P3s – Where are we and where are we going with P3 projects?

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P3s – Where We Are, Where We Are Going, and What You Need to Know

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In its 2017 report, the American Society of Civil Engineers (“ASCE”) estimated that, by 2025, total spending needs related to infrastructure systems in the United States will be $4.59 trillion. Using current levels of funding, the ASCE predicted that there would be a funding gap of over $2 trillion. In order to close that funding gap, ASCE predicts that investment from all levels of government and the private sector must increase to 3.5% of U.S. GDP by 2025. In the face of such need, government entities are turning to alternative project delivery methods to find funding and meet infrastructure needs in an efficient and cost-effective manner.

This Article focuses on the recent and ongoing evolution of public-private partnerships (“P3”) and the relationship of P3s to the construction industry. Part I offers an overview of what the construction industry needs to know about P3s. Part II discusses the use of surety bonds in P3 transactions. Part III describes various issues to be aware of in the event disputes or challenges arise in a P3 project, including the use of Dispute Review Boards on P3 projects and lessons from a P3 project that failed. Finally, Part IV considers the future of P3 projects in the United States, particularly in relation to recent policy pronouncements from the executive and legislative branches of government.

I. What Does the Construction Industry Need to Know About P3s?

This Part will describe several different delivery systems for public construction projects, including the evolution of the P3 model and the design-build-finance-operate-maintain (DBFOM) elements of P3 projects, with a focus on the levels of risk shifted to construction contractors in these various forms of public procurement.

A. Design-Bid-Build

Most U.S. infrastructure projects have been developed using the design-bid-build method. This method involves three distinct phases: the design phase, the bidding phase, and the construction phase. During the design phase, the public owner contracts with an architect or engineer to design the project with sufficient specification that independent prime contractors can estimate and bid on the cost of constructing the project. During the bidding phase, prime contractors submit bids on the cost of building the project. Finally, during the build phase, the winning bidder builds the project. The public owner retains design risk while the builder assumes construction risk. The public owner also retains the responsibility to provide financing and must operate and maintain the finished project.

B. Construction Manager at Risk

A second commonly used project delivery system is the Construction Manager (“CM”) at Risk model. Under this model, the public owner engages a construction manager to manage all parts of a project. The CM interacts directly with the design team retained by the public owner, thus encouraging value engineering and expediting the contracting process. Design and
construction risk largely shifts from the public owner to the CM, although the public owner retains the responsibility to provide financing and must operate and maintain the finished project.9

C. Design-Build

Under the design-build approach, the public owner hires a single firm for both the design and construction parts of a project.10 The firm that wins the contract may either both design and build the project or subcontract segments of the work. Regardless, it bears the risk involved with both parts.11 This model works best for projects where functionality is more important than aesthetics, as builders might sacrifice architectural features in an effort to finish projects in a cost-efficient and timely manner.12 As in the design-bid-build and CM at Risk models, the public owner has the responsibility to provide financing and to operate and maintain the project.

D. The DBOM and DBFOM Models

Certain P3 approaches shift the responsibility and risk for operations and maintenance, or occasionally just maintenance, from the public owner to the private developer. These approaches can take several forms, such as a design-build-operate-maintain (“DBOM”) agreement or, when combined with financing as described below, a design-build-finance-operate-maintain (“DBFOM”) agreement. The developer’s obligations are set out in a single agreement, although certain aspects of the work may be subcontracted to specialist firms, such as to design-build contractors and to operations and maintenance firms.

The DBOM model (as well as the DBFOM model) offers long-term efficiency advantages over the traditional design-bid-build model. The DBOM team can coordinate the design and construction of a project to account for long-term maintenance of the project, “thereby reducing the risk that issues will go unnoticed or unattended and deteriorate into much more costly problems.”13 It is important, however, for the public owner to specify with particularity the project’s operations and maintenance standards over the term of the agreement, as well as “handback” expectations for the quality of the asset at the end of the term. Given the length of these contracts, which often extend 20 years or longer, problems stemming from unspecified expectations may persist for decades.14

E. Reimbursement Models

Under the DBFOM model a government entity enters into an agreement with a private sector entity to design-build-finance-operate-maintain the project. Thus, the private party is tasked with financing the project. These projects are notable as most of the risk is transferred to the private sector entity. Typically, there are two types of payments that the private sector will receive in turn for assuming these risks. These two payment models are the revenue-risk model (also called the revenue concession model) and the availability payment model.
1. The Revenue-Risk Model

Under the revenue-risk model, the private developer acquires an interest in the project’s revenues for a specified period, for example, an interest on the tolls paid on a toll road. The developer, not the public owner, bears the risk if revenues underperform projections, but also receives the benefit if revenues exceed projections, subject usually to a revenue sharing mechanism with the public owner. Because the developer assumes greater risk, the developer will expect a greater return on its investment.

2. The Availability Payment Model

Under the availability payment model, the public owner makes periodic payments to the developer during the operation of the project. These payments may be combined with milestone or progress payments during construction. Although the public owner may rely on revenues generated from the project to partially fund the payments, the public owner bears the risk that those revenues materialize as expected. Availability payments are often used on projects that do not produce revenue or whose revenue is insufficient to cover a project’s cost (as a revenue concession would not be possible without further public subsidy). The public owner may pledge revenues from the project as security for its payment obligations; but absent such a pledge, the developer is relying on the credit of the public owner, which may also include the risk that the funds will be appropriated by the public owner’s legislature.

