

Ballard Spahr
Andrews & Ingersoll, LLP

**“NEW OPPORTUNITIES FOR THE USE OF PPPs”
PRESENTATION BY DAVID L. WINSTEAD
TO THE NATIONAL COUNCIL FOR
PUBLIC-PRIVATE PARTNERSHIPS
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THE PROMISE OF P³

P³ Equation Is Important to Meeting Nation's Challenges

- WHAT
 - Achieves goals government cannot accomplish alone
 - Leverages government assets/customers
 - Infuses business ingenuity, know-how, efficiency, capital
 - Stimulates “viral” self-generating growth
 - Meets public needs cheaper, faster, better
- HOW
 - Relationships based on trust and transparency
 - Safeguard with standards and performance measures
 - Size, scope, complexity of 21st century problems dwarf capabilities of institutions and programs invented in 20th

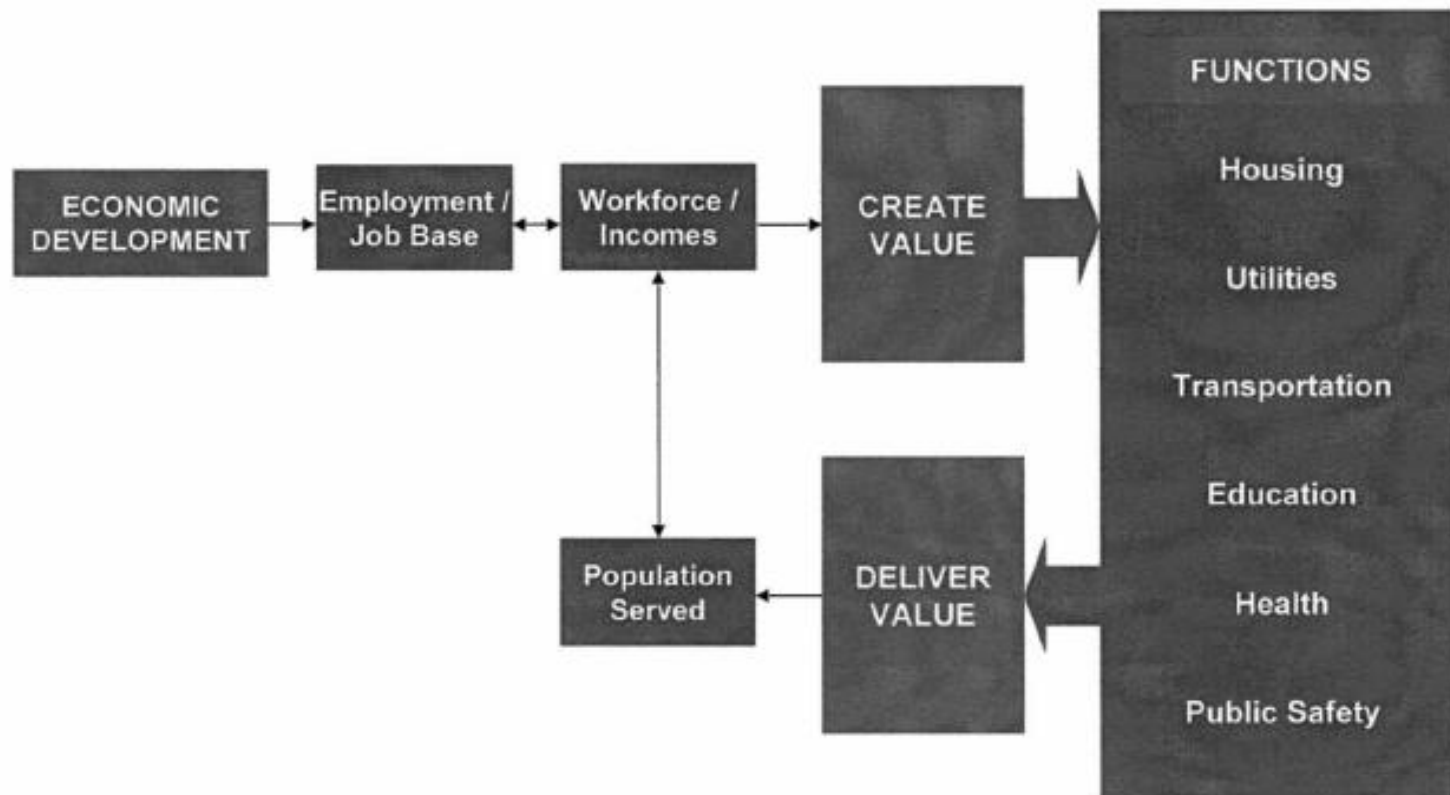
Principles

FIVE PRINCIPLES OF P³

1. P³ Captures Value
 - Business ingenuity, efficiencies, capital leverage government investment
 - “Funding multiplier” expands available resources
2. P³ Solves Problems
 - Faster, cheaper, better outcomes in complex functions
 - Applications in housing, infrastructure, energy, healthcare
3. P³ Overcomes Hurdles
 - Persistent, focused communications overcome potential/financial challenges
 - Flexibility, engagement surmount operational/regulatory barriers
4. P³ Needs Enablers and Incentives
 - Motivated agencies, enabling authorities incentivize private participation
 - Dynamic government markets attract ready/willing/able enterprises
 - Incentives applied to all parties promote risk management
5. P³ Builds Trust
 - Shared goals, incentives, safeguards
 - Transparent working relationships
 - Live-of-partnership agreements

P³ CAPTURES VALUE

Economic Development Enables Private Investment in Public Functions



