Private Sector Perspective on DBO and BOT – ("PPP’s")

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With Input From
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Executive Summary

- Great Results with EUL
  - Deal Flow is still “Anecdotal”
  - Cost of Participation is High

- Attracting Private Sector Interest in PPP’s
  - Proper Positioning of Opportunities by Federal Owners
  - Solves Numerous Problems on Both Sides
  - If Projects are Strongly Positioned, Financing follows easily

- Procurement Must Be Dramatically Simplified
  - To Give More Authority to Buying Entities
  - To Lower Transaction Costs
  - To Increase Early Transparency
    - Allow Competitors to Match Capabilities/Teams to Projects
  - Key Variables to Private Sector
    - Expected Cash Flow
    - Suitability of Chosen Project Delivery Method

- 2007 ABA Model Code for Public Infrastructure Procurement
Conditioned Power Project

- US Army - Interagency Services Agreement for multiple federal entities to buy power through Army
- 50 Year E U Lease
- 10 Year “GSA FAR type” Purchase Back of Energy by Army
- Unused Capacity Can Be Sold to Grid
- Special Purpose Entity to Receive Non-Recourse Financing
  - $120+ Million financing through capital markets
  - “Essentiality” of the Function Allowed financing
- Chevron won the procurement competition
  - Contractor and operator
- Second Phase (in Future) will likely add cogeneration capacity
Argonne National Labs

- Research and Development Facility
  - DOE is Ground Lessor
  - Special Purpose Entity is Lessee
    - Obtains Financing from the Capital Markets
      - Illinois Finance Authority issues taxable, revenue bonds
      - Essentiality of the facility and the function critical to financing in capital markets
  - Contracts for Development and Management accomplished on competitive basis
  - Leases space in to-be-developed Facility to M&O Contractor
    - M&O Contractor rent is a reimbursable from DOE under DOE M&O Contract
  - “EUL Like” transaction Under Separate Legislative Authority for DOE
Jesse Brown VA Medical Center

- Cogeneration Facility through EUL
  - 200+ bed acute care center, with 4 outpatient clinics
  - 3.4 Megawatt Cogeneration Plant in Chicago
    - Replaces Steam purchased from U of Illinois and Electricity purchased from Com Ed
- Special purpose trust raised financing for the $13 million project through capital markets
- Unused warehouse space leased by VA to energy contractor
  - Energy Contractor builds, maintains and operates the plant
  - Trust bills VA for steam and electricity
  - Trust pays principal and interest on its loans, and pays the contractor for O&M services
  - Trust pays into contingency reserve fund to cover major repairs and enhancements
- $31 million in savings over first ten years. VA Option to extend or reposition after 10 years.
Common Public and Private Sector Interests

- Best Practices in Facility Management Apply
- Projects That Make Sense
  - Function
    - Durable or Essential Needs
  - Program – Clear Scope of Work
    - Design – Construction – Ops & Maint
    - Approvals in Place or Readily Obtained
  - From Cost Perspective
    - Initial Cost
    - Long Term Operations, Maintenance, & Repair
    - Replacement/Rehabilitation/Decommissioning
- Revenues that Match
  - Lease Payments; 3rd Party Revenue Opportunities
An Example of How Private Sector Teams Think about PPP Opportunities from Transportation Sector

Dulles Greenway

Round 1
Private Sector Discipline Helps Address Life Cycle Cost Issues!

Will Revenues Be Sufficient to Pay Expenses and Return on Equity?

Dulles Financial Structure

- Gross toll Revenue
- Annual Costs
- Lease Paid To WMAA
- Debt on Financing
- Debt Long Term Finance
- Repay Lines of Credit
- Repay Equity

Order in Which Gross Revenue Areas Allocated

Will Revenues Be Sufficient to Pay Expenses and Return on Equity?
Configuring Projects That Are Mutually Attractive to the Public and Private Sectors

Clear Statement of

Expected Cash Flow
Expected Delivery Processes and Scope
The Quadrant Framework

IV Direct

Segmented

Indirect

Combined

Project Delivery Method

Source of Project Finance
Delivery Methods Fit the Quadrants

IV
- O&M Operate-Maintain
- PP Parallel Prime
- TKY Turnkey
- DBB Design-Bid-Build
- CM Constr. Mangmt.
- FT Fast Track

Direct
- DBOM Design-Build-Operate-Maintain
- “Super”-TKY Turnkey with Finance
- DBO Design-Build-Operate
- EUL Enhanced Use Leasing
- BOT Build-Operate-Transfer
- DBFOM Design-Build-Finance-Operate-Maintain

Segmented

Combined

III
- Indirect

Life Cycle Costs Included
Quads I/II
Quadrant IV Offers:
“Isolated Technology” Engine;
A Place to Diffuse Technology
From Quadrants I & II
Flexibility to Stop
At Design Completion

Quadrant I Offers:
“Efficient Technology” Engine;
Combined Delivery with Owner’s
Money
Associated Capital Investment
Different Players
Incrementally Better Solutions
Sustainable Opportunities
20-40% Savings in Life Cycle $$

Quadrant III Offers:
Few Advantages (Command + Control)
Averse to New Technology
and To New Capital
Example of Failure of This Strategy
US Superfund Contracting Program
Described in App. C, Principles Text