F. Project Structure

The charts above illustrate the differences in project structure between a classic construction project and a P3 construction project. A fundamental difference between P3s and traditional construction projects is that there is a “middle-man” between the construction and O&M contractors and the government. Typically, the project sponsor, which consists of one or
more equity investors, will form a limited liability company (“LLC”) or other form of special purpose vehicle (“SPV”) entity. The LLC will be responsible for raising capital both through contributions of the equity investors and through the issuance of project debt, implementing the project’s DBFOM aspects (pursuant to the DBFOM contract that the LLC and the public authority enter into), and contracting with the construction contractor through a design-build contractor and contracting with an operations and maintenance contractor through an operations and maintenance contract (although in some cases the LLC will “self-perform” the operations and maintenance work). The construction contract and operations and maintenance contract are known as “drop-down” agreements because they are “dropping down” the obligations in the DBFOM agreement between the public authority and the sponsor to the construction contractor and operations and maintenance contractor, respectively.

Two other differences from the classic approach are worth noting. One is that one or more construction firms that make up the construction contractor (which is often a design-build joint venture) will take an equity participation in the project sponsor. This is intended, in part, to give the construction contractor “a seat at the table” in the negotiation of the project agreement between the public authority and the project sponsor and in the financing of the project. Another difference from the classic approach is that the construction contractor and the O&M contractors will enter into an interface agreement. The interface agreement works to allocate risk and limit potential claims disputes between the construction contractor and the operations and maintenance contractor as part of the handoff between the construction and operations and maintenance phases of the project.

II. The Role of Surety Bonds

The prior section described several of the structural differences between the classic approach of public construction projects and the P3 model. Another major difference relates to the use of surety bonds in P3 projects as compared to traditional public construction projects.

In 1935, Congress passed the Miller Act, which requires all bidders on federally-funded public works projects exceeding $100,000 to furnish both a payment bond and a performance bond. The payment bond must be “equal the total amount payable by the terms of the contract,” while the performance bond must be “in an amount the [contracting] officer considers adequate, for the protection of the government.” Payment bonds provide protection to subcontractors worried about being paid, while performance bonds provide the public with recourse if the contracting party fails to complete the project. Following the federal government’s lead, every state has passed a “Little Miller Act,” which requires contractors to secure both payment and performance bonds.

P3s generally are state and local government projects and therefore are not subject to the (federal) Miller Act. Depending on the particular statutory authority under which a P3 is procured, a P3 may or may not be subject to a state’s Little Miller Act. In circumstances where neither act applies, public sponsors and industry participants are debating the merits of requiring surety bonds relative to other forms of project security, either through P3-specific statutes or contractual requirements.
A. Rationale for Surety Bonds in the Traditional Context

Surety bonds have been widely regarded as important means by which to protect taxpayers in traditional infrastructure procurements. Payment bonds protect public owners, subcontractors, and suppliers from a contractor’s inability to meet its financial obligations. In particular, subcontractors and suppliers are able to rely on the payment bond in the event of non-payment, which in turn promotes continued work without interruption. Performance bonds protect public owners and ultimately project users from failure of the contractor to perform, thereby reducing the risk to timely completion of the project.

B. Opposition to Surety Bonds in the P3 Context

Project developers often assert that surety bonds are unnecessary in P3 projects. While surety bonds were designed to ensure completion of a project, a P3 project includes obligations that extend beyond construction, and those ongoing obligations and compensation arrangements are considered by some to provide sufficient incentive to ensure completion of the project. For example, if a developer’s compensation is contingent upon project revenues (in the case of a revenue concession project) or upon ongoing availability of the project to the public (in the case of an availability payment project), the developer is strongly incentivized to complete the project on time. Moreover, the developer’s own lenders will insist on protections to ensure prompt repayment of any debt and to prevent termination of the P3 agreement (which may occur if the developer fails to complete the project on time or keep the project open to the public). Therefore, because other mechanisms exist to ensure timely completion of the project, developers often take the position that a surety bond is an unnecessary expense.

In many cases, the developer subcontracts the responsibility for design and construction of the project to a design-build contractor. In these circumstances, the financial participants in control of the project, including the equity owners and lenders, may impose surety or other security obligations on the developer, just as a public owner would do if it were contracting directly with the design-build contractor. But the developer often seeks flexibility to determine the appropriate type and terms of security (as determined by the developer) and resists attempts by the public owner to impose specific obligations by contract.

Private participants in a P3 project, including design-build contractors and developers, may also prefer alternative forms of security, such as letters of credit. A developer’s investors coming from the project finance industry are typically more familiar with letters of credit than surety bonds. In certain cases, a letter of credit may also be cheaper, although costs relative to bonds may vary considerably.

Developers and design-build contractors may fail to recognize the potential advantages of bonds over letters of credit: a performance bond guarantees performance, while a letter of credit guarantees only payment; bonds provide the principal with an opportunity to defend against the claim, while letters of credit are drawn on proper demand; bonds do not adversely impact the principal’s balance sheet, while letters of credit are reflected as a contingent liability; and bonds do not require the principal to post collateral to secure the bond, while an issuing bank may require a letter of credit to be secured by collateral. Nonetheless, a developer may seek
flexibility to determine for itself how to satisfy the project security requirement, and therefore request the option to post either a bond or a letter of credit as it determines appropriate.

C. Support for Surety Bonds in the P3 Context

Subcontracts and suppliers have advocated in favor of requiring surety bonds for P3 projects, no different than for traditional projects. The American Subcontractors Association recently asserted that “the reality of construction contracting” is not changed by the use of a P3 and “[t]he successful undertaking and timely completion of a P3 . . . will require that construction subcontractors and suppliers be fully and timely paid”, which is best ensured by a surety requirement.26 While the P3 structure may motivate a developer to timely complete a project, that may not necessarily ensure timely payment to subcontractors and suppliers along the way.

