

Toyo University Delegation 2010 PPP Briefing

Financing of PPPs in the U.S.

February 8, 2010

Agenda

- ❑ US Infrastructure Landscape
- ❑ Public Sector Financing Tools
- ❑ PPP Basics
- ❑ PPP – Typical Structure
- ❑ Private Sector Financing Tools
- ❑ Financing Considerations
- ❑ Lender Considerations
- ❑ Case Study – Capital Beltway HOT Lanes Project
- ❑ Key Industry Participants
- ❑ Closing Remarks

US Infrastructure Landscape

❑ Ever-increasing investment requirements

- ❖ Aging infrastructure unable to cope with the growing demand
- ❖ Annual transportation outlays have exceeded revenues since 2005
- ❖ Annual investment needs estimated at \$225 billion – current spending reflects only about 40% of that requirement

❑ Public sector entities are facing difficult fiscal conditions

- ❖ Resistance to tax increase
- ❖ Rising costs to maintain and operate existing infrastructure
- ❖ Current spending level unable to address increased traffic volume and congestion
- ❖ Sub-due response for the “User Pay” model

❑ Growing recognition and political support for innovative/alternative project delivery methods

- ❖ Innovative finance solutions
- ❖ Public-Private Partnerships (PPPs) / Concession

Public Sector Financing Tools

❑ Funding Sources:

❖ Taxes

- Sales Tax
- Gas Tax
- Property Tax
- Special Taxes

❖ User Fees

- Toll / Highway Revenues
- Passenger Facility Charges
- Farebox Revenues
- License Fees

❖ Grants and Loans

- Highway Trust Fund
- State Infrastructure Banks

❑ Financing Tools:

