsolicited and solicited procurements with finding of more timely or less costly
  – Proposals focused on using traditional financing to deliver new construction – limited private sector financial risk
  – 2005 revisions to address lessons learned
- Identify timelines and activities within each phase of procurement

- Require greater commitments or guarantees by proposers – mandatory risk sharing

- Increase flexibility in the development of interim agreements to accelerate required activities

- Promote transparency and public involvement
• 53 unsolicited proposals – 11 agreements worth $8.7 billion

• Solicited proposals for two projects:
  – Reconstruction of I-81 (in negotiation and tiered NEPA process)
  – Route 460 from Hampton Roads to I-295 in Richmond region (proposals due in September 2006)

• 8 proposals currently active – construction value of more than $11 billion
  – All new toll facilities
Program Has Changed Dramatically

• Generally, between 1995 and 2002, signed agreements were fundamentally sole source contracts using traditional public funds/debt – no financial risk or investment by private sector.

• Federal funding was not used to finance them.

• By virtue of the agreement, these projects became the funding priority for the Commonwealth.
2002 to Today

- Return/not accept unsolicited proposals which didn’t include private risk
- Put controls around “lobbying”
- Require ability to use federal funding
- Require project proposals to be a clear transportation priority of the Commonwealth
- Once decision made to develop project using PPP, became partners
Initial Concession Steps

- Worked with legislators and industry to:
  - provide policy direction for use of any lease payment (stay in corridor; transportation purpose)
  - defined transportation facility under long-term lease with concession operator as property indirectly owned by the Commonwealth which provided tax benefits
  - significant toll violation and enforcement legislation with “teeth”
Pocahontas Parkway

• First construction PPTA in Virginia
  – Originally financed using tax-exempt bonds (IRS Rule 63-20) - $346 million
  – Traffic and revenue projections did not materialize
  – Bonds downgraded; VDOT had loaned $

• Amended and re-assigned PPTA agreement to Transurban (T895) as a 99-year concession in June 2006 – paid off all outstanding debt/loans

• Approach to risk was “who is in best position to manage?”
<table>
<thead>
<tr>
<th>Risk</th>
<th>assumed by VDOT</th>
<th>assumed by T895</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financing</td>
<td>None</td>
<td>Yes</td>
</tr>
<tr>
<td>Traffic and Revenue</td>
<td>None</td>
<td>Yes</td>
</tr>
<tr>
<td>O&amp;M and Major Maintenance</td>
<td>Oversight</td>
<td>Yes</td>
</tr>
<tr>
<td>Change in Law (discriminatory)</td>
<td>Yes</td>
<td></td>
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<tr>
<td>Operating Standards</td>
<td>Oversight</td>
<td>Yes</td>
</tr>
<tr>
<td>Toll Rate Setting</td>
<td></td>
<td>Based on a toll escalation formula</td>
</tr>
<tr>
<td>Environmental</td>
<td>Shared</td>
<td>Shared</td>
</tr>
<tr>
<td>Construction of the Richmond Airport Connector</td>
<td>Oversight &amp; Excess of cap</td>
<td>Yes – if TIFIA loan</td>
</tr>
<tr>
<td>Force Majeure</td>
<td>Shared for uninsurable events (bridge)</td>
<td>Shared</td>
</tr>
<tr>
<td>Revenue over an agreed return on total investment</td>
<td>Shared</td>
<td>Shared</td>
</tr>
</tbody>
</table>
• Revenue Sharing – based on a series of calculations tied to real net cash flow and internal rate of return

• Termination - VDOT has the right to terminate for convenience after 40 years – at a cost

  – Forty years was the estimated time it would have taken the prior operator to pay off all liabilities
PPP Lessons Learned

• PPP is not appropriate for every project – Commonwealth estimates that 20% of need can be addressed thru P3s

• Engineering is easy part – financing and operations critical pieces

• Need private partner who has some risk for “after its built”; need healthy public partner

• Make solid decisions each time – they do come back
• Development of expertise takes time – have good lawyers and financial advisors – excellent traffic modeling

• Conflicts of interest and political interference

• Significant time commitments by both public and private partners – senior staff

• Set and manage realistic expectations among all parties
If We Were at Beginning?

- Learn from others
- It is a business decision not a political decision
- Solicit proposals – be in control
- Embrace prospect and allow failure
- Set clear policy goals and remember big picture
- Recognize that the agreements in each one will become precedent for next
• With concessions, we are returning to where we started – private operators of transportation infrastructure used by public

• Focusing on expanded capacity rather than greenfield development – systems operations critical

• Traditional methods and funding cannot meet our transportation needs
  – PPPs can’t save us but they can help us
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