- Public-Private Partnerships (P3) defined
- University issues and unmet needs
- P3: An alternative delivery method
- Roles of developer
- Financing structures
- Ground lease categories
- Assessing critical factors
- Pros and cons of P3
- CSU policy for real property development
A Public-Private Partnership (PPP) is a contractual agreement between a public agency (federal, state or local) and a private sector entity. Through this agreement, the skills and assets of each sector (public and private) are shared in delivering a service or facility for the use of the general public. In addition to the sharing of resources, each party shares in the risks and rewards potential in the delivery of the service and/or facility.

*Similar set up could also apply in a public-public partnership.

Source: The National Council for Public-Private Partnerships
- Limited debt capacity for certain type of projects
- Additional Facilities
  - Programmatic use (mission-serving)
    - Student development
      - Living and learning program
    - Medical and high tech research
      - Internship program, real world work experience
  - Revenue-generating use
    - Mixed-use development (various components of housings, offices and commercial operations)
University Issues and Unmet Needs

- Lack of construction and operating expertise
  - Example: Arena project
- Need for risk transferring
  - Development, construction, financing, operating
- Limited campus resources
- Need for faster procurement and delivery process
- High development and construction costs
  - Subject to prevailing wage law
Fast delivery method and viable financing alternative for long-term capital projects

Lower development and construction cost

Developer expertise
  - Design, construction, financing and operating

Transfer of risks (from university to other parties)

Preservation of campus debt capacity

Access to capital

Favorable accounting treatment: Off-balance sheet for university
Roles and responsibilities of Developer

**Developer roles:**

- University owned/financed structure: Developer and construction manager
- Project-based structure: Third-party developer, financing arranger and manager
- Equity-based structure: Developer, owner, operator and financier

**Developer responsibilities:**

- Pre-development and development services
- Construction management
- Financial structuring
- Operations and management
- CSU Systemwide Revenue Bonds
- University receives all net project cash flows (unrestricted)
- University controls and oversight: development, construction, ownership and operations
- University bears all risks
  - Development, construction, financing, operating
- General debt obligation: security in other assets
- Lowest cost of capital
- Direct debt and impact on university credit
Financing Structures

University-issued bonds
Financing Structures

Project-based bonds

- Tax-exempt or taxable bond issuance
  - Issued by conduit issuer
  - Higher cost of capital
  - Lower bond rating (non-investment grade)
  - Limited security interest in project-based revenue
  - Non-recourse debt
  - Debt service coverage 1.20x per bond covenant
  - Limitation on additional bond issuance
  - Funded debt service reserve fund
  - Funded capitalized interest fund
Ground lease

- University (lessor) leases project site to non-profit 501(c) 3 organization (lessee)
- Ground rent: fixed annual amount or net cash flow releaseable to lessor after payment of operating expenses, repair and replacement reserve and debt service
- Term of 30-plus years, with improvements and land reverting to university upon lease expiration
- Ground lease unsubordinated to other agreements of lessee
- Funded repair and replacement reserve
- **Non-profit**
  - Serves as borrower and obligor
  - Owner of completed project

- **University**
  - Receives restricted net cash flow via ground rent
  - No ownership; limited to no control and oversight of construction and program operations; some marketing and referral assistance

- **Developer**
  - Serves as developer, construction manager and operator (at university discretion)
  - Earns fee for development and construction mgmt.
Accounting treatment: Off-balance sheet
Credit impact on university
Preservation of university debt capacity
Possible university occupancy guarantee (student housing related)
Limitation on future university project construction
  - Non-competing provision
  - Subject to review and approval by institutional stakeholders (underwriter, banks, rating agencies)
Financing Structures

Project-based bonds (cont.)
Financing Structures
Developer Equity-Based

- University leases land to developer/owner
- University receives annual ground rent, potential excess cash flow participation in performance of project
- Private developer/owner has direct ownership
- Private developer/owner assumes all responsibilities and risks:
  - Financial, operation, maintenance, capital improvements, long-term ownership
- Developer funding: 100% equity or combined equity (25%-50% of total project cost) and debt
Developer return on cost (ROC) through long-term cash flow and project ownership

University benefits:
- No financing for the project
- No guarantees or master lease
- No operational or financial support
- Preservation of university’s debt capacity
- Favorable accounting treatment: Off balance sheet for university
Financing Structures
Developer Equity-Based

University

Ground lease

Developer
(Developer, owner, operator, financier)

$\text{Ground rent}\;$

$\text{Ground rent}\;$
Financing Structures
Developer Built-to-Suit for Purchase

- University leases land to developer
- Private developer assumes all responsibilities and risks: financial, operation, maintenance, capital improvements, ownership
- Private developer takes ownership of completed project and gives university option to purchase
- University secures own financing for purchase
- Debt financing on university balance sheet
- Direct credit impact for university
- Potential benefits for university: Lower project cost, faster delivery and quality construction.
Financing Structures
Developer Built-to-Suit for Purchase

