Comprehensive Development Agreements in Texas

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Overview

- Conventional Project Delivery: Why Change?
- Types of CDAs
- Specific CDA Issues
Conventional Project Delivery: Design-Bid-Build

• All projects are delivered through public-private partnerships (“PPPs”), just a question of degree

• In Texas, PPPs are called comprehensive development agreements (“CDAs”)

• In Texas and rest of U.S., most highway projects are delivered using the Design-Bid-Build (“DBB”) model

• Public owner
  • Designs project to 100% PS&E
  • Achieves environmental clearance
  • Breaks project up into biddable scopes
  • Pays invoices out of available tax revenues and/or bond proceeds
Conventional Project Delivery: Design-Bid-Build

• Operates and maintains project itself or through separately procured contractors
• Provides design oversight and construction management
• Keeps integration, traditional construction, long term performance and revenue risks

• Private Parties
  • Design the project and perform construction under standard construction contracts and specifications
  • Have conventional rights to claims and change orders

• Alternatives to DBB often require special state legislation and, if federally funded, may require exemptions from federal law (e.g. SEP 14, SEP 15)
Conventional Project Delivery: Why Change?

• DBB works well for the greater percentage of highway development, but there are situations in which PPPs can offer outcomes not available otherwise
  • Capture private sector innovation early in project development
  •Accelerate project delivery
  • Fix costs/completion date early in design phase
  • Encourage lifecycle cost efficiencies and quality facility performance over time
  • Shift risks and reduce claims that would be the government’s responsibility under DBB
Conventional Project Delivery: Why Change?

- Beyond asset creation and efficiency, PPPs can offer more upfront capital formation than muni revenue bonds
  - Tax-exempt financing has more conservative debt coverage ratios than private financing
  - Investor classes are different, offering different risk appetites
  - Private investors are willing to take more risk of toll revenues underperforming
  - With Congressional pilot program, private financing can access tax-exempt borrowing rates
  - Accelerated depreciation creates significant value for private equity that public sector cannot realize
Types of CDAs

• Design-Build-Maintain
• Toll Concession
• Availability Payment Contract
• Pre-Development Agreement
Types of CDAs: Design-Build-Maintain

• Suitable when project is:
  • Close to environmental clearance
  • Sufficiently designed to permit developer to guarantee price and completion date
  • Not 100% designed, to permit developer innovation

• Public Owner
  • Performs conceptual/preliminary design
  • Achieves environmental clearance
  • Procures contractor on basis of “best value” (hard bid and technical factors)
  • Pays all invoices out of available tax revenues and/or bond proceeds
  • Liable for more limited claims and change orders than DBB
  • Oversees design, construction and maintenance
  • Keeps long term revenue risk
  • Shares long term performance risk
Types of CDAs: Design-Build-Maintain

• Developer
  • Completes project
  • Assumes integration and other development risks conventionally retained by public agencies
  • Guarantees price and completion, with limited rights to claims and change orders
  • Assumes operating/maintenance responsibilities for limited period of years (e.g. 15)
  • Offers predictable near-mid term capital maintenance costs

• Examples
  • Utah DOT – I-15
  • New Jersey Transit – Hudson-Bergen LRT
  • Louisiana DOTD – Audubon Bridge
  • TxDOT – SH 130, Segments 1-4
  • CTRMA – SH 183A
  • TxDOT – DFW Connector
Types of CDAs: Toll Concession

• Suitable when project
  • Has same characteristics as DBM, plus
  • When goals are to
    • Raise more capital from future project revenues and/or
    • Transfer risk of revenue under performance and/or
    • Seek longer term certainty of asset maintenance

• Public Owner
  • Same as DBM, except:
    • Imposes performance requirements rather than regulation of means and methods
    • Contributes no or limited tax revenues to project costs
    • Liable for even fewer claims and change orders than DBM
    • Decides on toll rate setting mechanism over contract life
    • Relieved of all or most project revenue risk
    • Receives revenue share as when benchmarks met
Types of CDAs: Toll Concession

- Developer
  - Same as DBM, plus:
    - Assumes enhanced lifecycle performance risks
    - Collects tolls in accordance with rate-setting mechanism
    - Pays excess toll revenues to public owner
    - Hands project back in pre-agreed condition
    - Receives “tax ownership” and therefore depreciation tax benefits (increases value of project)
Types of CDAs: Toll Concession

- Examples
  - California DOT – SR 125, SR 91
  - Virginia DOT – Dulles Greenway
  - TxDOT – SH 130, Segments 5 and 6
  - TxDOT – SH 121 (Cintra)
  - TxDOT – I-635
  - TxDOT – SH 161
Types of CDAs: Availability Payment Contract

• Widely used internationally, although not yet in Texas

• Same as Toll Concessions, except:
  • Public Owner
    • Retains all project revenues, if any, and related risks
    • Pays private party based upon project availability and performance over extended period
  • Private Party
    • Assumes concession-type development and performance risks, sometimes even usage risk, but not collection of tolls, cost of collection or total revenue collected

• Examples
  • Florida DOT – Port of Miami Tunnel
  • British Columbia MOT – Sea to Sky Highway
Types of CDAs: Pre-Development Agreements

• Suitable when
  • Project not yet completely defined
  • Financial feasibility not yet determined, but preliminarily has good potential
  • Public owner seeks private sector innovation in defining and accelerating an optimally feasible project
• Public owner procures Developer on basis of “best development plan”
Types of CDAs: Pre-Development Agreements

• Awards contract with two phases:
  • Initial phase to determine feasibility
  • Implementation phase

• During initial phase:
  • Public and private partners “co-invest” in pre-development activities
  • Public owner retains complete control over environmental clearance process, with Developer payment/performance of technical studies
Types of CDAs: 
Pre-Development Agreements

• If project proves feasible, Developer has right of first negotiation for agreement covering implementation phase

• Implementation phase agreements can take form of any other three CDA models
  • Design-Build-Maintain
  • Toll Concession
  • Availability Payment Contract
Types of CDAs: Pre-Development Agreements

• While rare internationally, widely used in U.S.