❖ General Obligation Bonds

❖ Revenue Bonds

❖ GARVEE Bonds

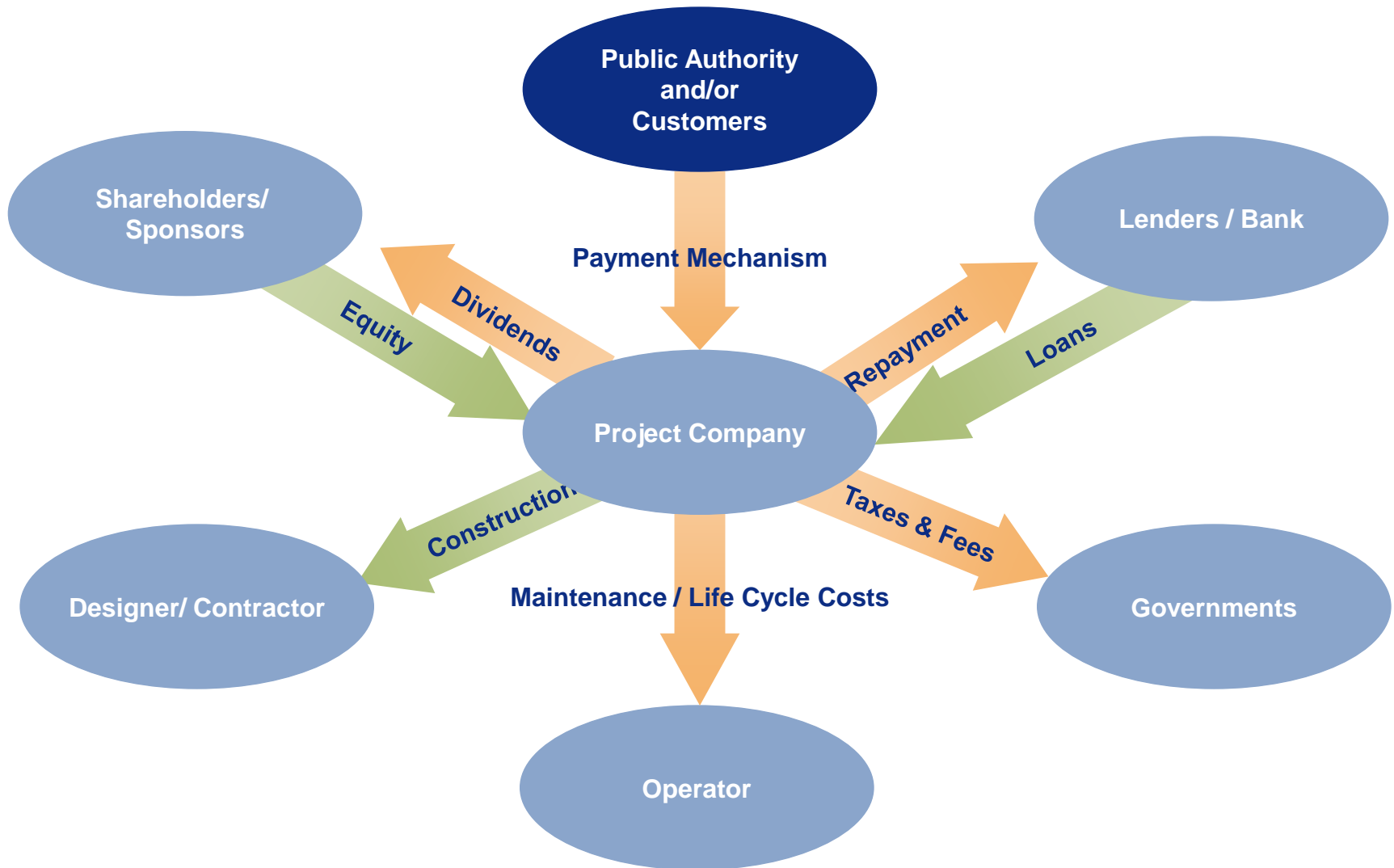
❖ TIFIA Loan Funds

❖ PayGo (Pay as You Go)

