P4: The Role of Planning in Successful Public-Private Partnerships (P3s)
Adding That Critical P to Your Process

by Keith Storms, Scott Evans Miller, and Buddy Hall

Before your institution decides to pursue a P3, make sure you’ve considered the fourth P—Planning—and how the P3 aligns (or doesn’t) with your campus master plan.

INTRODUCTION

PUBLIC-PRIVATE PARTNERSHIPS—in which public and private sector entities partner to deliver a service or facility for the use of the general public—are spreading in the United States and elsewhere as cash-strapped public entities seek investment funds from private sources. In a recent report, Moody’s Investors Service (2016) noted that U.S. higher education entities are expanding their use of P3s beyond student housing to include other types of university facilities. However, university officials also warn that a P3 approach is no “magic bullet.” Careful upfront planning can be the difference between a successful project and disappointment.

Further, it is important not to let immediate challenges and opportunities cause one to lose sight of long-term obligations. Institutional real estate holdings and campus ecosystems are prized assets, ensuring the long-term welfare of students and the entire community for decades, even centuries, to come.

In this article, we underscore the importance of taking this long view and share lessons learned regarding finance, planning, and negotiation at institutions that have undergone a P3 process. We also offer additional best practices regarding campus master planning to ensure a successful P3 process while maintaining the campus’s long-term integrity.

Challenged by tight finances and the need for new and renovated facilities, many higher education institutions are pursuing P3s. The stated benefits are numerous. Most fundamentally, institutions get needed facilities built while limiting the amount of new debt they take on. Financial risks and sometimes even management concerns can be shifted to the private sector.

Leadership quotes touting the benefits of the deals are common. “Every extra dollar we can generate or save is one less dollar from the students, their parents or Texas taxpayers,” said Texas A&M University System chancellor John Sharp in 2015 as he announced a P3 for student housing. “Besides the revenue it generates, the ... project also puts the debt and the risk on the books of the private sector” (Texas A&M University 2015, ¶ 7).

Yet for every P3 that comes to fruition, many do not. Even those that do come to fruition include compromises. That’s because such deals are financially complex, last a long time, and involve a tricky set of trade-offs and benefits. Institutions often give up control over land or property management for decades. With student housing, they give up revenue streams. Institutions may have to budget differently, spend maintenance funds differently, and deal with management changes over the life of the contract. “Not a magic bullet.” “Not free money.” “Long term.” These are some of the key
phrases higher education officials have used in describing P3s.

That’s why we think P3s really should be called P4s, with the fourth P for Planning. This involves planning beyond budgets and finances to account for institutional goals, land use, facility design, campus flow, campus feel, life-cycle cost, maintenance, and academic goals. More than once, as master planners and architects, we’ve seen a campus master plan—the road map for an institution’s long-range development—get leapfrogged in the process of putting a P3 in place. This often results in compromising the design integrity of the campus ecosystem and reduces the project’s likelihood of success. Elements often compromised that affect the campus context include building siting, scale and proportion, style, material quality, and links between buildings and the campus landscape. Each new campus facility, a new student housing complex for instance, can impact the entire campus in terms of access to classrooms and study areas; student life and culture; vehicular, pedestrian, and bicycle traffic; energy use; and even drainage patterns. These are the things accounted for in a master plan.

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“Institutions who’ve done P3s well do really good planning,” said Jose Coll, director of the School of Social Work at Texas State University and a P3 proponent, in a telephone interview on January 20, 2017. “It is critical to do it early, not only from a campus master plan piece, but also from a budget and finance perspective.”

EVOLUTION OF THE P3

The term P3 is broad and represents a wide variety of deal structures and arrangements. In higher education, public-private partnerships generally occur when an institution leases university-owned land to a developer to build, or build and manage, a facility. Until recently, most P3 projects on college and university campuses were residence halls, which produce a clear revenue stream for investors. Often these ventures involved housing projects with retail outlets at the ground level near campus edges or on outparcel properties. Now, P3s are expanding into more areas of higher education and deeper into campuses, too. This places even more emphasis on the need for proper planning, as core campus parcels can have exponentially more impact and consequence on the campus ecosystem than outparcels.

