

ARNOLD SCHWARZENEGGER
Governor

Department of Alcoholic Beverage Control
Department of Corporations
Department of Financial Institutions
California Highway Patrol
California Housing Finance Agency
Department of Housing & Community Development
Department of Managed Health Care
Department of Motor Vehicles
Board of Pilot Commissioners



DALE E. BONNER
Secretary

Department of Real Estate
Department of Transportation
Office of the Patient Advocate
Office of Real Estate Appraisers
Office of Traffic Safety
California Film Commission
California Office of Tourism
Infrastructure and Economic Development Bank
Public Infrastructure Advisory Commission

BUSINESS, TRANSPORTATION AND HOUSING AGENCY

August 10, 2009

Chairman Alvarado and Commissioners
California Transportation Commission
1120 N Street
Sacramento, California 95814

Re: Policy Guidance for Selection of Public-Private Partnership Projects

Dear Chairman Alvarado and Esteemed Commissioners:

At the June 10, 2009, meeting of the California Transportation Commission,¹ I sounded a note of extreme urgency regarding the State's continuing fiscal crisis and our worsening infrastructure deficit. As you are fully aware, traditional funding and delivery methods cannot keep pace with California's growing demand. With the current fiscal and economic crises, comprehensive solutions remain elusive and California's economic competitiveness is at risk.

Senate Bill 4, which was passed during the Second Extraordinary Session of 2009-2010, authorizes Caltrans and regional transportation agencies (sometimes referred to below as "transportation agencies") to enter into public-private partnership (P3) agreements to secure alternative and additional private financing and achieve more timely and efficient delivery of critical infrastructure. This legislation is vitally important to our ongoing efforts to improve the State's infrastructure and fiscal condition, to create jobs and to accelerate economic development by expediting investments in transportation.

Much progress has been made in implementing the new law. The Business, Transportation and Housing Agency (BTH) and Caltrans have been coordinating with regional transportation agencies, some of which are or soon will be prepared to submit applications to the CTC to proceed with P3 projects under SB 4. In addition, as required by SB 4, BTH has established the Public Infrastructure Advisory Commission (PIAC) to: (1) identify transportation project opportunities throughout the state; (2) research and document similar transportation projects throughout the world to identify and evaluate lessons learned; (3) assemble and make available to Caltrans or regional transportation agencies a library of information, precedent, research, and analysis concerning P3 transactions; (4) advise Caltrans and regional transportation agencies, upon request, regarding P3 suitability and best practices; and (5) provide, upon request, P3 procurement-related services to Caltrans and regional transportation agencies. The PIAC

¹ Hereafter, "CTC" or "Commission."

convened its first meeting on July 29, 2009, and has its second meeting scheduled for September 1, 2009.

To continue this steady progress, we are asking the CTC to act prudently, but expeditiously, in carrying out its important responsibilities under SB 4. Neither Caltrans nor regional transportation agencies may proceed with a P3 project without first securing the CTC's selection of the project. In addition to its "gatekeeper" function, the CTC will: certify the useful life of projects sponsored by Caltrans, adopt the criteria for the final evaluation of proposals for procurements based on qualifications and best value, authorize the extension of tolls and user fees after the expiration of P3 lease agreements that include tolls or user fees, and report annually to the Legislature on the progress of each project and ultimately on the operation of the resulting facility.

During the past 90 days, our respective staffs, Caltrans and other stakeholders have worked in good faith to develop guidelines that explain how the Commission will perform its statutory duties under SB 4. On Friday, July 31, 2009, BTH received a copy of the CTC staff's proposed guidelines (Draft Guidelines) that will be presented to the Commission at its August 12-13, 2009, meeting. Unfortunately, the Draft Guidelines provide for additional substantive requirements beyond those included in SB 4 and introduce new terms and concepts that would likely add unnecessary time, ambiguity, uncertainty and costs to the P3 program and seriously chill competition.

The Draft Guidelines Are Contrary to the Framework Set Forth in SB 4

SB 4 is designed to require the CTC's review of specified matters before the relevant transportation agency, or agencies can exercise their discretion to negotiate and execute the best deal for the public. Yet, the Draft Guidelines would have the Commission withhold its selection of a P3 project pending its review (and implicitly, approval) of a final P3 lease agreement. As a result, public and private parties would be asked to expend millions of taxpayer and private dollars leading up to a procurement, and millions more to complete the procurement process – all before knowing whether the CTC will allow the project to proceed as a P3 project.