In the event of a dispute with subcontractors and suppliers or other circumstances leading to delayed payment or even nonpayment, the project’s progress could suffer, and service commencement could be delayed. The lack of any surety bonds in favor of subcontractors and suppliers marginally increases risk to those firms, and therefore indirectly increases total project costs as subcontractors and suppliers account for that risk. Letters of credit may be inadequate for protecting subcontractors and suppliers or, given the relative novelty of letters of credit in the infrastructure development industry, cause confusion as to the relative rights of competing beneficiaries.

Advocates also note that while investors, lenders, and letters of credit can ensure payments are made to a public owner or to subcontractors when required, they cannot ensure performance. The Surety & Fidelity Association of America argues that those “under the misimpression that [surety] bonds do not benefit the public . . . on a P3 project . . . because the concessionaire arranges for the project financing” fail to recognize “the performance protection aspects of the performance bond.”27 In other words, a defaulting developer may compensate a public owner for its failure to perform, but that compensation does not necessarily result in timely completion of the project and availability for public use – which is the public owner’s ultimate goal.

III. What Happens If Something Goes Wrong?

Although there are of course many benefits to P3 projects, there is always the possibility that something goes wrong. This Part seeks to explain some of the steps that construction lawyers can take to prevent or minimize a negative outcome if something were to go wrong during a P3 projects. These actions will be analyzed in two parts, those that can be taken before and during the bidding process to mitigate risks that may occur, and those that apply after the project has been awarded. It then explains the nature of Dispute Review Boards in the P3 context. It concludes by telling a cautionary tale about a P3 project gone wrong.
A. Before and During the Bidding Process

There are numerous ways that a construction lawyer can minimize potential negative exposure or outcomes before and during the bidding process.

First, when initially entering the P3 market it is helpful to partner with firms that have experience in this robust, diverse, and competitive market. As every jurisdiction has different regulations and rules that impact the cost and success of a project it is helpful to work with organizations and individuals who know these factors. Firms that are experienced in the P3 space can serve as an invaluable resource for those looking to enter the field.

Second, it is important to remember that different jurisdictions have different laws. P3 projects are often subject to the oversight of multiple governmental authorities. Thus, it is important to understand the laws and regulations of these authorities and to keep in mind that the statutes that authorize P3 projects will differ by jurisdiction. Although bidding documents often summarize the local laws, it is important to remain cognizant of the fact that the laws pertaining to a project will vary by location. Furthermore, laws pertaining to a P3 project may differ from those applicable to a traditional public construction project, so it is important to be aware of these differences. Similarly, it is important to ensure that any licenses required by the city, county, or state are acquired and that any differences in licensing requirements related to P3 projects are noted.

Third, P3 projects are uniquely sensitive to the contemporary political atmosphere. It is important to understand the likelihood of a project’s success and any potential opposition given the relevant political actors and viewpoints. It is best to be aware of the political dynamics at the federal, state, and local levels to best understand the interplay between a particular project and the political atmosphere. Project developers assess the political climate to determine whether the likelihood of project completion is high enough to support the investment of time and expense that the pursuit of a P3 project requires.

Fourth, take advantage of opportunities to communicate with the government owner throughout the bidding process. Workshops and answer sessions can lead to valuable information that increases an understanding of the project and makes a bid more efficient. Having a conversation with the government can cultivate a positive relationship while allowing a project sponsor and construction contractor to obtain desired revisions to its bid. Additionally, government owners appreciate thoughtful, reasoned, and engaged participation. These processes are often different from a traditional procurement in which interaction with government owners is limited. The construction contractor and its attorneys should develop an approach for participating in this process in a P3 project. With the project sponsor as the primary interface with the government owner, the construction contractor and its attorneys should work with the project sponsor to develop a mechanism for the contractor to raise its material legal issues either directly through participation in meetings with the government owner or indirectly through the project sponsor.
B. After the Bid Has Been Awarded

There are several actions that can be taken by construction lawyers to minimize the impact of project risks after a bid has been awarded.

First, remember that a construction contractor’s rights and remedies may differ from those of a traditional construction project. As described above, the construction contractor is not in direct privity with the governmental owner, as is usually the case in a traditional construction project. As a result, the construction contractor has to pursue its remedies through the project sponsor and therefore should ensure in its “drop-down” design-build agreement with the project sponsor its rights to assert claims and pursue remedies are protected. Furthermore, a governmental entity may have sovereign immunity defenses, which can limit a construction contractor’s ability to seek legal recourse against them, either directly or through the project sponsor. In some jurisdictions, a waiver, or partial waiver, of sovereign immunity defenses applies to a P3 project. It is important to be aware of the specific sovereign immunity defenses and associated dispute resolution process that applies in the jurisdiction in which the P3 project is undertaken. Also, as described above, most availability payments in a P3 project are subject to appropriation and, as such, it is important to consider appropriations risk in the context of a P3 project. In addition to availability payments, other types of payments in P3 contracts (under both the revenue risk and availability payment models) typically are subject to appropriations risk, such as termination payments and payments related to certain events, known usually as supervening, relief, compensation or adjustment events. A construction contractor will not have a separate claim against the project sponsor related to a failure of a governmental entity to make an appropriation.

Second, it is important to look into labor and subcontracting requirements. Many P3 projects require that certain thresholds are met relating to the hiring of disadvantaged, minority, or female-owned businesses. In addition, there are potential laws relating to the cost of labor, such as prevailing wage laws, or to entering into project labor agreements. It is important to keep these factors in mind when hiring subcontractors and labor.