The University of Kansas (2016), for instance, is embarking on a $350 million P3 to redevelop its Central Campus District. The project includes a new science building, residence hall, dining facility, apartment complex, and even parking and utility facilities (figure 1). Purdue University (2016) and West Lafayette, Indiana, held a ceremonial groundbreaking in June 2016 for their “town-gown” partnership with a private developer for a $120 million modification of State Street, which runs through the city and campus.
Figure 1 University of Kansas Master Plan

Images by Hanbury
In August 2016, the University of California, Merced, closed on a $1.3 billion P3 that will facilitate a near doubling of the size of its campus by the end of the decade. The mixed-use development combines academic, administrative, research, recreational, residential, and student services facilities (figure 2). The developer will design and build the facilities and ensure that major building systems operate effectively over the 39-year contract. The developer will also raise all required private financing. In return, the university will pay the developer roughly $49.3 million a year over the life of the contract as long as all terms are met. All told, the developer will receive about $1.9 billion in payments from the university over the life of the contract in exchange for $700 million in upfront capital and all expenses, including the design, construction, operation, and maintenance of the facilities. Property rights, revenue streams, and the responsibility for delivering services stay with the university.

Figure 2 UC Merced 2020
“UC Merced, the youngest campus in our system, is poised to become a model for our other campuses as we look for the most efficient ways to construct, operate and maintain facilities that enable us to pursue our teaching, research and public service missions,” said UC president Janet Napolitano when announcing the developer (Waid 2016, ¶ 7).

Along with the benefits already mentioned, P3 proponents say P3s may help institutions reduce operating costs and get buildings built more quickly. Construction costs may be lower, too, and institutions avoid, at least in the short term, taking on more or as much debt. By keeping debt levels down, P3 proponents say institutions may enjoy higher bond ratings, which may enable them to borrow money at lower rates.

Examination of the aforementioned P3 project at Texas A&M reveals what officials expect in terms of the financial benefits as well as the financial arrangements needed to pull off the project (Texas A&M University 2015).

The Texas A&M University System leased 48 acres for its new student housing facilities to NCCD-College Station Properties LLC, a Texas nonprofit corporation. The nonprofit engaged private enterprises to develop and manage the project. NCCD-College Station will pay $18.5 million upfront to Texas A&M. Future revenues to the university are projected to average $20 million annually over 30 years. The facilities revert to the university system when the lease ends. Raymond James took the bonds to the market, garnering an overall cost of funds of 4.82 percent with a final maturity in 2047.
Park West, as the development is known, is the largest of five recent public-private projects of the Texas A&M System in College Station. Those five projects, system officials said, are expected to generate more than $900 million in benefits to Texas A&M over their lifetime—typically 30 years or more (Texas A&M University 2015).

“Aside from the revenue it generates, the private sector—not the Texas A&M System—also bears the cost for the five projects ($500 million-plus),” system chancellor Sharp and Texas A&M president Michael Young wrote in an op-ed in the Dallas News (Sharp and Young 2015, ¶ 7).

“Thinking outside the box through alliances with the private sector such as this gives us 21st century tools to meet 21st century needs,” they added (Sharp and Young 2015, ¶ 8).

PLANNING MITIGATES PITFALLS

Yet partnership means the deal has to work for both sides. That means private enterprises that fund, build, and perhaps manage new campus facilities also need to make them financially profitable. In order to get a project done—and done profitably—the private partner in a P3 may take less of a sustainable interest in the entire campus ecosystem than the public partner. It’s simply not part of the business deal. Meanwhile, in its desire to meet a pressing need, an institution may be enticed to make a short-term decision, for instance committing a parcel of land of potential higher and better use.

The P4 mind-set is a tool to mitigate risks of this type. Enough institutions have now gone through the P3 process, in part or in whole, for all of us to benefit from their lessons learned.

At a daylong seminar in late 2015 organized by California State University’s (CSU) Facilities Management Institute, institutions gathered to discuss P3 best practices. The session, which was attended by approximately 100 individuals from 23 CSU campuses, was also intended to provide background information on recent P3 projects.

Event materials noted that viewing a “P3 as a long-term solution, as opposed to a ‘quick fix’ to remedy a facilities need or budget shortfall,” was one of the key best practices (CSU Facilities Management Institute 2015, California State University slide 10).

During the seminar, participants identified an effective P3 “organization” as one in which “long-term planning” is considered and decision makers question whether the conceived P3 project is a method of accomplishing a goal identified in a campus master plan. In other words, P4 is the key.

Officials from the University of California, Merced, and the University of California, Davis, also shared what we think are good insights that all administrators should keep in mind as they explore P3s.

UC Davis officials noted the following (CSU Facilities Management Institute 2015, UC Davis p. 9):

» “A Public Private Partnership is not a ‘magic bullet.’”

