# Public-Private Partnerships in North Carolina

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Mary Nash Rusher, Esq.
Hunton & Williams LLP
421 Fayetteville Street
Suite 1400
Raleigh, NC 27601
919-899-3066
mnrusher@hunton.com

# What does “PPP” mean?

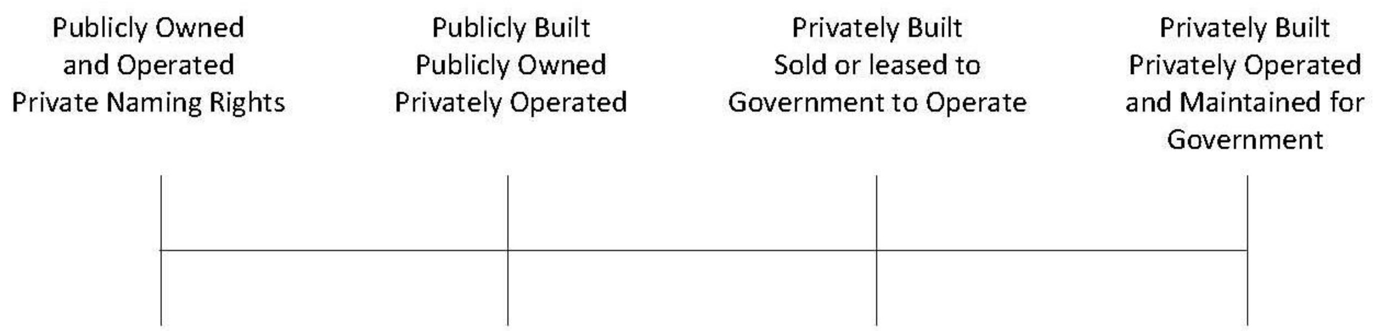
- PPP Refers to a wide range of relationships between the public and the private sector
- Can refer to relationships that work both ways:
  - Public sector provides support, financing, incentives for private development

    or

  - Private sector develops, builds, finances, and/or operates projects in conjunction with the public sector that would ordinarily be undertaken by the public body
  - Could be as little private involvement as naming rights or as much as complete ownership and operation

# What does “PPP” mean?
(cont’d)

- Relationships relating to public enterprises or assets fall along a continuum of ownership and control between government and private sector




- Can include different levels of involvement for public and private sectors
- Different levels of involvement/ownership can come at different times in life of asset

# What does "PPP" mean?

(cont'd)

- Key question in understanding nature of relationship between public and private entities
  - Who will build it?
  - Who will own it?
  - Who will operate it?
  - Who will maintain it?
  - Who will finance it?
  - Who will receive "profit" (e.g. excess revenue, if any) from it?
  - Can private sector can deliver reliable services faster and/or at less cost to the public and make a profit at the same time?

# Benefits and Hurdles for PPP

**Benefits:**

- **Potential to transfer construction , timeline, financing risk to private sector**
- **Potential to reduce overall project costs and compress timeline; take advantage of experienced construction team; move away from low bid**
- **Project can benefit from tax benefits (historic, New Market, depreciation, etc.)**

**Pitfalls:**

- **Private sector expects a market return**
- **High transaction costs**
- **Private financing more expensive**
- **Concerns about public assets in private hands**

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# Use of PPP Structure in North Carolina

- PPPs in financing and development of private assets or public assets for private projects (e.g. infrastructure for private development)
  - Incentives
  - IDB's and Exempt Facility Bonds
  - Tax Increment Financing (TIFs)
  - Assessments and special assessment district financings
  - Hybrid arrangements (e.g., "synthetic" TIFs)
- PPPs in development and operation of revenue generating assets
  - Water and sewer systems
  - Solid waste disposal systems
  - Toll roads and bridges

# Use of PPP Structure in North Carolina (cont'd)

- PPPs in development and operation of public assets
  - Jails
  - Public parking decks
  - Convention Center/Hotel
  - Schools
  - Stadiums
- PPPs in support of private development
  - Roads and sidewalks
  - Water/Sewer extensions
  - Parking Decks