Quadrant II Offers:
“New Technology” Engine;
Combined Delivery with
Private Sector’s Money
New Capital Investment
New Players
Different Solutions New Services
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30-40% Savings in Life Cycle $$

Quadrant III Offers:
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Combined Delivery with
Private Sector’s Money
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Quadrant I Offers:
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The Quadrants Have Remarkably Different Cash Flows
Design Bid Build and Design Build

Very Little Opportunity to Play with Overall Cash Flow

Life Cycle Costs are Not Considered
Design Bid Build = Cash Flow A + Uncertainty

Design Build = Cash Flow B + Uncertainty
Design Build Operate (Maintain)

- or Enhanced Used Leasing

- Flexible Tool to Manage Overall Cash Flow Across an Infrastructure Network
- The “Weapon of Choice” for Long Term Stability:
  - Managing Rates, Fees, and Tolls
  - Preventing Rate Shock
  - Funding Capital Improvements Now through Future Lease Payments
- Getting Out of the Annual Appropriation Business (and Fights about Deferred O&M&R)
- An Efficiency Engine If Used Competitively
Design Build Operate = Cash Flow C + Budget Predictability

Design Build Operate = Cash Flow D (Budget Stability)
Design Build Operate = Cash Flow E (Moderate Stability)

Design Build Operate = Cash Flow F (Tailored Stability)
Design Build Finance Operate

- The “High Risk High Reward” Scenario for Private Sector
  - Drivers for this Method
    - New Technology
    - New Methods – design, construction, operations
    - High Early Investment – with uncertain early revenue
    - Conservation of Scarce Public Funds -- If financed on the Public side, High Risk High Reward Projects Can Consume All the Public Sector’s Available Capital
  - DBFO is Primarily a Technology Engine – Overcomes Public Sector Reluctance to Experiment with New Technology by Placing Risk/Reward Squarely on the Private Sector
  - DBFO is a Technology Spreader – Once proven, new methods and technologies are available to be used in DBB, DB, and DBO
Design-Build-Finance-Operate

- A Unique Animal
- NO DIRECT PUBLIC CASH (as defined in the ABA 2000 MPC) after contract award
- Design Build Finance Operate = Cash Flow G (Revenue and Expense Balanced, but at Contractor’s Risk)
The Irony of US Infrastructure

Available Capital:
- Appropriations
- Private Sector Capital; Debt/Equity; Public Sector Debt
- Investment Funds

Processes that Connect the Two

Infrastructure Needs:
- Maintenance and Repair;
- Rehabilitation; Operations; Replacement, New Facilities
US Infrastructure Procurement – The Past and A Prediction for the Future

Enhanced Use
Leasing Included

DBB
CM
DBOM
DBFOM

Segmented
Combined

Direct
Indirect

BOO
Building a Coalition to Widen These Processes

Goal is to establish durable procurement mechanisms that allow proven project delivery and finance methods to be used simultaneously at federal, state, and local levels.
The 2007 ABA Model Code for Public Infrastructure Procurement

- We believe the 2007 Model Code Provides a Base to Meet Mutual Interests of the Private and Public Sector in Moving Infrastructure Project Forward
  - Transparent processes
  - Competitive processes
  - Reductions in Transaction Costs
  - Promotes:
    - Good Planning
    - Fair Treatment of Potential and Actual Competitors
- Consistent with Current Procurement Policies for Acquisition
The Model Provides Authority to Use Five Project Delivery and Finance Methods Simultaneously

- Design-Bid-Build
  - No Change from 1979 Statute
  - Straight Brooks Act + Fixed Price Construction
- Pure Maintenance & Operations
  - IFB Process
  - Lump Sum Fixed Price
- Design Build, Design Build Operate (EUL), and Design Build Finance Operate
  - Uses Competitive Proposal Process (Art. 3) With Several Adjustments
  - Two Hard Competition Points
    - Design Requirements
      - RFP Release After Owner Establishes Requirements
      - Stated Evaluation Factors, Including Weights (if any) on Factors and Subfactors
    - Proposal Development Documents
      - Response to RFP Submitted When Design is Sufficiently Complete to Establish Price (typically 30% +/- Design)
    - Independent Peer Reviewer (Design Peer Review Function)
The ABA 2007 Model Code for Public Infrastructure Procurement

1. Pure O&M  →  Contract O&M

2. DBB (1)  →  Design → Construction → Self Operate

3. DBB (2)  →  Design → Construction → Contract O&M

4. DB (1)  →  Design-Build  →  Self Operate

5. DB (2)  →  Design-Build  →  Contract O&M

6. DBO  →  Design-Build-Operate

7. DBFO  →  Design-Build-Finance-Operate

Functional Description in RFP

Competition Design Development
Questions?

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Education


Background

Fellow, American College of Construction Lawyers
Section of Public Contract Law
  Chair from 1994-95
  Reporter for ABA 2007 Model Code for Public Infrastructure Procurement
  Founding Member of Construction Practice
MIT
  NSF CAREERS Grant – 1997 to 2001 to develop procurement models integrating DB, DBO and DBFO into US project delivery methods