• Examples
  • California DOT – SR 125, SR 91
  • Virginia DOT – I-95/395 HOT Lanes
  • Virginia DRPT – Dulles Rail Extension
  • Oregon DOT – I-205 South Corridor
  • Washington State DOT – Tacoma Narrows Bridges
  • Georgia DOT – Northwest Corridor; GA 400 Crossroads
Types of CDAs: Pre-Development Agreements

• In Texas, TTC-35 CDA is example

• Initial Phase
  • TxDOT controls NEPA process
  • Developer works with TxDOT and other stakeholders to prepare Master Development Plan

• TxDOT reserves all decision-making on which projects to develop, means of financing and methods of project delivery

• TxDOT granted Developer right of first negotiation for up to $400 million in near term facilities

• Satisfied by award of SH 130/Segments 5 and 6
Specific CDA Issues

- Project Ownership
- Contract Duration
- Non-Compete Clauses
- Termination Compensation
Specific CDA Issues: Project Ownership

• A public entity should **always** be owner of project, regardless of delivery option

• Under toll concession or availability contract, public sponsor may transfer “tax ownership” to a private entity in order to create federal depreciation tax benefits
  
  • Certain improvements qualify for accelerated depreciation if lease exceeds useful life of asset
  
  • Other expenses amortized on a straight-line basis over term of lease
  
  • Public owner can “claw back” much of depreciation benefits through competitive procurement

• Practical effect is to significantly reduce project costs without additional tolls or tax monies
Specific CDA Issues: Contract Duration

- **Design-Build-Maintain**
  - Time necessary to design and build project **plus**
  - Capital maintenance agreement of up to 15 years to act as warranty and encourage life cycle efficiencies

- **Toll Concessions**
  - Private sector obligations for longer term performance outcomes and O&M costs
  - Long enough to create depreciable asset (useful life)
  - Maximize capital formation (longer term = more capital = enhanced project feasibility)
    - The lower the project’s financed capital costs and the higher the potential revenues, the shorter the contract duration
    - Conversely, the higher the project’s financed costs and lower the potential revenues, the longer the contract duration
Specific CDA Issues: Contract Duration

• Availability Payment Concessions
  • Same motivations as toll concessions, except
  • Capital formation as driver replaced by availability of government revenues for payment

• Pre-Development Agreements
  • Pre-implementation phase depends on achievement of milestones and deadlines to reach financial close
  • Implementation phase depends upon nature of negotiated agreement
Specific CDA Issues: Non-Compete Clauses

• CDAs Seek Balanced Approach to Unplanned Facilities
  • Public Sector Need – right to build other projects over time to address traffic safety and system capacity issues
  • Private Sector Need – protection of the originally expected revenue stream

• Often Referred to Case Study: 16 Year Old SR 91 Provision
  • Contract prohibited operation of competing facilities
  • Narrow exceptions
  • Result: Private partner had, and exercised, legal right to enjoin expansion of free lanes on SR 91
Specific CDA Issues: Non-Compete Clauses

• Lessons Learned
  • No right to enjoin, with public sector free to build whatever it wants
  • Expand exemptions
  • Sole remedy is $ to cover proven net revenue impact
  • In some circumstances, even this limited economic remedy may not be necessary
Specific CDA Issues: Non-Compete Clauses

• Both the SH 121 CDA (Cintra) and SH 130 Segments 5&6 CDA are already largely in conformity with SB 792 and permit without compensation to Developer:
  • Improvements included in planning documents (e.g. STIP, UTP, MPO plans)
  • Anything more than specified miles from project
  • Improved safety, maintenance or operational improvements
  • HOV lanes
  • Environmental agency required work
  • ITS improvements
Specific CDA Issues: Non-Compete Clauses

• In the event TxDOT desires to build future facilities not planned at time CDA signed:
  • Free to build and operate
  • No compensation unless developer can prove negative economic impact
  • In that narrow circumstance, compensation reduced by positive, cumulative effect on project revenues TxDOT has created from other unplanned facilities
  • As used now, more correctly called Unplanned Revenue Impacting Facilities because competing facilities could have positive or negative impacts on project revenue
Specific CDA Issues: Non-Compete Clauses

- Use of provisions outside U.S. varies
  - Legal regimes may include restrictions in statute or constitution, rather than concession
  - Physical impossibility frequently obvious to investors
  - Lengthy history of governmental respect for concession rights creates market comfort
Specific CDA Issues: Termination Compensation

• Pre-Development Agreements and Design-Build-Maintain
  • Termination available for many reasons
  • No need to exercise maintenance option
  • Only limited compensation for buy-back
Specific CDA Issues: Termination Compensation

• Toll Concessions
  • Termination for cause: little or no exposure to compensation
  • Termination for convenience
    • TxDOT may terminate for any reason at any time
    • Special provisions define compensation requirement
    • Will conform to SB 792
Specific CDA Issues: Termination Compensation

• Despite press to the contrary and 16 year old provisions, buyout worked well in SR 91
  • Provision required compensation as if a condemnation (i.e.; fair market value)
  • FY 2002 – Operating Revenue = $27.2 million/yr. on 8.7 million vehicles.
  • Government agency paid $207.5 million
  • FY 2006 – Operating Revenue = $44.231 million/yr. on 14.3 million vehicles.
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