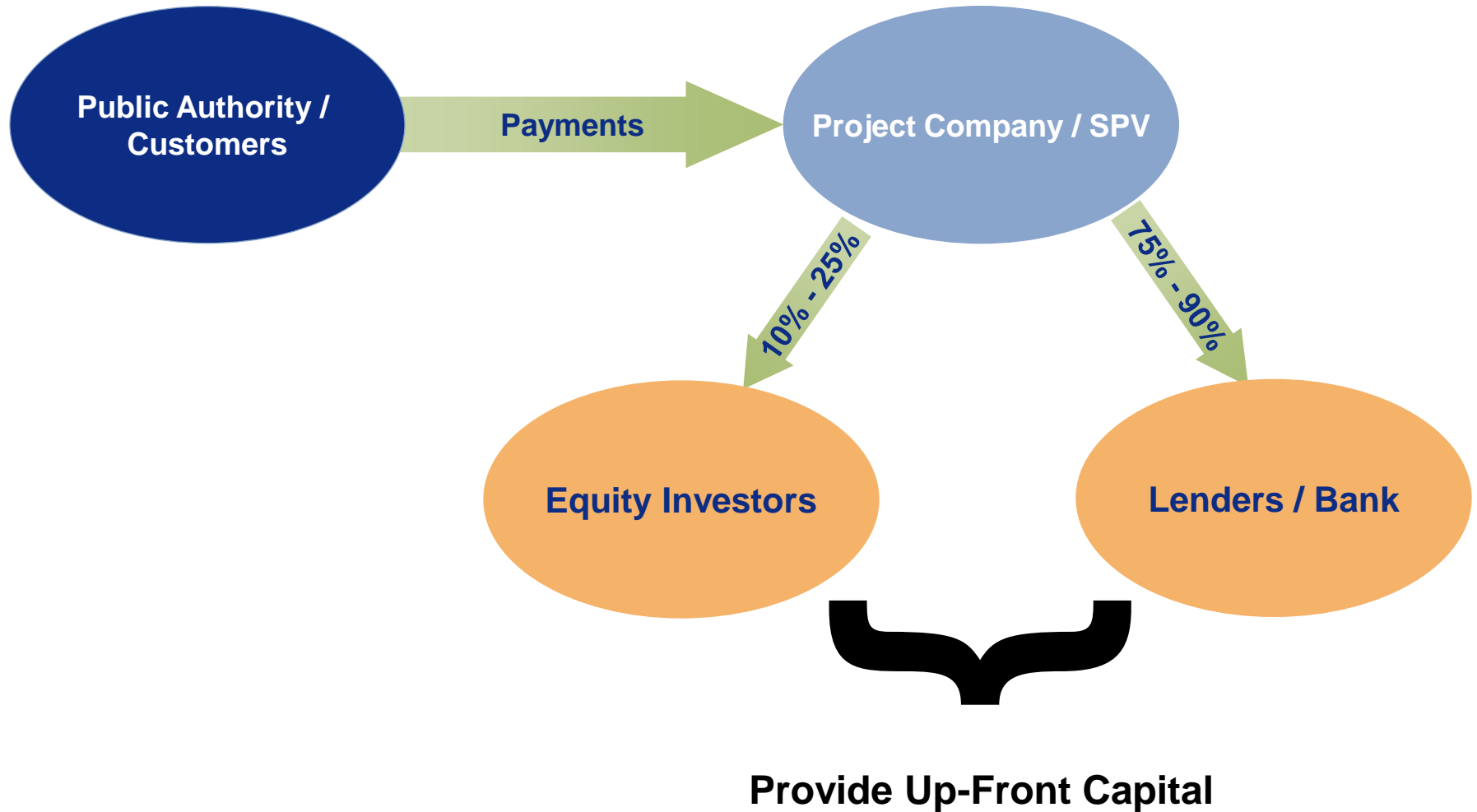
The Public-Private Partnership Basics

- ❑ PPP is a long-term contract arrangement between a public and private entity for the provision of infrastructure services – most PPP agreements range from 25 to 75 years in length
- ❑ The contract encompass all or portions of the project phases including, design, build, finance and/or operate and maintenance for a multitude of public structures (i.e. roads, hospitals, courts, schools, wastewater facilities)
- ❑ Common characteristics include:
 - ❖ Balanced sharing of risk between the public and private sectors
 - ❖ Output-based service specification contracts, as defined by the Public Sector
 - ❖ Innovative financing for the project – private financing to meet capital costs with a mix of public funds and/or user fees
 - ❖ Contractual incentives and disincentives clearly defined from the start to ensure that the private sector partner meets obligations
 - ❖ Asset is typically handed back to the public sector at the termination of the contract
 - ❖ Private-sector innovation used to shape new solutions

PPP – Typical Structure



PPP Infrastructure Financing – The Structure



Private Sector Financing Tools

❑ Funding Sources:

❖ User Fees

- Toll / Highway Revenues
- Passenger Facility Charges
- Farebox Revenues
- License Fees
- Availability Payments
- Shadow Tolls
- Hybrid (part toll, part subsidy)

❖ Public Subsidies

- Upfront capital contribution
- Milestone payments
- Tax credits
- In-kind contributions

❑ Financing Tools:

❖ Debt – Capital Markets

- Bank Debt
- Project Bonds
- Subordinate Debt

❖ Debt – Concessionary

- TIFIA
- Private Activity Bonds (PABs)
- Build America Bonds (BABs)
- State Infrastructure Banks (SIBs)