C. Dispute Review Boards

A common method to mediate disputes in the P3 sector is the use of a Dispute Review Board. It is important for P3s to have management systems in place for preventing issues from becoming formal disputes and for resolving disputes that inevitably do arise. This Part offers a discussion of DRBs and how they can accomplish those goals. A DRB is formed at the beginning of a project to follow construction progress, encourage dispute avoidance, assist in the resolution of disputes, and issue non-binding recommendations that parties are free to accept or reject. The use of a DRB is subject to applicable law in a jurisdiction where a P3 is being undertaken as well as the preference of the procuring authority, when the DRB structure is permitted or not otherwise restricted by law.

For the government owner, the risk profile of a P3 project will differ from a traditional project. For one, the government owner will pass the risks of design, construction, and operation
to the project sponsor through a P3 developer agreement. Additionally, many P3 agreements limit the grounds on which the project sponsor can make claims against the government owner, often to fundamental commercial areas. However, there are still risks that DRBs can mitigate. For one, high-stakes fundamental commercial claims warrant the use of DRBs. DRBs can often foster a sense of partnership that benefits both partners and the project as a whole. Additionally, claims in one area of a P3 project can have tangible impacts on the project as a whole, meaning that DRBs can be useful in resolving even seemingly minor or isolated claims. Another characteristic of P3 projects is increased public scrutiny. A DRB can provide transparency and neutrality that will justify decisions to the public. The project sponsor can use a DRB to provide a solid basis for decision in discussions with its lenders. DRBs can also be used to avoid default terminations.

To determine whether and what type of a DRB should be used on a given P3 project it is helpful to first create a “dispute risk profile.” A completed dispute risk profile should detail the “type, frequency, and size and project impact of disputes that could arise on the subject project.” Additionally, it is best to consider which players would be involved in certain disputes. Next, each player involved in the P3 project can assess potential dispute resolution options and the positives and negatives of each.

The conventional DRB model that is used in the U.S. is relatively simple. At the beginning of the project, three neutral members with extensive experience in construction and claims-resolution will be appointed to the DRB. It is best practice for DRB members to be selected in a consensual nature from a pre-selected pool of experts. After the DRB’s members initially become familiar with the project, they will be kept abreast of project developments and will periodically return to the project site to receive status updates and identify emerging disputes. A DRB is also typically available to give the parties advisory opinions. If disputes do arise, a DRB manages and organizes the hearings and decisions process, oftentimes through informal hearings without the presence of lawyers. Typically, parties can choose whether to accept or reject a DRB’s recommendations.

DRBs can be (and oftentimes are) customized to better manage particular friction points or dispute profiles. Sometimes, DRBs will be implemented for use in only some of the project’s friction points. For example, a DRB to deal with government owner/project sponsor disputes. Sometimes, subject matter DRBs can be used that will resolve disputes centering on certain topics. Despite the temptation for a focused or narrow DRB, the costs and logistics of multiple DRBs lead many projects to use an “Omnibus DRB” that shares the cost of the DRB among parties depending upon the user of the process. In addition to sharing costs, an omnibus DRB has a holistic view of the entire project allowing it to take all relationships and potential problems into account, leading to uniformity and consistency.

Due to the long-term nature of P3 projects and the complicated issues different actors face DRBs can be used to minimize friction points and help better deliver the benefits of the P3 model. As described above, however, it is important for the construction lawyer to keep in mind that the DRB model is typically used between the government owner and the project sponsor. The construction contractor needs to understand this structure if it does exist and have a vehicle
for asserting claims through the project sponsor as part of the “drop-down” design-build agreement it enters with the project sponsor.

D. A Cautionary Tale

While the nascent P3 market in the United States has seen a number of successful transactions across different P3 structures (both revenue risk and availability payment) and different asset classes (roads, bridges, airports, ports and social infrastructure, such as courthouses, student housing and public buildings), a cautionary tale about a project gone wrong demonstrates some of the unique risks to be aware of in relation to the P3 model. The I-69 Section 5 project was procured by the Indiana Finance Authority (“IFA”) and Indiana Department of Transportation as an availability payment P3 that aimed to build a construct a portion of a greenfield road in Indiana. The project failed due to myriad problems, despite having no complex construction challenges. In fact, the failure was significant enough that it has led to speculation that it may have played a role in the Trump Administration’s shifting attitudes on P3 projects.⁷⁴

It should be noted that the challenges of the I-69 Section 5 project relate to a unique confluence of events that is unlikely to occur in other P3 projects.⁷⁵ However, specific events that occurred on the I-69 Section 5 may be more likely to occur in isolation on other P3s and by themselves could pose significant challenges. The failure of the project was driven by the default of an experienced Spanish contractor, extraordinary project delays, insufficient liquid security, and a lack of time for shareholders to devise a solution.⁷⁶

The project consisted of the construction of a 21-mile section of U.S. Interstate 69 that is a portion of a larger project to extend Interstate 69 from Indianapolis to Evansville, Indiana.⁷⁷ The winning bid had an estimated cost of $325 million.⁷⁸ The term of the agreement was 35 years and the project plan called for construction to be finished within 27 months.⁷⁹ As the project payments were structured as availability payments, the winning bid team’s risks were largely contained to building the road, keeping it up to standards, and keeping costs low.⁸⁰

The winning bid team (an equity partnership between a Netherlands infrastructure fund and a Canadian pension fund investment manager) signed a design-build contract with a Spanish company that was an affiliate of the infrastructure fund.⁸¹ The features of the contract were relatively common with market practice.⁸² The lead contractor had a good international reputation but had never been involved with a project in the United States P3 market.⁸³

It did not take long for problems to arise. Delays began almost immediately as a result of bad weather, slow design work, and a slow permit approvals process.⁸⁴ Preliminary matters such as erosion control and tree clearing could not begin until winter, leading to further delays.⁸⁵ At the time the four-month delay was disclosed there was an eight-month buffer between the project’s substantial completion date and longstop date.⁸⁶ Around the time that delay was disclosed, the project applied for several relief events, including permit delays.⁸⁷
When the four-month delay became an eight-month delay, the project began to depart even further from the norm. As the substantial completion date was pushed closer and closer to the longstop date, Standard & Poors (“S&P”) lowered its credit rating for the project.