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# Issues to Consider

- Constitutional prohibition against lending public credit to private party (N.C. Constitution, Article V § 3)
- Public bidding laws relating to construction of public assets (N.C.G.S. Ch. 143, Art. 8)
  - Often requires statutory exception (for example, there are specific exceptions in legislation for TIFs and Special Assessment District Projects and for NC Turnpike Authority)
- Cost of borrowing
  - Taxable rates for the private sector (unless tax exempt financing available) versus tax exempt rates for a governmental entity
  - Credit quality of the developer versus government
- Effect of private involvement on ability of public entity to get tax-exempt financing
- Value to developer of ability to take depreciation of asset

# PPP for Private Assets

- Various tools state and local governments can use to encourage investment and economic development
  - Incentives
    - <u>State</u>: JDIG Grants
      One North Carolina Fund
      Work force training at community colleges
      Various tax credits and tax breaks
      Research and Development tax credit
      North Carolina Ports tax credit
      Sales tax reduction on manufacturing machinery
    - <u>Local</u>: Economic development grants – Cash grants financed by property taxes
      Construction of infrastructure for industry
      Low cost buildings, low cost leases of locally owned buildings

# Tax-Exempt Private Activity Bonds

"Public" Financing through Private Activity Bonds

-- County industrial facility and pollution control financing authority or the North Carolina Capital Facilities Finance Agency issues bonds at a tax-exempt rate, lends the proceeds to a private company for certain purposes authorized by Internal Revenue Code and North Carolina law

- Credit of State and county <u>not</u> pledged
- Allows private company to borrow at lower tax-exempt interest rate
- Interest on income from bonds exempt from federal and North Carolina income taxes

# Private Activity Bonds
(cont'd)

– Industrial development bonds:  allows tax exempt financing of manufacturing facilities (up to $10 million);
– Exempt facility bonds:  allows tax exempt financing of specific types of privately owned property
  – Privately owned water service
  – Solid waste disposal
  – Airports
  – Private industry projects at public ports

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# Tax Increment Financing (TIFs):

In 2004 the voters of the State of North Carolina approved an amendment to the North Carolina Constitution to allow for tax increment financing (known as “project development financing” in North Carolina statutes)

- Local governments issue bonds that are repaid from the increase in property taxes that result from the increase in tax value from improved property
- Government designates the development financing district; improvements made, and increased tax revenues collected in, the district

# Tax Increment Financing (TIFs)
(cont'd)

- TIF allowed for a number of types of facilities:
  - airport facilities
  - auditoriums, arenas, stadiums, civic centers
  - art galleries and museums
  - parking facilities
  - sanitary sewer systems
  - storm sewers and flood control facilities
  - water systems
  - public transportation facilities
  - industrial parks
  - community college facilities
  - school facilities
  - low or moderate income housing
  - electric systems, gas systems
  - streets and sidewalks
- Facilities financed with TIF's that are part of a development plan may be constructed by a private company; the public bidding laws do not apply unless the parties elect for them to apply

# Tax Increment Financing (TIFs)
(cont'd)

- Examples in North Carolina:
  - $21,500,000 in financing approved for entertainment complex in Roanoke Rapids
  - $25,000,000 (plus costs of issuance) in public infrastructure financing approved for the mixed use development of a former Brownfield site in the Town of Woodfin (Buncombe County)
    - First series of Woodfin bonds issued 8/2008 ($12,960,000)
  - $95,000,000 in public infrastructure financing approved for Phase I of the North Carolina Research Campus in Kannapolis (No bonds yet offered for sale).

# Special Assessment Financing

- Counties and cities are authorized to make special assessments against benefited property within the county or city for the purpose of financing construction, reconstructions, and renovating certain type of infrastructure as set forth in N.C.G.S. Chapter 153A, Article 9 and 9A (for counties) and Chapter 160A-20, Article 10 and 10A (for cities)
  - Permitted projects are the same as the project that can be financed with TIFs (SB 97, ratified 8/6/09)
  - SB 97 also permits special assessments to finance the installation of distributed generation renewable energy sources or energy efficiency improvements that are permanently fixed to residential, commercial, industrial or other real property
  - Assessments can be pledged to secure revenue bonds or as additional security for TIFs

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# Special Assessment Financing

- Payment for projects can come from variety of financing sources, including GO's, revenue bonds and TIFs
- Assessments paid in annual installments – not to exceed 30 installments; assessments are due on date property taxes are due
- Requires petition signed by owners of 66% of assessed value of all real property to be assessed, public hearing and period (10 days) during which petition can be withdrawn
- If a project funded through assessments is funded 25% or less by GO bonds or a unit's general fund and is to be built by a private party, the public bidding rules do not apply unless the parties elect for them to apply