❖ Equity

- Private Equity
- Public Equity

Comparison of Financing Options

☐ Senior Debt

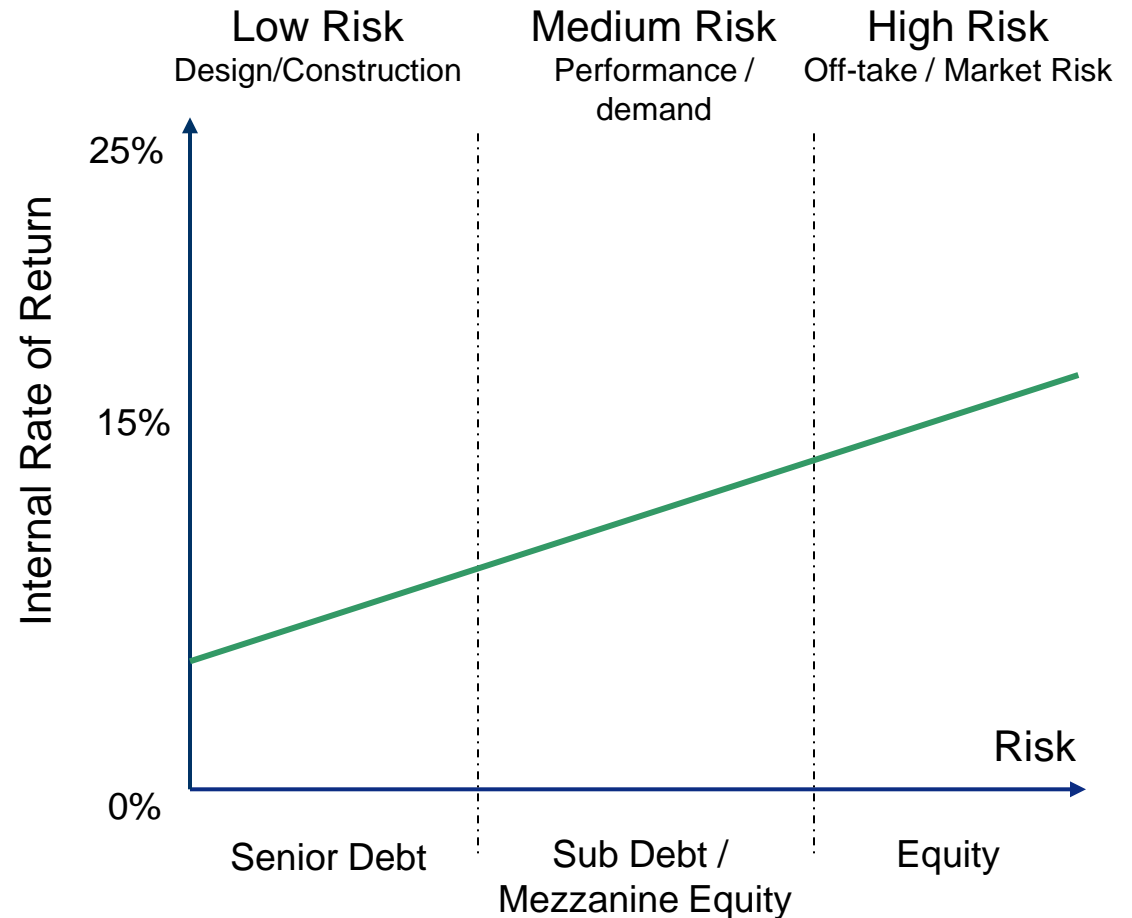
- ❖ Bank Loan
- ❖ Debt Capital Market

☐ Mezzanine

- ❖ Bank Loan
- ❖ Debt Capital Markets
- ❖ TIFIA Funds
- ❖ Private Equity Funds

☐ Equity

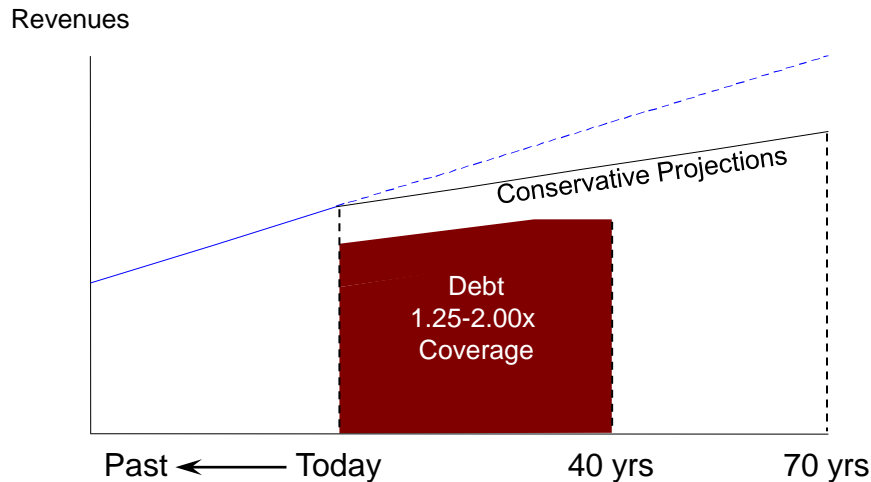
- ❖ Private Equity Funds
- ❖ Equity Capital Market



Private Sector Financing

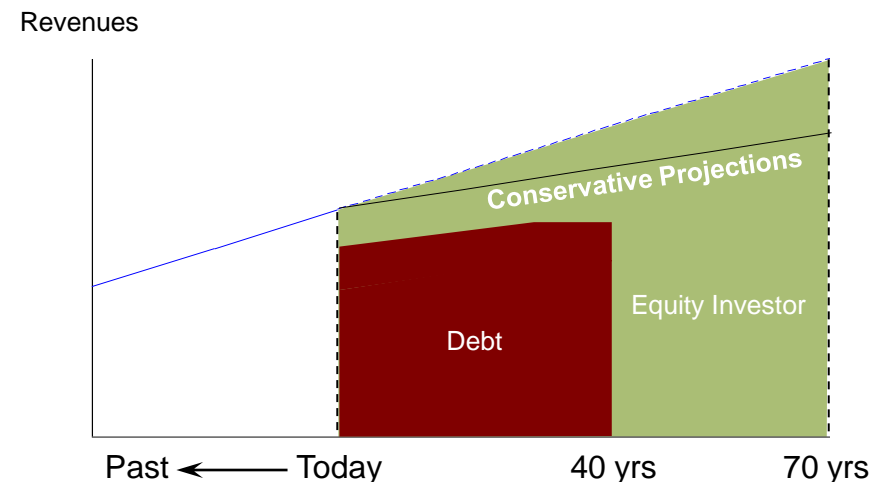
- PPP structure may provide an opportunity to capture the growth delta in volume and revenue increase