Although the governmental body (the IFA) considered offering schedule relief, there was another unanticipated tipping point. In September 2016, the project drew on its construction letter of credit. At the same time there were rumors that subcontractors had not been paid. These matters led to further downgrades and negotiations to resolve the situation with the contractor. A settlement was reached with the IFA extending the substantial completion date to May 31, 2018 (an extension of 19 months) and the longstop date to November 30, 2018 (an extension of 13 months). The settlement also committed to providing funds to support construction efforts, reimburse delay costs, and replenish the drawn construction letter of credit.

Although the settlement meant an end to the project’s financial woes, the project ultimately failed when the contractor was unable to commit its share of funds after its bank lenders cut off its credit lines. In an unsuccessful effort to secure more loans, the contractor’s parent filed a pre-bankruptcy motion in Spain to negotiate a restructuring. As that effort was unsuccessful the parent eventually applied for bankruptcy protection.

By April 2017 it appeared that the project lacked funding and was likely to default even as the parties continued to try and find a solution that did not involve the contractor. By that summer, the IFA had received legislative approval to issue conventional bond financing to complete the project. In August, an agreement was finalized that allowed the lenders to terminate the concession agreement while reimbursing their outstanding debt balances. A default did not occur and bondholders were reimbursed at par value plus a premium (that was paid for by the developer) for the completed portion of the roadwork.

In summary, four specific circumstances derailed the I-69 Section 5 Project. One, insolvency of the construction contractor and the parent that did not allow the contractor to meet its obligations to complete the project at the agreed upon price and schedule. Two, a dearth of local contractor experience that led the mismanagement of early delays to have cascading and compounding effects. Three, a bid selection process that focused upon the least cost. Four, insufficient levels of performance bond insurance that did not allow performance bonds to assist in the replacement of the contractor. As described above, the combination of all of these factors contributed to the significant issues that led to the governmental owner taking over the project, but any of these factors, in isolation, could pose challenges to the success of a P3 and should be kept in mind by a construction contractor in participating in a P3 project.

IV. The Future Of P3s

The combination of the significant infrastructure needs of the United States and the continued growth of the P3 market has led to actions at the federal executive and legislative branch levels to propose federal policy challenges that would promote the use of P3s. While most P3 transactions are undertaken at the state and local levels of government, the federal
government can play a critical role in developing policies that facilitate and encourage the consideration and implementation of P3s.

In early 2018, the Trump Administration released its proposed infrastructure plan (the “Plan”). Explicitly, the broad points of the Plan appear to be silent on P3s, other than a specific reference to passing legislation to “eliminate constraints on [the] use of public-private and public-private partnerships in transit” by eliminating the constraints within 49 U.S.C. Chapter 53 and its implementing regulations. However, proposals throughout the Plan would have broad implications and impacts on the P3 market in the United States.

Moody’s Investment Services has suggested that the Plan would result in more private investment through P3 projects. Specifically, Moody’s cites the Plan’s proposals for expansion of authority for federal agencies to use alternative delivery methods, including P3s, for project procurement, increasing federal programs providing low-cost loans and private activity bonds to finance infrastructure projects, including P3s, and streamlining of federal permitting processes. Moody’s predicts that the future of P3 projects will be dependent on the ability of state and local government to raise revenue in nontraditional ways. Moody’s scores the Plan negatively for a lack of funding details and the long-term problems that can potentially be caused by shortened environmental reviews.

This Part will now examine the proposed Plan in detail and the impact it would have on the future of P3 projects across the United States.

The Plan proposes to create an infrastructure incentives program that would encourage private investment in infrastructure. The Plan states that the incentive program would aim to attract significant new non-Federal revenue streams, modernize project delivery practices, increase economic growth, and spur the development of rapidly involving infrastructure technology.

The incentives program would function through state and local governments receiving grants from the federal government. Once selected for the incentives program, project sponsors would enter into agreements in which they would agreed to comply with express progress milestones. Federal incentives funds are made available based upon the condition of achieving those milestones.

As written in the Plan, the incentives program applies to a wide variety of infrastructure asset classes, including surface transportation, passenger rail, ports, and water resources, among others.

The evaluation process related to the incentives program focuses upon a wealth of different criteria. Those criteria include the dollar value of the project, the likelihood that there will be long-term non-Federal revenue to fund the investment, the likelihood that non-Federal revenue will be able to pay for operations, maintenance, and rehabilitation, how project delivery approaches would be updated to increase efficiency, the project’s improvement of new technologies, and how the project will spur economic and social returns.
The incentive grants that would be paid as a result of the project would be limited to 20 percent of new revenue or less. The Plan also seeks to ensure that the grants are relatively diffuse as no State would be allowed to receive more than ten percent of all available grants.

If an agreement is entered into and the milestones are not achieved after two years, the agreement would be voided unless the lead Federal agency determines that good cause exists to renew the agreement for up to one year. If an agreement is voided, any funds will be re-awarded through a new application process.