P³ CAPTURES VALUE

Economic Value Derives from Private Capital, Public Property

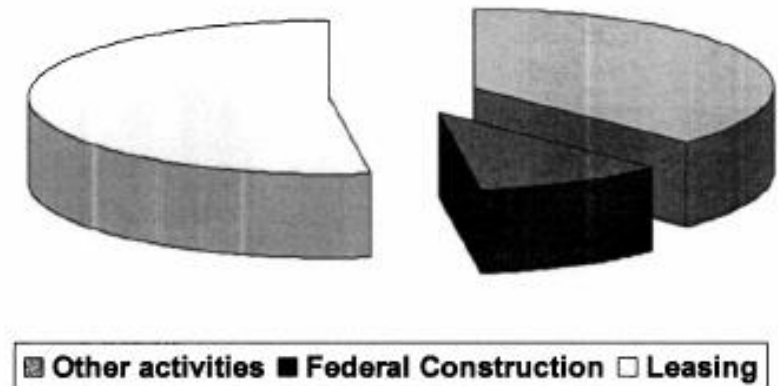
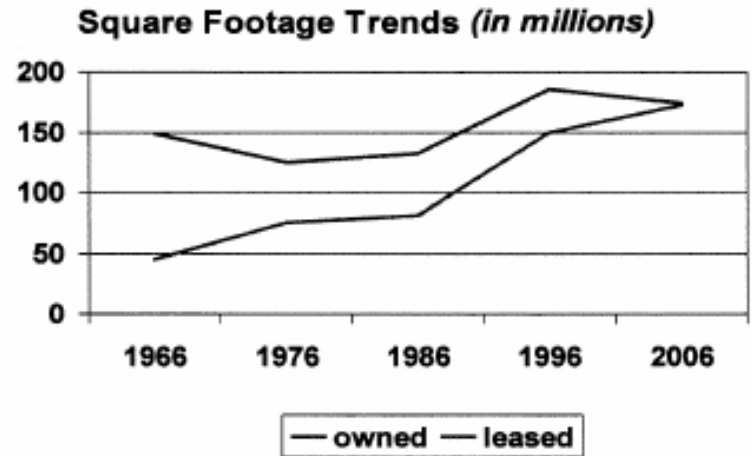
- HOW
 - P3 stimulates business to create value by injecting private ideas, energy, capital into public assets and/or services
 - Opportunities when government functions cross silos/real estate
- EXAMPLES:
 - **GSA:** Southeast Federal Center (DC): Redevelop major mix-use urban site; provide long-term management/sustainment
 - **VA:** Bayside (MD): Revitalize veterans' center for retirement housing/assisted living with major area impact
 - **USACE:** Gaylorn Texan Resort (TX): Lease USACE property for resort; revenues fund park

Current Issues Facing Federal Real Property Management

- Federal real estate portfolio
- Authorities GSA has
- Issues GSA faces
- Impact of scoring
- Infusion of \$5.55 billion from Recovery Act for construction, renovation, and green building initiatives

Portfolio Trends

- Government-owned space has remained relatively stable over the last 40 years while leased space has more than tripled
- Since 1990:
 - The rental of space budget has grown from \$1.5 billion to 4.3 billion - over 50% of the FBF budge obligations
 - Discretionary funds available for new construction and repair and alterations obligations have shrunk from 40% to 16%



Right-sizing of the Inventory

- Portfolio Restructuring Strategy
 - Reduced our underperforming assets from 45% percent to 25% through efforts of Federal Real Property Council
 - Reported excess 271 assets achieving a cost avoidance of \$611.9 million in capital reinvestment needs
 - Through the property disposal process, leveraged the equity in these assets to return \$139.4 million to the Federal Buildings Fund