Municipal Bond Structure



Allows conservative amount of debt to fund projects

PPP Structure



More capital for given project (debt and equity)

Financing Considerations

- ❑ Private participation is not free money – i.e. credit rating
- ❑ New Federal financing programs have made private financing of infrastructure projects more competitive
 - ❖ TIFIA / PABs
 - ❖ Tax effects of depreciation and interest expense
- ❑ Project scope needs to be balanced with project's financial viability
 - ❖ Many iterations may be required to find a financeable scope
- ❑ The need for the private sector to make profit
 - ❖ Higher risk transfer to the private sector requires higher expected return
- ❑ Many new infrastructure projects require some level of public sector contributions
- ❑ Control over establishing future toll rates / user fees
 - ❖ Pre-fixed toll schedule vs. range-bound increase

Lender Considerations

☐ Predictability of Cash flows

- ❖ Greenfield vs. Brownfield
- ❖ Demand Risk & Payment Mechanism

☐ Performance Requirements

- ❖ Developer experience & qualifications
- ❖ Well-defined roles & responsibilities
- ❖ Project's Risk Profile (e.g. new technology)

☐ Equity Commitments

- ❖ Debt/Equity Ratio
- ❖ Parent Company Support
- ❖ Availability of Contingent Equity

☐ Coverage Ratios

- ❖ Annual Debt Service Coverage Ratios
- ❖ Loan Life Coverage Ratios
- ❖ Project Life Coverage Ratios

☐ Break Even Scenarios

- ❖ What if scenarios – i.e. sensitivity analysis

☐ Reserve Accounts

- ❖ Debt-Service Reserve Account
- ❖ Major Maintenance Reserve Account
- ❖ Escrow Account

☐ Equity Drawdown / Debt Repayment

- ❖ Cash Sweep
- ❖ Annuity / Sculpted / Balloon

Public vs. Private Financing

Public Finance - Typically, financing is achieved through the issuance of tax-exempt debt. Revenue sources for debt service could be general or special taxes or user fees in case of revenue bonds.

Strengths

- Public Sector retains ownership and direct operational control of the asset
- Generally lower cost of tax-exempt debt
- Issuer has established credit in most cases
- Deep, liquid tax-exempt debt market

Issues

- Full retention of all demand and operating risk
- No “equity” capital to add value, limited leverage
- Public Sector responsible for all capital expenditures (i.e. Renewal/Replacement)
- Funding delays could result in cost escalation

Private Finance - Typically, financing achieved through equity contribution and issuance of taxable and/or tax-exempt debt. Revenue sources for debt service and equity returns are typically user-fees or availability payments made by the public partner.

Strengths

- Equity helps generate maximum upfront funding
- Transfer of capital and operating cost risk to private sector
- Public retains control of project performance through concession agreement
- Can be structured to avoid direct impact on taxpayers

