Statewide Transportation Needs Assessment Revenue Report –Public-Private Partnerships

Innovative Finance: Public Private Partnerships (P3s)

Introduction

Public agencies throughout the nation are currently analyzing and seeking alternative options for meeting transportation investment needs, including public-private-partnerships (P3s). P3s are contractual agreements formed between a public agency and a private sector entity that allow for greater private sector participation in the delivery and financing of transportation projects. There are many different types of P3 models and degrees to which the private sector assumes responsibility. Additionally, different types of P3s may be more applicable for development of new facilities while others may be more suitable for the operation or expansion of existing assets. For the purpose of this report, the discussion will focus on P3s involving private partners to finance, construct, operate and maintain new highway capacity as well as recent utilization of availability payment models.

Under a concession delivery model, a public agency would award a long-term contract to a private firm or consortium of firms to design, build, finance, operate and maintain a revenue generating project (e.g., a tolled road) for a specific term. The benefits of the concession model include full life-cycle costing which transfers operations and maintenance cost risks to the private sector and creates incentives for the private sector to make tradeoffs between higher upfront capital costs and lower long-term operations and maintenance costs. Adding the financing element to this model means that in the best case, the public agency would not be financially liable for the project and it would be up to the private sector to raise the necessary funds, manage the construction and assume the traffic and revenue risk on the project.

Under an "availability payment" P3 project structure, the public agency would contract with a private sector partner to design, construct, operate, and/or maintain a highway for a contracted period of time. Availability payments are often used for highway projects that are not expected to generate adequate revenues to pay for their own construction and operation, either because the highway is not tolled, or the tolls are not forecast to generate sufficient income. This requires that the public agency have sufficient and credible non-toll sources of funding to make all required availability payments. Under availability payment structures, the public agency generally retains the revenue risk rather than the private partner.

Availability payments may be structured in a variety of ways. In certain cases, no payments may be made until after construction is complete. Alternatively payments may be predicated on particular construction milestones. Project sponsors may also define how the periodic payments are to be made, and may also set a maximum payment cap based on agreed-to operating and maintenance performance standards.

Availability payments have been used extensively in Canada, Europe, and Australia, but are just beginning to gain interest in the U.S. The Presidio Parkway P3 project in San Francisco is using an availability payment structure, incorporating construction milestones and ongoing availability payments.

It is the first transportation P3 in California under the recently enacted P3 statute, Streets and Highways Code section 143.

Yield Potential

Ultimately, revenue to pay for a P3 project will need to be generated from the public (e.g., tolls, taxes, or other user-fees). Private entities contribute resources with the expectation of being repaid with a market-appropriate profit. When P3s are successful, the private partner is able to make a profit while also generating benefits for the public sector that may not have been achievable otherwise. P3s have been of considerable interest to transportation agencies in recent years as they offer an opportunity to accelerate the delivery of much needed projects—raising the upfront capital necessary for construction.

Use/Restrictions

Although construction and long term preservation can cost less under a P3 model, transaction costs are usually much higher due to legal fees, financing costs, and procurement expenses. Generally, the higher transaction costs of P3s mean that the use of P3s is limited to mostly a small segment of transportation projects—typically large and complex projects with stable revenue streams.

Conclusion

P3s allow public agencies to leverage future revenue streams for up-front capital in the form of private investment. With such access to financial resources, P3s can accelerate project delivery. These arrangements, however, do not eliminate the need for additional transportation revenue.

Reference Materials

- FHWA Office of Innovative Program Delivery
  http://www.fhwa.dot.gov/ipd/p3/index.htm
  http://www.fhwa.dot.gov/ipd/forum/