The Federal Buildings Fund and Capital Investment Need

- GSA's Federal Buildings Fund (FBF) receives income from customer agencies paying commercially equivalent rent for space provided to them in Government-owned and leased buildings.
- GSA relies upon the resources of the Federal Buildings Fund (FBF) to operate, maintain, and invest in its owned assets; to meet all current lease commitments; and to fund the acquisition of new assets, whether leased or owned.
- New construction requirements for Land Ports of Entry (over \$5 billion), the Executive Branch, and the Judiciary (Courthouses) are \$10 billion.
- Reinvestment requirements to maintain existing federal buildings exceed \$7 billion.
- Positive impact of \$5.55 billion investment through Recovery Act into Federal Building Renovation & Energy Efficiency

Unique Elements of Real Estate

- Real estate is an appreciating asset for which the Government often has a long-term need.
- The self-insured status of FBF allows GSA to enter into operating leases requiring only the budget authority needed to cover annual lease payments.
- GSA's multi-year leasing authority allows contracts with lease terms of up to 20 years.
- GSA has responsibly funded and managed large scale programs, as well as significant individual projects, for which Congress authorized leveraged financing (not requiring up-front scoring of the full budgetary commitment).

Section 412 of the FY05 Appropriations Act

Grants GSA two new authorities

1. Retention of proceeds
 - FBF proceeds in FY07 – FY of approximately \$200m
2. Real property disposition
 - New vehicles of disposition, e.g. leaseback arrangements
 - Outlease/leaseback applications never approved for use

40 U.S.C. § 585(c)

- Authority to outlease unimproved property to private sector developer and leaseback buildings constructed on land owned by GSA
 - At the end of the term, improvements would revert to GSA
- Outlease restriction of 30 years is of concern to development community

ESPCs

- Authority to time-finance renovations that result in energy-savings
- \$200m in investment financed – more to come
- Administratively burdensome but growing potential – given 2030 goal of carbon-neutral buildings

Authorities of GSA

- Adaptive Use Authority
 - Authority to outlease or exchange unused portions of historic properties
 - Proceeds retained for use in historic properties
- Acquisitions-by-Exchange
 - Allows GSA to leverage equity in its assets
 - Must be used to acquire an existing building
- Cooperative Use Act Outleasing
 - Limited to certain activities and areas of buildings and adjacent land
 - Commercial rates can be charged
 - Proceeds can be retained for operational expenses

Current Issues

- GSA has two alternatives to acquire space - operating leases and direct federal construction. Building purchases are a third option but like new construction depend on scarce appropriations.
- Given the demands on the FBF, operating leases have become the most prevalent way of meeting new customer requirements.
- The commercially equivalent Rent collected from customer agencies housed in leased space covers only the obligations under lease agreements and administrative expenses.
- Only Rent collected from customer agencies housed in Government-owned space produces income (e.g., \$7 per square foot) for the FBF in excess of expenses.
- Increasing reliance on leasing erodes the income base of the FBF, decreasing capacity to acquire new owned space and meet the reinvestment needs of existing owned space.

Before Scoring

- Congress has periodically approved “off-budget” financing, allowing GSA to acquire real property assets through annual payments without requiring substantial, up-front budget authority.
 - In the mid-1950s, GSA received authority to privately finance construction of 23 buildings.
 - In the early 1970s, GSA received purchase contract authority to finance the construction of 68 projects worth \$1.4 billion adding 11m square feet of inventory.
 - In the late 1980’s Congress authorized a total of 10 lease purchase projects in annual Appropriations Acts.
- By all real estate metrics these alternately financed projects have been successful.

Criteria of an Operating Lease

Seven criteria define an operating lease

1. Ownership of the asset remains with the lessor during the term of the lease and is not transferred to the government at or shortly after the end of the lease term.
2. The lease cannot contain a bargain-price purchase option.
3. The lease term does not exceed 75% of the estimated economic life of the asset.
4. The present value of the minimum lease payments over the life of lease does not exceed 90% of the fair market value of the asset at the inception of the lease.
5. The asset is a general purpose asset rather than being for a special purpose of the government and is not built to unique specification for the government as lessee.
6. There is a private sector market for the asset.
7. The risks of ownership remain with the lessor (the project should not be on federal land).