In California, history shows that public agencies and prospective investors, who have watched the experience of other states, will simply not participate in a process that requires them to commit all the resources necessary to bid on a project, including months of intensive work and lost opportunity costs, if it is possible that, even after a contract is awarded, the CTC still may decide that the project is not a suitable P3 project.

We are aware of and respect the view of those who say the Legislature, in removing the requirement for legislative approval of final P3 agreements, intended to transfer this authority to the CTC. While reasonable minds can differ on whether the CTC *ought* to have such authority, SB 4 as passed by the Legislature and signed by the Governor included no such authority in the language of the law.

The goal reflected in SB 4 is to remove the potentially disruptive and chilling effect of having P3 agreements subject to approval of *any* third party that would not have the requisite expertise or the benefit of its own expert financial, legal or technical advisers, or that may end up approving or disapproving a final agreement based on factors having little or nothing to do with the contents of the agreement. This is why SB 4 amends the prior law to expressly state that the appropriate transportation agency “shall retain the discretion for executing the final lease agreement.”

In reviewing the experience of other states, we are not aware of a single instance in which a project was disapproved based on individual provisions that appeared only in a final agreement. Rather, decisions to disapprove projects have been based on factors having little or nothing to do with the agreement itself. This is why the Governor pushed for a P3 statute that does not include this element of decisional risk, when the better policy, as clearly articulated in SB 4, provides for a process that includes multiple checks that ensure a full review of all pertinent issues, but then allows the transportation agency to retain the discretion to execute the final agreement after a full and transparent vetting.

This is sound policy because, unlike the laws of other states, SB 4: provides for a substantive review and determination of whether proposed projects should proceed as P3 projects, prescribes many of the most critical contract requirements, and ensures transparency and inclusion through public vetting before the CTC, public hearings, and review by the Legislature and the PIAC. Even in California, the absence of third party approval is not without precedent. The legislation guiding what may be the State’s largest P3 project – the High Speed Rail system – requires legislative or voter approval of the *project*, but does not require any third-party approval of final agreements that may be executed to implement the project. Having approved the project, the Legislature and voters have left to the High Speed Rail Authority the discretion to execute necessary agreements. (See Public Utilities Code sections 185043 and 185036; and see Cal. Attorney General Opinion No. 07-1002, February 7, 2009, at p. 7.) The same is true of the large and complex arrangements that transit agencies and other regional transportation agencies have carried out in California over the last three decades, utilizing federal and local resources for many contractual variants, without CTC or legislative review, but remaining wholly accountable to officials elected and appointed to achieve efficiency and to protect the public interest.

It has been suggested that, in reviewing a final lease agreement as proposed in the Draft Guidelines, the CTC would not be inclined to second guess the details of the agreement, but would instead be making an overall judgment that the final agreement satisfies the requirements of SB 4. If this is the goal, it can be achieved much earlier in the process before a lease agreement is finalized since applications for project selection will include virtually all of the information necessary to make this judgment, including a proposed financial plan. Third party approval is not required because the particulars of these provisions will be available for review and comment by the public, the Legislature, the CTC, and the PIAC – all before the agency that negotiated the final agreement can exercise its discretion to sign or not sign the agreement. Accordingly, there is no good reason to withhold a project selection pending receipt of a final lease agreement and much of the other information required by the Draft Guidelines.

The Draft Guidelines Add Requirements that Are Ambiguous and Difficult to Implement

Under the process set forth in SB 4, the CTC is to select the candidate projects if they are primarily designed to: (a) improve mobility; (b) improve the operation or safety of the affected corridor; (c) provide quantifiable air quality benefits for the region in which the project is located; and (d) address a known forecast demand, as determined by the department or regional transportation agency. (Streets & Highways Code section 143, subds. (h)(3) and (h)(4).)