In focusing on rural infrastructure development, the Plan incentivizes States to “partner with local and private investments for completion and operation of rural infrastructure projects.” The proposed Rural Infrastructure Program includes the goal of working to enhance regional connectivity through public and private rural projects.

The Plan also includes a Transformative Projects Program that would provide Federal funding to ambitious, innovative, and transformative infrastructure projects that are likely to be commercially viable yet include risk characteristics that deter private sector investment.

One idea that has been met with enthusiasm in a variety of sectors is asset recycling. The incentive program, described above, has certain components that are similar to asset recycling. Asset recycling functions by allowing a governmental body to lease or concession an existing infrastructure asset to a private company while the government in turn uses the proceeds from that transaction to invest in other infrastructure projects. Although not specifically included in the Plan, asset recycling could be utilized as one means of raising new revenue to qualify for the incentive program. Furthermore, some predict that the federal government could set up a dedicated pool of funds that could be offered to state and local governments as monetary bonuses, or incentives, for engaging in asset recycling. In addition to permitting asset recycling to be a source of funds to apply for the incentive grant program, the Plan proposes to help facilitate more asset recycling transactions by proposing a change in an existing federal rule that requires investors who enter into concessions for existing public infrastructure assets to repay all of their existing tax-exempt debt. The Plan proposes that tax-exempt debt be allowed to remain outstanding in these circumstances. This change would eliminate the effective discrimination that exists against concessions of existing public assets through the requirement that they must be financing through higher-cost taxable financing as opposed to being able to continue to utilize tax-exempt financing that otherwise generally applies to public assets.

Across the Pacific, Australia has had success with asset recycling and Australian officials, including the current Australian Ambassador to the United States, Joe Hockey, who originated the Australian asset recycling program, have advocated that it be implemented in the United States. The Australian government launched a $4 billion asset-recycling fund that paid Australian state and local governments that engaged in asset recycling 15% of the value of the asset that was subject to a concession.

The Plan also seeks to make major updates to the way infrastructure projects are financed. For one, the capacity of Private Activity Bonds (a type of tax-exempt bond commonly
used in P3 projects) would be increased by $6 billion. Furthermore, $14 billion would be used for the expansion of existing credit programs to address a broader range of infrastructure needs. A major aspect of the proposed increase of funds is the broadening of what types of projects are eligible to receive the funds. Notably, the eligibility to use Private Activity Bonds would be broadened so as to allow for greater federal leverage and more efficient infrastructure improvements. In discussing the broadened eligibility of Private Activity Bonds, the Plan states that the revised parameters would allow “longer-term private leases and concession arrangements for projects financed with Public Activity Bonds.” State volume caps and transportation volume caps on Public Activity Bonds would also be removed so as to ensure the bonds are available for future projects.

The Plan also proposes the disposition of federal real property assets. The Plan contemplates that some assets of real property the federal government owns could be more appropriately owned by state, local, or private entities. The Plan includes a list of specific assets that could be divested. Altogether, the plan aims to make the process by which federal property can be divested more straightforward.

As mentioned previously, the Plan also seeks to encourage and incentivize alternative project delivery in transportation infrastructure, including through “private investment.” The majority of the Plan’s discussion in this area centers around the ability of States to engage in alternative project delivery and management and encouraging States to develop delivery mechanisms that focus not only on construction but on long-term operations and maintenance, which is a hallmark of the P3 approach. This section of the Plan focuses on highway, transit, rail, and airport projects (notably including a number of changes that are intended to facilitate expansion of the Airport Privatization Pilot Program, which involves the concession or privatization of existing United States airports).

In its treatment of water infrastructure, the Plan seeks to allow the Clean Water Revolving Fund to provide financial assistance to privately owned public-purpose treatment projects. Additionally, the Plan seeks to add flexibility to water infrastructure projects that have minimal federal involvement. The Plan also seeks to minimize the differences between public and private projects by applying the same environmental standards to both. The Plan also proposes allowing the Secretary of the Army to execute agreements with private entities to use government funds for the construction, repair, or rehabilitation of inland waterways. Additionally, the Plan considers allowing governmental entities and third parties to collect user fees under the Water Resources Reform and Development Act. The length of time that the U.S. Army Corps of Engineers could enter into contracts would be extended. Also, hydropower facilities would be allowed to operate commercially. All of these changes would help facilitate additional private investment in, including P3 projects related to, water and wastewater infrastructure in the United States.

One of the areas in which the Plan is supportive of, and complementarily to, P3 projects is the improvement of infrastructure permitting. The Plan’s proposed permitting modifications would create an expedited structure for environmental reviews, delegate decision-making to States while coordinating State and Federal reviews, and authorize pilot programs that allow innovative approaches to environmental reviews. The Plan aims to do this in several ways.
One, is by creating a deadline of 21 months to complete environmental reviews. Another is by simplifying environmental reviews so that one agency is reviewing one document. Several others are to classify which alternatives are viable, streamline regulatory processes, and eliminate redundancies in EPA reviews. The Plan also seeks to reduce the scope of agency reviews and reduce duplications between Federal agency actions. The Plan proposes to allow design-build contractors to conduct final design activities and acquire rail rights-of-way before the NEPA process is complete. There are also plans to shorten the permitting process by removing unnecessary documents and removing duplication in the review process by eliminating certain review teams. The Plan also allows Federal agencies to streamline their own procedures while creating incentives for enhanced mitigation. Notably, the Plan also authorizes Federal agencies to accept funding from non-Federal entities to support environmental and permitting reviews. Overall, the Plan seeks to accelerate the time under which environmental reviews are performed in order to expedite the permitting process. Additionally, the Plan seeks to reduce inefficiencies on the government’s side and uncertainty on the developer’s side while increasing the scope of projects that can be developed.

