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Understanding the 4 "P's" Before the P3 (Public-Private Partnership)

By Seth Merewitz

To get a P3 proposal to the starting line, public officials need to make sure that there is clarity and agreement on basic issues and priorities.

Aging and inadequate infrastructure, required upgrades and scarce public financial resources to pay for construction of new facilities is fostering a new spirit of innovation — out of necessity, rather than desire. Public-private partnerships (P3) is a tool that is being considered and implemented in California and elsewhere for economic development, real estate asset monetization and regional- and local-serving infrastructure.

Professor Stephen Goldsmith, director of the Innovations in Government Program at the Harvard Kennedy School, wrote an informative “5-Part Test” to get a public-private partnership project to the finish line. However, in California and elsewhere, many excellent P3 opportunities are lost as local officials fail to get the potential P3 to the starting line.

P3's is not a financing mechanism! In a successful public-private partnership, the public agency and the private investor function as “partners” pursuant to a contractual relationship throughout project development, financing, construction and even operation and maintenance.

P3's utilize many different deal structures and financing techniques to deliver projects that each allow for a certain amount of “risk shifting” from the public to the private entity. The public agency can also benefit from the expertise of the private provider, receive a project quicker than the normal procurement methods (for example, using authority found in California Government Code section 5956 et seq. for a P3 project or the recently expanded design-build authority) and, in return, the private entity receives a steady cash flow from the improvement with user fees or other payments.

Before a public agency is prepared to discuss if a public-private partnership arrangement is appropriate, consideration must be paid to the major steps required prior to the start of any public-private partnership proposal, negotiation or implementation. In short, an agency should first consider and agree upon the 4P's: Problem, Project, Priorities and Politics.

1. What is the Problem to solve?

While it may seem obvious when an element of a local agency infrastructure is in need of repair or upgrade, it is not always apparent what is holding up the fix. Is it simply a lack of resources, insufficient taxing authority or a stifling regulatory environment? Or maybe it is a credit rating downgrade, debt or pension obligations? Maybe the agency seeks operating efficiencies, capital cost reductions or rate stability? Whatever the local issue is, it is best to get the problem well-defined (and any other internal issues in order) before trying to entice a P3 partner to assist.



2. What Project is needed to solve the problem?

Many opportunities may exist to solve an identified problem. But without arriving at a defined project, it can be difficult to efficiently identify and evaluate potential partners. It is critical for the public agency to take time to analyze the various alternatives, educate elected officials and members of the public on the nature of the problem and the various approaches to fixing it, and then develop a vision for the desired project.

3. What are the Priorities of the community?

Where there can be clearly identified problems and projects, a community must also assess how this project and this problem compares with many other pressing needs. More than just prioritization of the project, agencies must look deeper and consider the various economic and risk factors for a given project. Finally, it is important to work with all parties to generate a common expectation and understanding of the process and timing of the negotiation and project delivery. Sometimes, agency staff or private parties can have expectations that do not match, which can lead to unnecessary challenges.

4. What is the Political environment for such a venture?

It is critical upfront to understand the political environment and various parties in and around a public-private partnership transaction — their goals, level of sophistication, risk tolerance, biases, etc. Some of the significant interested parties include: public agency-elected official, public agency staff / legal counsel, investors/developers, members of the public, special interest groups and regulators at the regional, state and federal levels. Moreover, many public agencies need to confront and overcome institutional bias from various outside consultants (financial, engineering, etc.) that may not have worked in a P3 context.

Finally, as the public-private proposal is being structured before being made public, make sure to prepare for success and build in elements to maintain transparency, keep open communication and regular interaction — as this is a marriage and every healthy marriage is based on open communication! Moreover, prepare for the P3 by making sure that the public agency has clarity on all required regulatory processes required for project approval (e.g. CEQA, NEPA, etc.) and an identified and secure revenue stream. Addressing these issues prior to the announcement of a P3 can also increase the amount of interest from investors and potential partners.

These P4 items can help the public agency prepare for the private investor/developer to better work cooperatively on the public-private partnership. Understanding these P4 items can also assist in the evaluation of the potential opportunity, working through the structure of the deal and then to implementation. Without a grounding in all these issues, parties can waste time and inflict great frustration on one another. We can do better! Our communities are counting on it.

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Seth Merewitz

Partner

(213) 787-2567

seth.merewitz@bbklaw.com