The Draft Guidelines introduce additional requirements that are ambiguous and difficult, if not impossible, to implement. For example, Sections 2, 3 and 5 add the requirement that the CTC approve a project's financial plan, including the allocation of financial risk and various other financial terms. Section 3 adds the requirement that procedures and criteria to be used to select a contracting entity or lessee be "clear, consistent with statute, and fair to all parties concerned." These terms are inherently subjective, have no grounding in SB 4, and raise substantial questions about the CTC's intended role in determining who is a party sufficiently "concerned" so as to have standing to challenge the "clarity," "consistency," or "fairness" of the procedures or criteria, and in adjudicating any bid protests or other disputes based on such newly established standards and requirements. These are issues outside the CTC's area of expertise and, presumably, are not the focus of its interest.

We are also concerned that the Draft Guidelines include multiple additional steps with long time periods for placing items on the Commission's agenda, which could result in substantial and costly delay. These steps include placing items on the agenda at least 30 days prior to preliminary approval, another 60 days prior to full project approval, and 30 days more for approval of the "supplement" if it deems there is a "material" change in the agreement.

However well-intentioned, the Commission should refrain from using its procedural guidelines to create new substantive requirements or additional hoops and hurdles that overly complicate and extend beyond the process established in SB 4. While we do not understand this to be the Commission's desire or intent, doing so, even inadvertently, would be contrary to the Commission's traditional role and require particular expertise that the Commission does not possess.

The Guidelines Should More Closely Track SB 4

On July 27, 2009, BTH delivered to the Commission and its staff draft guidelines (Suggested Guidelines) that suggest a straightforward process for carrying out the CTC's responsibilities under SB 4 while minimizing undue costs, decisional risk and delay. The Suggested Guidelines propose a clear process the components of which may be taken up separately or together: (a) CTC selection of the project based upon the required statutory criteria, its scope and preliminary financial plan (addressing the sources of funding) before the procuring agency had to make the investment in final procurement documents and lease agreement; (b) CTC adoption of the evaluation criteria for best value and review of substantially complete procurement documents and form of P3 agreement (typically 90-95% final) before the multi-million dollar bid

Chairman Alvarado and Commissioners

August 10, 2009

Page 5

investments are made by both the private and public sectors; and (c) CTC review of any material changes to those documents after bids are in, when the agreement is in final form. In this way, the public and private partners would be assured by the fact that the post-bid approval would be limited to those factors that would have changed the original CTC decision. This approach is more consistent with SB 4, which is carefully crafted to allow for transparency and inclusion in the process while avoiding the structural features that have undermined the success of prior P3 legislation here and in other states. Further, the Suggested Guidelines propose what will be the most open and transparent process for reviewing P3 transactions, indeed any form of transportation development agreement, in the United States.

As the Commission considers these or any other draft guidelines for this program, I would ask that you bear in mind the urgency of the matter. Any undue delay in the adoption of appropriate guidelines will seriously compromise the implementation of this important program, putting at risk our ability to move forward with projects that could otherwise provide significant economic and other public benefits in the very near future.

Please know that we very much appreciate the Commission's continued leadership and its willingness to take the important steps necessary to help alleviate if not correct the long-term and systemic under-investment in our transportation infrastructure.

Sincerely,



DALE E. BONNER

Secretary

cc: Jim Bourgart, BTH Deputy Secretary for Transportation and Infrastructure
Randall Iwasaki, Director, Department of Transportation
Bimla Rhinehart, Executive Director, California Transportation Commission

July 24, 2009

CALIFORNIA TRANSPORTATION COMMISSION

DRAFT POLICY GUIDANCE APPROVAL OF PUBLIC PRIVATE PARTNERSHIP PROJECTS

July 2009

Section 143 of the California Streets and Highways Code, as amended by Chapter 2 of the Statutes of 2009 (Senate Bill 4, Second Extraordinary Session), authorizes the California Department of Transportation and regional transportation agencies to enter into comprehensive development lease agreements with public or private entities for transportation projects, commonly known as public private partnership (P3) agreements. Section 143 further provides that P3 projects and associated agreements proposed by the Department or a regional transportation agency shall be submitted to the California Transportation Commission, and that the Commission shall select and approve the projects before the Department or regional transportation agency proceeds with the P3 procurement process. For Department projects, the Commission shall also certify the Department's determination of the useful life of the project in establishing the P3 agreement terms. Where the Department or a regional transportation agency uses a final evaluation of proposals based on qualifications and best value to select a contracting private entity, Section 143 mandates that the Commission adopt the criteria for making that evaluation.