The Plan also seeks to entrust environmental reviews and permitting procedures to the States in order to reduce duplication and streamline existing procedures. The Plan also contemplates creating pilot programs to experiment with new ways to address environmental impacts while delivering projects in a predictable and timely way. Additionally, the Plan seeks to reform the judicial review standards for environmental reviews. Lastly, the Plan contains numerous workforce development and workforce empowerment initiatives.

In its review of the Plan, S&P Global noted that new ideas about funding infrastructure investment could lead to innovative solutions and private investment. As mentioned previously, the Plan’s incentives program seeks to reward State and local governments for thinking outside the box and developing novel methods of infrastructure investment and project delivery. Although not every state or locality will be able to meet the higher investment that is expected of them under the Plan, S&P projects that those that do will include those that are looking for creative solutions to projects that include collaborating with the private sector and embracing new revenue models such as tolling. As governments will need to consider user paying models to raise funds, S&P reasons that governments will become more open to participating in P3s.

S&P also characterizes the plan as having a “clear objective to leverage the private sector.” As mentioned previously, even though the Plan does not explicitly mention the use of private capital, it “clearly intends to stimulate P3s and potentially encourage outright privatization.” Many of the details of the plan described earlier (for example, the expansion of Private Activity Bonds) are cited as intending to have this effect.

Despite the apparent bright future for P3 projects in America, it is crucial to remember that the infrastructure Plan is just that, a plan. In fact, publication The Hill has characterized the Plan as “all but dead in Congress.” According to The Hill, the major stumbling block in the Plan was the need to raise additional funding; the publication predicts any positive movement is unlikely until after the midterm elections.
Even though it appears the Trump Administration’s Plan won’t be enacted into law in 2018, there is still talk about a comprehensive infrastructure investment plan in Congress. In late July 2018, Congressman Bill Shuster, the Republican chairman of the House Transportation and Infrastructure Committee, released his own draft of an infrastructure plan. Congressman Shuster’s plan offers similar concepts as the Trump Administration’s plan (as will be discussed below) and promises to shape the infrastructure debate going forward.

Chairman Shuster proposes reforming the Highway Trust Fund to prevent it from going insolvent by 2020 through the appointment of a committee of industry experts who will make recommendations related to future highway funding.

The proposed bill also creates a pilot program that would examine the feasibility of replacing current Highway Trust Fund user fees with a per-mile user fee. The proposal aims to create a national volunteer pilot-program that would examine whether existing user fees on diesel and gasoline could be replaced with a per-mile user fee. Volunteers could be owners of either passenger or commercial vehicles and the program would be administered by the Transportation and Treasury Departments. Additionally, the proposal aims to increase the number of transportation system users who contribute to the Highway Trust Fund. In the meantime, funds will be raised through a 15-cent-per-gallon tax on gasoline and a 20-cent-per-gallon tax on diesel before those taxes are eventually eliminated. Increases would be phased in over three years and would be subject to inflation. The bill calls for similar taxes on alternative fuels.

In a departure from the Trump Administration’s focus on decreasing federal investment and shifting increased responding on the funding of infrastructure to state and local governments, Chairman Shuster’s proposal “increases federal investment in our Nation’s infrastructure. . . [i]t provides for direct federal investment in a broad array of transportation projects, including projects that use new innovations and technologies to transform the way we move goods and people.”

Conversely, in a manner similar to the Trump Administration’s Plan, Chairman Shuster advocates measures that are “designed to remove barriers to private investment and encourage the private sector to participate in the effort to rebuild our Nation’s infrastructure. . .”

The proposed bill seeks to implement a dedicated asset recycling program through the authorization of “incentive grants to encourage public entities to lease their infrastructure to the private sector and then use both the funding from the lease and incentive grant to improve other public infrastructure.” The usage of incentive grants would be limited to improvements to transportation infrastructure.

The Chairman’s proposal also directs the General Services Administration to “carry out a pilot program to complete 3 to 5 building projects as public private partnerships consistent with Office of Management and Budget scoring rules and requires the GSA to conduct a review and evaluation of projects executed under the pilot program.” The goal of this program is to examine how private dollars can be used to build and rehabilitate Federal buildings.
While neither the Trump Administration’s Plan nor Chairman Shuster’s proposal is likely to be enacted into law in its entirety in the near future, both policy documents are significant in their own respect. The Plan lays out the current Administration’s policy vision related to federal policy on United States infrastructure. Elements of the Plan are expected to influence the Administration’s policy decisions in upcoming years, including being reflected in decisions related to annual budgets, rulemakings, and executive orders. While the entirety of the Plan may not become law, certain components of the Plan may be enacted either through executive or legislative action. At the same time, Chairman Shuster’s plan lays out a vision for transportation funding and financing that may influence future legislative action—and, to the extent it overlaps with the Administration’s Plan—may reflect the framework of legislation that could garner both executive branch and legislative branch support. Together, the Administration’s Plan and Chairman Shuster’s proposal signal a direction toward increased private investment—and more P3s—in United States infrastructure.

