Private Sector Financing for Water Infrastructure

Notes for the Economic/Funding Working Group of the Blue Ribbon Panel on Water Sustainability

April 12, 2010

Robert L. Wagner, Principal
Public Private Partnerships Arizona, Inc.
Part of the Yavapai Regional Capital Group

Traditional Financing for Water

Municipal bonds, with or without USG or State assistance (e.g., stimulus monies and WIFA,).

- Rely on city/county/state tax flows to pay off bonds.
- Can be structured to rely on project-specific revenues in selected instances, but usually not.

Other specialized bonds, including Buy America Bonds, that have U.S. tax features attractive to some.

- Levels depend on authorizations by U.S. Congress.

Budget flows or other city/county/state/USG funds.

Private Financing Option

<u>Public Private Partnerships (PPPs)</u>

- *Definition*: use of private equity and debt under a legal contract between public and private sectors to design, finance, build, operate and maintain infrastructure assets.
- *Repayment source:* PPPs rely **only** on project revenues.
- *Size*: **<u>>$50 million</u>** or a group of smaller, similar projects totaling >$50 million.
- *Critical issues*: transparency, full up-front due diligence, clear and reliable revenue source, relationship with traditional financing sources, risk-sharing, benefits from WIFA guarantees/subordinated debt.

PPP Benefits

Greater Efficiency and Lower Costs

- Projects more likely to be delivered on time and to budget. (Early U.S. private power projects completed at about **40% lower cost** than their public counterparts.)
- Ability to use smart design and cutting-edge technology improves cost/benefit ratio.
- Governments avoid postponing new infrastructure until they have the funds in hand or building projects in pieces that ultimately cost more.
- Clear differentiation between *spending* and intelligent, long-term, economy-building PPP *investment*.

PPP Benefits (continued)

<u>**Risk-Sharing**</u>

- Proper allocation of risks to the parties best able to manage them translates into lower user fees.
- Public Sector can shed some risks the private sector is much better at controlling, such as construction risk.
- With *sensible* risk structuring, private capital on an <u>after-tax basis</u> is on a par with tax-exempt debt, thus construction and operational savings flow to <u>lower user charges</u>.

PPP Benefits (continued)

Transparency

- Thorough up-front due diligence required by private sector decreases costs to the public by eliminating uneconomical projects or those inadequately designed.
- Private financiers insist on knowing “where the bodies are buried” = avoiding costly surprises.
- Private capital is at risk over a long term so projects must be designed to highest engineering standards with long-term maintenance in mind.

PPP Benefits (continued)

Additional Funding and Economic Development

- Significant increase in investment for viable projects = more rapid growth in economies, jobs, and taxes.
- Private debt and equity translates to lower government debt and improved municipal bond ratings, or monies available for other projects.
- Governments *guarantee* public service delivery, not *provide* it as well.
- Delivery on-time and to budget with no change orders requires much better up-front design.

PPP Benefits (continued)

Other

- Benefit from smart design and technology if *output* rather than *design* specifications are set.
- PPPs reduce real estate developer influence that can unduly skew project selection and design.
- Private Sector must plan maintenance with a 30-50 year life-cycle in mind; maintenance hard-hit by governments' economic limits.
- Government less involved day-to-day; it can focus on making certain a PPP meets contractual obligations.
- While PPP users can *choose* to pay user charges, taxes are *mandatory*.

PPP Benefits (continued)

<u>Other</u> (continued)

- Getting U.S. banks back into project finance and diversifying away from real estate and exotic assets, will ensure that U.S. contractors have a level playing field in rebuilding the nation's infrastructure.
- Project lending can help revitalize the U.S. banking system, making it more competitive, while ensuring lower-risk credit portfolios.
- A rapid rise in well-conceived U.S. PPPs also will utilize $175 billion of investment monies currently sitting *unused* in equity infrastructure funds.