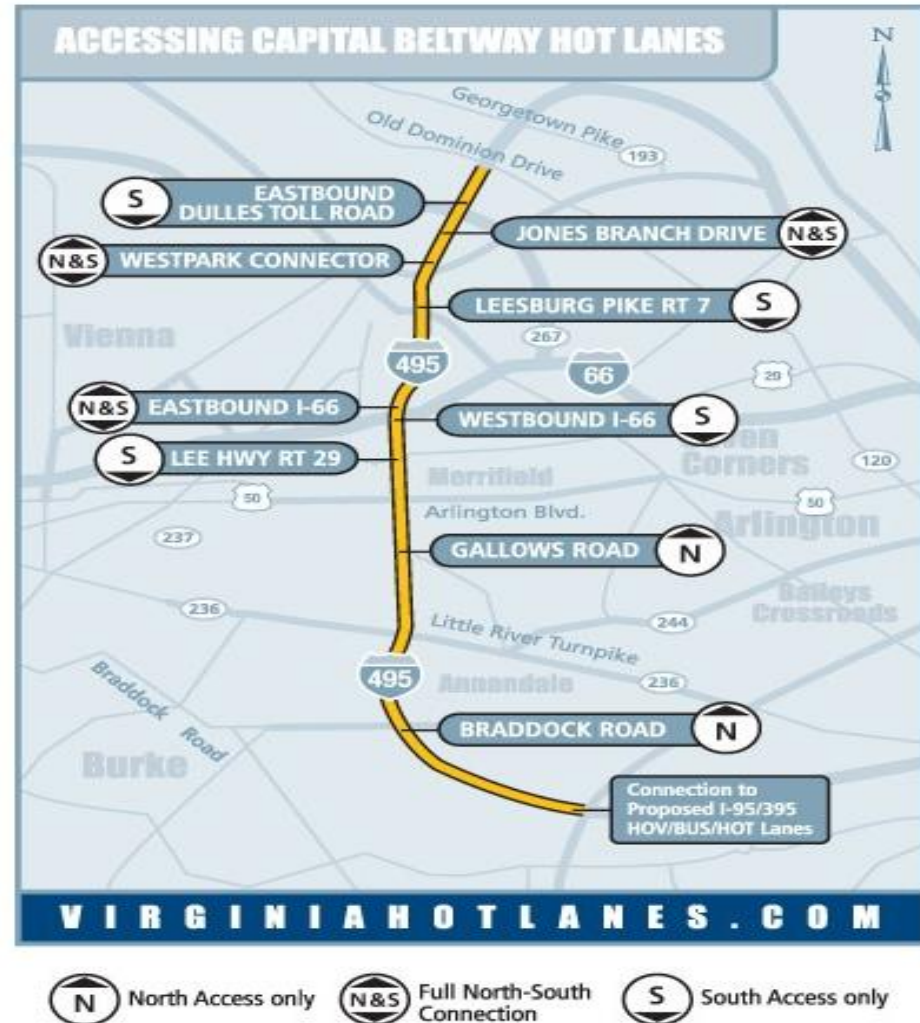
Issues

- Agency role shifts from day-to-day operational control to oversight
- Policy and public acceptability concerns, with focus on investor ROI versus direct agency control
- Possibly more frequent adjustment of user charges under private control
- Labor Issues

Case Study – I-495 Capital Beltway HOT Lanes Project

❑ Project Background

- ❖ First toll facilities in the US to use dynamic congestion pricing
- ❖ 3rd most congested highway in the U.S.
- ❖ New traffic capacity with 14-mile HOV network added to the Capital Beltway in Northern Virginia
- ❖ Private sector is responsible for construction schedule and budget, financing, traffic and revenue, and operations & maintenance
- ❖ Revenue sharing with the Commonwealth if the HOT lanes toll-paying volume exceed certain threshold
- ❖ Commonwealth not restricted from advancing surrounding transportation improvement projects