# PPP for Revenue Producing Infrastructure

## Water and Sewer Systems – Several Models

- Government owns the system, and contracts with private company to operate and maintain the system; IRS rules allow this arrangement (up to 20-year term) even in a system financed with tax-exempt bonds; OR
- Government purchases system previously owned by private operator; OR
- Government sells system to private operator that operates it under N.C. Utility Commission (NCUC) oversight; OR
- Private entity uses tax-exempt financing (exempt facility bonds under IRC § 142(a)(4)) to build and operate private system under NCUC oversight

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# PPP for Solid Waste Disposal Systems

Government contracts with private sector to handle collection and disposal of residential and commercial garbage

- Private companies such as Waste Industries, Republic Services, Waste Management
- Capital investment in private assets can be financed on a tax-exempt basis as solid waste disposal facilities under IRC Section 142(a)(6)
- Another model: Government owns the landfill, but contracts for some or all of the steps in collection and disposal to be done by private company – collection and hauling, transfer stations, recycling
- Other solid waste options in "green" sector: tax credit bonds to finance landfill gas-to-energy projects (with power sold to public utility)

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# Toll Roads

## N.C. Turnpike Authority (NCTA) (NCGS § 136-89.180 et seq.)

- NCTA has the power to construct certain specific highway toll projects, and can issue revenue bonds supported by toll revenues
- NCTA is directed to solicit competitive proposals for developer to be included in the construction of certain turnpike projects
- NCTA permitted to use alternative contracting methods (other than public bidding laws) for construction so long as NCTA documents that it will expedite timing or lower cost or otherwise serve the public interest

# Toll Roads (cont'd)

- NCTA has two projects underway:
  - Triangle Expressway (opened December 2011): financed by the issuance of bonds secured by the future revenues from the toll road and Build America Bonds
    - Design-Build construction process overseen by NCTA and NCDOT
  - Mid-Currituck Bridge: NCTA has entered into a Predevelopment Agreement with the Currituck Development Group, LLC ("CDG")
    - CDG and NCTA will work together to design, construct and finance Mid-Currituck Bridge
    - Arrangement may include operation and maintenance by CDG

# Jails

- State of North Carolina used PPP model to construct 7 jails
  - Legislation permitted the North Carolina Infrastructure Finance Corporation (NCIFC) to enter into construction contracts with private company to construct jails in Alexander, Anson, Scotland, Greene, Bertie, Pamlico and Avery Counties, using prototype design
  - RFP used to choose the private company, setting forth prototype design, but public bidding rules not required
  - Jails were then leased to State of North Carolina under a lease purchase agreement
  - For the early deals, taxable financing used for construction financing; later deals used tax exempt financing

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# PPP for Parking

- Parking Decks
  - Raleigh: Progress Energy building
    - Progress Energy built the parking deck while it was building its headquarters office building; once completed, it sold the deck to the City
    - City issued debt to purchase the deck; Progress retained the right to certain spaces
  - Charlotte: Parking in Metropolitan Midtown Development
    - The City of Charlotte and Mecklenburg County made economic development grants to the Metropolitan Midtown developer to pay a portion of the costs of constructing a parking deck.
    - City and County received no ownership interests
    - Reimbursement payments to the developer equal to tax increment generated over a period of years (10) and subject to a ceiling on aggregate payments.

# Parking (cont'd)

- Charlotte:  Revitalization of Elizabeth Avenue
  - The City of Charlotte agreed to purchase up to 1000 condominium parking spaces in new decks built as part of a revitalization of Elizabeth Avenue.
  - City used COPs debt to purchase spaces but only after:
    - total incremental tax revenue from project area exceeds $25,000,000 and
    - total area incremental revenue exceeds 110% of COPs debt service
  - County funds 1/2 of debt service from its share of incremental tax revenue
  - Upon retirement of COPs debt, City will convey pro rata share of spaces to County
  - Developer has right to buy back the spaces for greater of fair market value or debt payoff amount

# PPP for Conference Center/ Hotel/ Arena/Museums

- Conference Center/Hotel
  - Raleigh:
    - City of Raleigh, Developer and Hotel Owner entered into an agreement pursuant to which the City leased land to the Hotel owner under a Ground Lease; Developer built a full service hotel, which includes a conference center, meeting space and ballroom.
    - Upon substantial completion of the project, the hotel was "condominiumized", so that the hotel became one unit and the conference center a separate unit. The City purchased the conference center unit from the hotel owner, and entered into a long term lease back to the hotel owner of the conference center at a nominal cost.
    - The City borrowed money that was used on a pari passu basis with the private investment to pay costs of developing the hotel and conference center. The city also undertook to provide 200 parking spaces for the hotel and conference center guests.