Scoring Treatment Leases

- If any of these rules are violated, the lease is considered a capital or lease purchase for scoring purposes.
- PBS must obtain budget authority for the present value of the minimum lease payments plus taxes.
- If all of the rules are met, the lease is considered an operating lease.
- GSA need only budget for the annual obligations over the life of the lease.
- This short-term cost advantage creates an incentive to lease

Analytical approaches further restrict GSA

- Conservative assumptions
- Use an 85% rule not 90% to allow for change
- No consideration of asset appreciation
- Risk adverse/mechanical

Impact of Scoring

- Financial constraints and the budgetary treatment of capital investment influence the method of acquisition
- Limits the use of public-private partnership (P³) for GSA real estate opportunities
- Leasing where Federal construction is preferred
- Fewer 20 year leases
- Fewer opportunities for ownership
- Higher cost with shorter terms
- More complex leasing process / more transactions

Solutions

- P³ options (for example: Exchanges, Section 412 Projects, ESPCs) relieve scarce Federal Building Fund resources to provide capital for investment and reinvestment in real property assets.
- Focus on Government-owned assets which constitute the income-producing base of the FBF – generating \$7/square foot.
- GSA's unique role in the acquisition and stewardship of real property requires a balanced approach as described below:
 - Provide additional resources through direct appropriations into the FBF for national priorities and opportunity purchases.
 - Reinterpret scorekeeping guidelines under current authorities (with the agreement of congressional and administration stakeholders) to allow GSA to engage in P3 projects and leveraged acquisition of assets to meet long-term needs (e.g., sale/leaseback and lease/leaseback).

P³/Infrastructure Group at Ballard Spahr

- The P³/Infrastructure group at Ballard Spahr has experience in diverse legal disciplines that can be relevant to a P³ transaction as well as a track record in P³ projects. Projects by which government entities bring private sector participation into the ownership, operation or financing of traditionally public enterprises, can potentially involve almost any publicly owned asset, in a variety of legal structures.
- There are a variety of examples of projects in public housing, commercial development, transportation and energy that are worth mentioning:

Military Housing

- Pearl Harbor Naval Station
- McGuire Air Force Base/Fort Dix



Transportation

- **Southport (Philadelphia, PA)**
 - represented the Commonwealth of Pennsylvania in its effort to seek proposals from parties interested in participating in a public-private partnership to finance, design, develop, construct, operate, and maintain a new marine container terminal facility to be located in the City of Philadelphia



Transportation

- Farley-Penn Station Project (New York City)
 - rehabilitation and expansion of the Farley Post Office and Pennsylvania Railroad Station in New York City, involving the Port Authority of New York and New Jersey, Amtrak, and the United States Postal Service
- Central Texas Turnpike Project (Austin, Texas)
 - two financings for the Central Texas Turnpike Project in Austin, Texas
- TIFIA Program
 - Firm selected by the U.S. Department of Transportation as special counsel for the TIFIA program:
 - worked on numerous major TIFIA financings, to include:
 - Leeville Toll Bridge Project on the Louisiana Gulf Coast
 - Warwick Intermodal Project at the T.F. Green Airport in Warwick, Rhode Island

Toll Road Privatization

- I-95/395 HOT Lanes (Virginia)
 - Special Counsel to the Office of the Attorney General and the Department of Transportation (“VDOT”) of the Commonwealth of Virginia for Privatization Matters in October 2006, VDOT entered into an Interim Agreement with Fluor-Transurban to develop and operate high-occupancy toll (HOT) lanes along the I-95/395 corridor in northern Virginia.
- Pennsylvania Turnpike
 - represent of the Commonwealth of Pennsylvania in proposed privatization of the Pennsylvania Turnpike, whereby the Commonwealth would enter into a long-term concession and lease agreement with a private entity selected through a competitive procurement process
- Pocahontas Parkway (Richmond, Virginia)
 - underwriters in the tax-free construction financing of the Pocahontas Parkway, a four-lane toll road and a bridge near Richmond, Virginia. with an aggregate value of \$354 million
- Knik Arm Bridge (Anchorage, Alaska)
 - serve as counsel to the Knik Arm Bridge and Toll Authority for the Knik Arm Bridge Project, a P3 toll bridge in Anchorage, Alaska. Project included a concession agreement, \$600 million of financing, and a conditional loan pursuant to the TIFIA program, which will benefit the private developer



Energy/Infrastructure

- Montgomery County, Maryland
- Commonwealth of Pennsylvania/
PECO Energy Company



P³/Infrastructure Group at Ballard Spahr

- Utah Transit Authority
 - legal advisors to the Utah Transit Authority (UTA) which was transformed from a bus company to a multi-modal business--including both bus and rail operations--covering 78 communities in a six county area known as the Wasatch Front
- Union Pacific Intermodal
 - represented Bank of America Securities on a 1999 refinancing and restructuring of an intermodal container transfer facility that provides an intermodal link between the Ports of Los Angeles and Long Beach and the Union Pacific (UP) railroad network