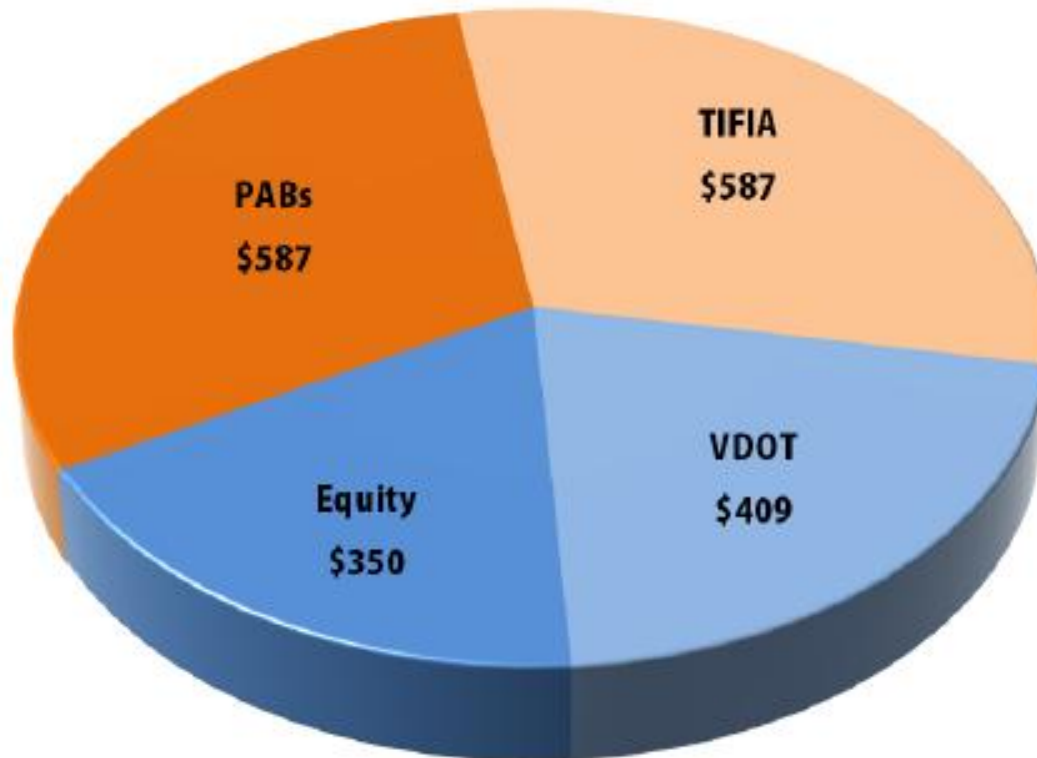


Case Study – I-495 Capital Beltway HOT Lanes Project

❑ Contract Agreement

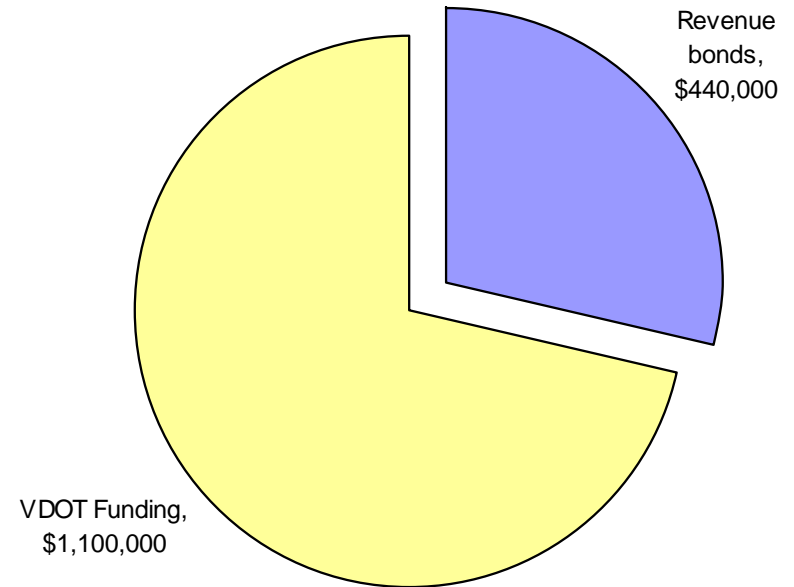
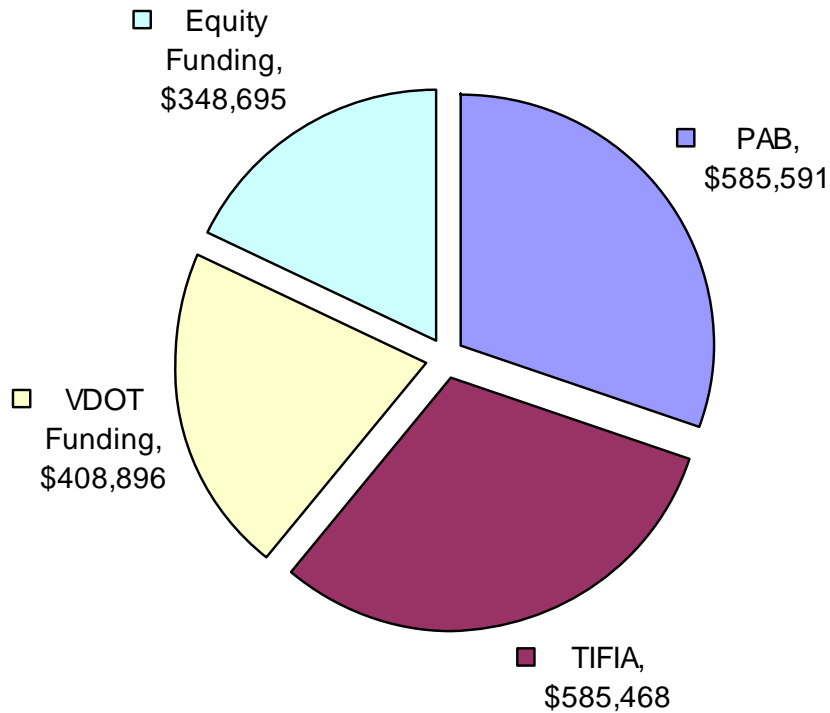
- ❖ Total construction cost: Approx. \$1.4 billion fixed-price design build contract
- ❖ 80-year concession term that began in December 2007
 - 5 years of construction period and 75 years of operations

❑ Funding sources – total \$1.93bn:

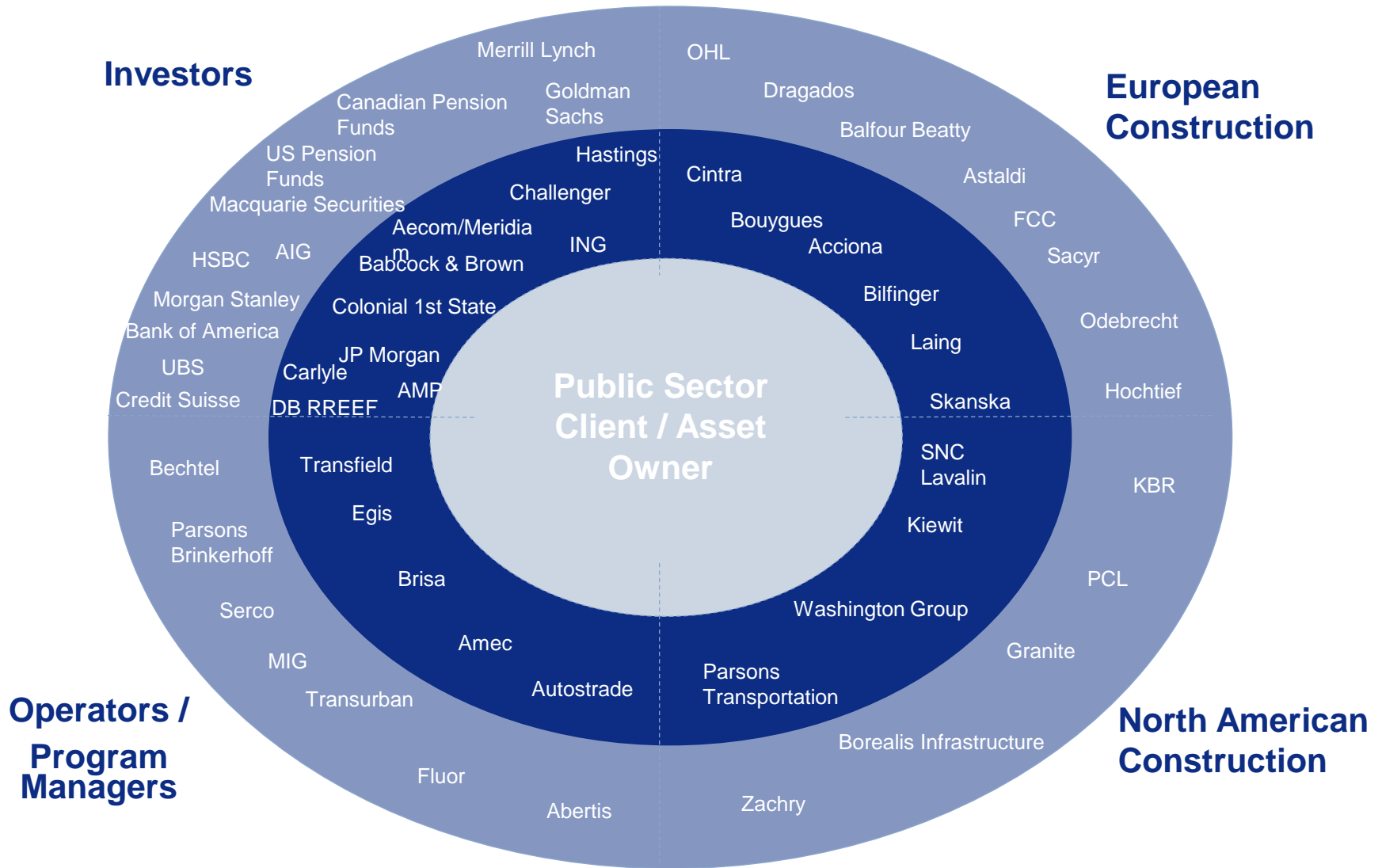


Case Study – I-495 Capital Beltway HOT Lanes Project

- Project Financing – Comparative analysis was performed to ensure that PPTA route required fewer public funds than the most likely alternative funding route



Key Industry Participants



Closing Remarks

- ❑ Significant availability of private equity for infrastructure projects
- ❑ Well-structured projects are being procured and financed even in the difficult financial environment
 - ❖ I-495 Capital Beltway HOT Lanes, Virginia
 - ❖ North Tarrant Expressway, Texas
 - ❖ I-595 Corridor Roadway Improvements, Florida
- ❑ Infrastructure investment is viewed as long-term, stable, predictable cash flows
- ❑ PPP is known to deliver more consistent quality of services and operating performance
 - ❖ A combination of the payment mechanism / contract and lender's due diligence reinforce desired behavior
- ❑ More than 20 States are actively pursuing or considering PPP as an alternative project delivery method for infrastructure projects
- ❑ "Partnership" is the key for successful project development and implementation
- ❑ Procurement process can be lengthy and costly

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