University

Ground lease

Sells completed project

Developer
(Develops, constructs, finances, owns/sells project)
Ground Lease Categories

- Construction and design
  - Scope project
  - Project specifications
  - Target completion dates
  - Penalties/remedies for non-performance

- Management structure
  - Permitted use the facility
  - Target market
  - Parties managing of residential life program, leasing, marketing, billing, maintenance
- Fixed annual rent or net cash flow
- Profit participation (% of net cash flow)
- Lease term (30-plus years)
- Repair and replacement reserves
- Financial support and marketing referral
- Funding mechanism
  - Debt, Equity
- Sale provisions
  - Built to suit project for purchase by university
- Default remedies
- Are CSU’s design and functionality requirements incorporated in the private developer’s plan?
- Does the private developer have the necessary construction, financing and management expertise?
- Is prevailing wage required if the project is located off-campus and not owned by university.
- Is the university committed to long term leasing of its land and foregoing future real property development opportunities?
- Are there any capital improvement expenditures to preserve long-term condition of the building?
How does P3 model compare to University model in terms of financial feasibility, project viability and savings (e.g. lower rental rate to students under student housing project)?

Does the P3 option provide sufficient long-term savings to offset CSU financing advantage and developer profit requirements?

Is there sufficient demand and profitability for a financially feasible P3 project?

Will the project pose a competitive threat to the university’s existing operations (e.g., housing)?
Assessing Critical Factors
Management Control

- Is the university prepared to assume the risks and responsibilities associated with the project if the project is no longer viable?
- Is the university comfortable with not having operational control and oversight of project?
- Is the university fine with non-competing clause and being restricted from adding future projects?
- Will the completed project have any displacement effect on university existing program?
- Is the university required to provide financial and marketing support and student referral?
Assessing Critical Factors
Credit Impact/Debt Capacity

- Will the P3 financing structure result in an off-balance sheet position for the university?
- Will the P3 financing structure preserve debt capacity for the university?
- Will there be any bond covenants limiting additional bond issuance by university?
Pros

- Preservation of debt capacity
- Construction and operating expertise
- Access to capital
- Off-balance sheet for university
- Fast and economical delivery method for capital projects

Cons

- High cost of capital
- Reduced control for university
- Long-term ground lease
- Complexity of deals
- Multi-party roles and responsibilities
- Limitation on future university development
University-Land Development Review Committee (LDRC) discussion on key issues and needs

University conducts preliminary research via Request for Information (RFI) and/or Request For Qualification (RFQ)

University seeks conceptual approval by BOT

Structural development and details

- Selection of development partner(s) (RFQ, RFP)
- Negotiation of terms, financial structure
- CEQA, EIR, Master Plan, Schematics
- LDRC updates

Final approval by BOT
EO 747 applied to:

- Projects with long-term contractual relationships that use/develop campus real property to further educational mission of the campus
- Acquisition of physical assets, income and/or educational benefits for students and faculty
- Third-party development contracts via ground lease

Defines...

- Executive Roles and Responsibilities
- Process for BOT Conceptual approval
- Process for BOT Final approval of Development Plan
President: Responsible for real property development
- How will the project further educational mission?
- Scope of project
- Highest and best use of university property
- Does the project better meet the educational program needs than the current master-planned program use?
- Will project impact or displace a current program use?

Executive Vice Chancellor (EVC)/CFO: Responsible for assisting campus in planning and staff review and analysis prior to BOT action

Chancellor and EVC/CFO: Responsible for determining the applicability of EO 747 to a project
CSU Policy - Real Prop. Development

Process for BOT Conceptual Approval

- CSUCO involvement: Land Development Review Committee (LDRC), Financing & Treasury (F&T) and Capital Planning Development Construction (CPDC)
- University info gathering via RFI/RFQ
- LDRC review:
  - Market demand study, CEQA determination, pro forma, development concepts
- Issuance of specific procedures from Executive Vice Chancellor/CFO regarding a project
- Conceptual BOT approval
- Regular updates to LDRC
- Update of conceptual plan—emphasis on how project furthers the educational mission
- Request for Qualifications (RFQ) and Request for Proposal (RFP)
- Due diligence results and assessment of risks
- Summary of terms and conditions for key agreements
- Multi-year financial plan
- Final BOT approval
CSU Policy for Financing and Debt Management

- Board of Trustees Resolution RFIN 03-02-02 and Executive Order 994
  - information and procedures in connection with financing activities of campuses and auxiliary organizations

Leases—Executive Order 669

- Delegated authority to university president to enter into lease agreement supporting a public/private partnership, subject to approval by CSU Office of the Chancellor
- Prevailing wage
  - Legal determination
  - CSU policy decision
- Impact on CSU SRB program
- P3 option should meet a need that the campus or CSU cannot otherwise provide through established programs
- P3 decisions should align project purpose and structure with university goals
- Avoid impact on CSU credit or debt capacity
- Get Chancellor’s Office involved early and often