The purpose of this guidance is to set forth the Commission's policy for carrying out its role under SB 4 X2 in P3 projects, in order to assist and advise the Department, regional transportation agencies and private entities that may be contemplating the development of P3 agreements. This guidance does not address Department and regional transportation agency P3 project procedures that are not within the purview of the Commission. Consistent with statute, the Commission may make exceptions to this policy for a project where it finds that particular provisions of this policy are not applicable to the type of P3 agreement under consideration.

Scope of Commission Project Approval. The Commission will approve each P3 project with the following elements. These elements may be taken together or separately, as deemed appropriate. The elements involve the adoption of a resolution after conducting a public hearing on the project as a scheduled meeting agenda item. The Department or agency may engage in preliminary actions leading to the development of a P3 agreement, including the solicitation of expressions of interest and proposals and the prequalification and shortlisting of potential contracting entities, prior to the Commission's project approval. However, the Department or regional transportation agency may not conduct the final evaluation of proposals prior to the Commission's project approval.

Performance Objectives. The Commission will select the project after reviewing the Department's or regional transportation agency's request for P3 selection. The Commission will typically place a request for P3 selection on its agenda if the Commission office receives such a request at least 21 days before the next scheduled meeting. The request for P3 selection will include the following:

- The description of the scope of the transportation project and its boundaries, including construction work and the performance of maintenance and operations.
- The Department or regional agency's estimate, with supporting documentation, of the extent to which the project will be designed to achieve each of the following performance objectives:
 - improve mobility by improving travel times or reducing the number of vehicle hours of delay in the affected corridor;
 - improve the operation or safety of the affected corridor;
 - provide quantifiable air quality benefits for the region in which the project is located; and
 - address a known forecast travel demand, as determined by the Department or regional transportation agency, with supporting documentation.

Project Proposal Report. The Commission will review each project with reference to a project proposal report submitted by the Department or regional transportation agency. A project proposal report will include the following:

- The draft project procurement documentation (e.g., request for proposal) that the Department or regional transportation agency intends to use in the solicitation of the contracting entity or lessee. Where the Department or regional transportation agency will make a final evaluation of proposals based on qualifications and best value, the project procurement documentation will include the criteria for making that evaluation.
- The proposed form of P3 lease agreement associated with the project, including proposed terms and conditions.
- For a Department project, the Department's determination of the useful life of the project in establishing the P3 agreement terms, including the basis used in making that determination.
- The project financial plan, which will include:
 - travel demand and toll revenue forecasts (if tolled), as determined by the Department or regional transportation agency;
 - commitments of state or local revenues to the project (including capital, operating, maintenance, and debt service);
 - if tolled, the alternative source of project revenue should toll revenues fail to meet projections or otherwise be insufficient to meet project costs; and
 - public financial responsibility for meeting project costs (including costs for operations, maintenance, and debt service) in case of default by the contracting entity or lessee.

After reviewing the project proposal report, the Commission will approve the project if it finds all of the following:

- That the project proposal report sufficiently describes the scope of the project and project financial plan;

- That the project proposal report sufficiently describes the procedures and criteria to be used to select a contracting entity or lessee;
- That the Commission's approval of the project and its financial plan will not create an undue risk to state transportation revenues committed to other projects; and
- That the project is designed to achieve the above-stated performance objectives.

Project Changes. In the event that, following a Commission approval of a project proposal, there is a change in the project that is material to the Commission's prior findings with regard to performance objectives or to the state's financial commitment to the project, the Department or regional transportation agency will submit to the Commission a supplement to its project proposal, including the final form of the P3 agreement, setting forth a description of such changes and the support thereof for the Commission's review of its prior approval.

Agreement Finalization and Execution. The Department or regional transportation agency will submit to the Commission a copy of the negotiated agreement prior to proceeding with the public hearing required by statute. After completion of the public hearing, the Department or regional transportation agency will submit to the Commission the comments received at such public hearing simultaneously with their submission to the Secretary of the Business, Transportation and Housing Agency, the chairs of the legislative fiscal committees and the Public Infrastructure Advisory Commission. The Department or regional transportation agency shall retain the discretion for executing the final lease agreement. If and when such agreement is executed, the Department or regional transportation agency will submit a certified copy of the P3 agreement to the Commission within 30 days of its execution.