V. Conclusion

While the relative growth of the P3 market in the United States in light of the significant infrastructure needs of the country is a subject open to debate, it is undeniable that P3 delivery methods are here to stay and will only become more prevalent—in projects of different sizes, among different asset classes and across different jurisdictions. As described herein, P3 delivery methods involve unique commercial and legal issues both for construction contractors and their lawyers. This paper has attempted to make the construction lawyer better equipped to advise on P3 transactions by setting out some of the key differences in transaction structures, applicable laws, surety bond arrangements and dispute resolution mechanisms between P3 and traditional methods of procurement, as well as by providing lessons learned from a uniquely challenged P3 and an overview of current federal policy proposals on the use of P3s and private investment to meet the daunting gap between the infrastructure needs of the United States and available federal, state, and local funds.
1 The author wishes to thank Jacob English, a 2018 Mayer Brown LLP summer associate, for his assistance in the writing of this paper.


3 Id.


6 Circo, supra note 5, at 168.

7 Id. at 168-69.

8 PAKKALA, supra note 5, at 11.

9 Id.

10 Circo, supra note 5, at 171.


12 Circo, supra note 5, at 171; see also GEORGE LEFCOE, THOMPSON ON REAL PROPERTY, THOMAS EDITIONS § 97.04(a)(4) (noting that “the design-build format has been thought to work best for projects that are easy and straightforward—a standard type of building”).

13 Id.

14 Id.


16 Id.

17 Id.


20 Id.


22 U.S. DEPARTMENT OF TRANSPORTATION, supra note 100, at 29 (noting that the Act allows for exceptions when the contracting officer makes a written determination, supported with specific findings, that a payment bond in that amount is impractical” and asserting that this exception “recognizes that the surety market places limits on total bonding available to each contractor, increases the pool of contractors interested in competing for the project, and permits the contracting officer to tailor the financial security requirement for larger projects based on an assessment of the agency’s potential maximum exposure in the event of default, which is generally much smaller than 100 percent of the contract price”).


24 U.S. DEPARTMENT OF TRANSPORTATION, supra note 100, at 29.


29 Id.
See Horsnail and Smith, supra note 27 at 39.

Id.

See Horsnail and Smith, supra note 27 at 40.

Id.

See Horsnail and Smith, supra note 27 at 40.

Id.

See Horsnail and Smith, supra note 27 at 39-40.

Id.

Hereinafter, DRB.


Id. at 55.

Id. at 57.

Id. at 58.

Id.

See Dettman and Scott, supra note 48 at 58.

Id.

Id.

Id. at 59.

Id.

Id.

See Dettman and Scott, supra note 48 at 64.

Id. at 67.

Id.

Id.

Id. at 68.

See Dettman and Scott, supra note 48 at 75.

Id. at 68.

Id.

Id. at 69.

Id.

See Dettman and Scott, supra note 48 at 73-74.

Id. at 74.

Id.

Id. at 75.


Id.

Id.

Id.

See Lessons Learned, supra note 73 at 3.

Id.

Id.

Id.

Id. at 4.
83 Id.
84 See Lessons Learned, supra note 73 at 4.
85 Id.
86 Id. at 6.
87 Id.
88 Id.
89 See Lessons Learned, supra note 73 at 6.
90 Id. at 6-7.
91 Id. at 7.
92 Id.
93 Id.
94 See Lessons Learned, supra note 73 at 7.
95 Id.
96 Id. at 7-8.
97 Id.
98 See Lessons Learned, supra note 73 at 8.
99 Id.
100 Id.
101 Id.
102 Id.
103 Id.
104 See Lessons Learned, supra note 73 at 8.
105 Id.
106 Id. at 8-9.
108 Id. at 24.
109 Id. at 24-25.
111 Id.
112 Id.
113 Id.
114 See A Legislative Outline, supra note 106 at 3.
115 Id.
116 Id.
117 Id.
118 Id.
119 See A Legislative Outline, supra note 106 at 3.
120 Id. at 4.
121 Id. at 5.
122 Id. at 5.
123 Id. at 5.
124 See A Legislative Outline, supra note 106 at 5.
125 Id. at 5.
126 Id. at 6.
127 Id. at 8.
129 Id.
130 Id.
131 Id.
132 Id.
133 See Should America Sell, supra note 127.
134 Id.
See A Legislative Outline, supra note 106 at 10.

Id.

Id. at 10-11.

Id. at 13.

Id. at 14.

Id.

Id. at 17.

See A Legislative Outline, supra note 106 at 19.

Id.

Id. at 20.

Id. at 26.

Id. at 27.

See A Legislative Outline, supra note 106 at 27.

Id. at 28.

Id. at 28-29.

Id. at 29.

See A Legislative Outline, supra note 106 at 29-30.

Id. at 30.

Id. at 35.

Id.

Id.

See A Legislative Outline, supra note 106 at 35-36

Id. at 36-37.

Id. at 37-38.

Id. at 38.

Id. at 39.

See A Legislative Outline, supra note 106 at 39.

Id. at 40.

Id. at 41.

Id. at 47-48.

Id. at 48-49.

See A Legislative Outline, supra note 106 at 49-50.

Id. at 51-53.


Id. at 2.

Id. at 3.

Id. at 3.

Id. at 3.

See A Substantive Shift, supra note 170 at 3-4.

Id. at 4.


Id.


See THE HILL, supra note 179; Chairman Shuster’s Vision Statement: Infrastructure Discussion Draft, TRANSPORT.HOUSE.GOV, 5-9446 at 1.

See Vision Statement, supra note 180 at 2; Discussion Draft Section by Section, TRANSPORT.HOUSE.GOV, 5-9446 at 1.

Id.

Id.
See THE HILL, supra note 179.
See Vision Statement, supra note 180 at 2.
See Vision Statement, supra note 180 at 3.
See Vision Statement, supra note 180 at 3.
See Section by Section, supra note 181 at 2.
Id. at 4.
Id.