# Sports Arena

- Sports Arena
  - Charlotte:
    - The City of Charlotte entered into a complex series of agreements with the owner of the NBA Franchise (Bobcats) to finance the construction of a new downtown arena complex
      - Arena is owned by the City
      - Arena is subject to long term lease and operating agreements in favor of the Bobcats
      - Food and beverage revenue is used to service third party debt
      - Bulk of financing provided by City issued COPs

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# Museum Complex

- Charlotte Museum Complex
  - Private Developer, as part of the construction of an office/retail/residential redevelopment of a downtown block agrees to include space for three separate museums and a theater facility
  - City finances the construction costs of the cultural facilities through COPs
  - Components constructed as separate condominium units
  - Upon completion, museums are conveyed to City.
  - Debt Service on COPs provided by
    - incremental taxes from the commercial portion of the development and
    - vehicle rental tax

# PPP for Roads

- Local Road Construction
  - On a least two separate occasions Charlotte has reimbursed developers for the cost of road construction or improvements as a development incentive. Typically, City and Developer agreed on road costs subject to reimbursement. After roads are completed City will begin reimbursement of costs over a period of time (usually 10 years) equal to 45% (but up to 90% in high priority areas) of the tax increment generated by the incentivized private development, but not to exceed previously agreed upon maximums
    - IKEA Boulevard
    - New connector road between Tyvola and Billy Graham Parkway (old Coliseum redevelopment)
    - Project included both public and private funding, public and private construction, and public and private operation
    - Example of “synthetic” TIF

# PPP for Schools

**Public Schools –Statute NCGS §§ 115C-531-532 intended to allow for "PPPs" for schools**

- Statute contemplates that developer/private party will build the school and lease it to school district
- Must be a capital lease (i.e., school district will own the school at the end of the lease for a nominal sum; developer cannot take depreciation)
- Developer must enter construction contract in compliance with public bidding rules; therefore, no true design-build possible
- Iredell, Wake, Cumberland, Mecklenburg, and Rockingham Counties (maybe others) all considered and even started down the road to implement; none could find savings in time or money sufficient to justify

## Schools (cont’d)

### Other possibilities under existing law:

**Developer could get its own financing and build the school and then sell it to the school district/county upon completion**

- Issues:
  - getting school board/county to commit up front to purchase a school two-three years in future
  - developer financing may be more expensive than county financing
  - what assurances does developer have that county will have debt capacity 2-3 years out?
  - how much control can school board have over design and characteristics without triggering public bidding laws?

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# Schools (cont'd)

## Some argue existing statute (NCGS 115C-530) permits a developer to construct a school and lease it to school board

- Allows developer to take depreciation and take advantage of tax credits for "green" aspects of the school
- Fosters innovative use of school property by teaming up with others in the community for use of portions of the school

Concerns:

- Taxable financing based on credit strength of developer not county
- Concerns about school district's ability to control construction, meet department of insurance standards for school building
- Public bidding laws still apply

# Financing

## Other ways to provide financing for public infrastructure

- Infrastructure Bank - Existing
  - Revolving loan fund for specific project
    - DOT – roads (Federal grants)
    - Water project (Federal and state grants)
- Statewide infrastructure banks
  - Various models: generally designed to get funds to less credit worthy local governments in order to assist them in building infrastructure
    - revolving funds; must have initial funding
    - state puts its credit strength behind borrowing
    - state funds debt service reserve fund on appropriation basis
  - Initial funding: pension plans, state appropriations

# For the Future

- Important to focus on what public and private sector hope to accomplish with any PPP proposed – what is the objective?
  - Achieve faster/cheaper construction?
  - Shift or share construction costs/risk?
  - Shift or share operating/maintenance risk?
  - Shift financing risk?
  - Foster economic development in a particular area?
  - Create new funding source?
- Legislation should be drafted with particular objective in mind

# Questions?

**Mary Nash Rusher, Esq.**
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