» “This is a long-term relationship—pick your partner carefully.”

» “Make sure that you are clear on what you are trying to accomplish by entering into a P3.”

» “Expectation management is key.”

» “Understand [the] difference in private sector development types/standards.”

Picking a partner carefully is especially key given that P3s span decades. The housing P3 discussed by UC Davis at the seminar runs for 65 years. Over the course of that long a partnership, people on both sides of the equation will come
and go. Over time, P3s may be transferred by private parties or developers may sell companies, said Mark Rutheiser, associate director of real estate services at UC Davis, in a telephone interview. It is imperative that agreements be thorough enough to withstand all of these changes. “It is far from a handshake deal,” he noted.

UC Merced also shared its lessons learned (CSU Facilities Management Institute 2015, UC Merced p. 20):

» “Make sure the organization has the institutional fortitude, belief and faith to see the process through ... it should not be considered ‘free money’.”

» “Clarify the overarching design principles and objectives early; then careful translation into performance requirements.”

UC Merced noted that it has mitigated against financial risk in ways big and small. For instance, the deal specifies that the university won’t put any funds into the project until the developer puts in at least $150 million. After that, the university invests on a pro rata basis alongside the developer. That way, there will always be more assets than the university has paid for, said UC Merced senior adviser to the chancellor Daniel Feitelberg in a telephone interview.

Should a worst-case scenario arise, say the developer goes bankrupt and investors fail to step in with an adequate plan, UC Merced will have invested less than the investors and will also continue to own the land and the facilities, Feitelberg said. If the project is delayed and the facilities aren’t available to the university per agreed-upon timeframes, the university doesn’t pay until they are. Investors simply lose that income, he added.

Another safeguard? Over the length of the contract, the facilities have to meet a broad array of performance standards, Feitelberg said. These include such things as proper functioning of the IT infrastructure, plumbing, heating, cooling, and items as nitty-gritty as elevator maintenance. If the university believes a performance guarantee is not being met and the private parties don’t adequately respond, the university can reduce payment. It will then be up to the private parties to prove that they met the standard and should be paid in full. “This flips accountability on its head,” said Feitelberg.

One financial risk to institutions is overestimating the revenue that will be generated by a P3. Universities and colleges may agree to pay private parties a set amount as long as the parties complete their side of the deal, for instance, delivering a residence hall. However, if enrollment or housing fees don’t materialize as planned, institutions may still be on the hook for full payment to the private parties.

“You need to consider what will be the demographics of the school, five years from now and 20 years from now. What will your school look like from an enrollment and fiscal standpoint? What will this building look like?” Texas State University’s Coll said. “It is one of the hardest jobs: enrollment management and planning.”

Another risk is the cost of capital. Institutions need to pay close attention to the cost of private capital and what level of control they will have over the rents and fees that students will face as investors seek returns from that capital. Institutions may be enticed to give up too much in some P3 deals, including revenue streams and control over student residence halls, because they’re so thrilled to get quality housing they don’t have to pay for.

That’s not necessary with proper planning, and issues large and small should be worked out ahead of time. That includes details on who will control the rent and what say, if any, the institution will have in those rents. Another issue with student housing is who will enforce the student code of conduct once students move in. In general, the more transparent the arrangement, the better. If a developer is not
willing to reveal and discuss everything, it may not be the right partner for your institution.

That said, higher education officials also need to recognize the private party as a partner. There must be community buy-in and appropriate sharing of risk.

**IMPACT ON CAMPUS**

Weighing the P3 as part of the master plan is critical. Asking questions—the right questions—can make the difference between a satisfying result and an unsatisfying one.

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To get a fuller picture of the challenges, opportunities, experiences, and expectations of P3s as identified by institutions, we reached out to Hanbury clients, as well as other institutions, from across the United States and Canada. Through an informal survey, we gathered input from 30 respondents, including officials from finance, planning, housing, and facilities. Their anecdotal responses underscore our thinking that more planning is needed for successful P3s.

For instance, fewer than one-third of respondents said that proposed or implemented P3s “often” or “almost always” aligned well with campus master plans in terms of scope, timing, and location. The others said that P3s only “rarely” or “sometimes” aligned well with campus master plans.

What’s more, 12 of 29 respondents indicated that P3 projects “sometimes” largely superseded a campus master plan. More respondents, 16, said P3s “never” supersede a master plan while one said they “always” do. One respondent did not answer the question.

Respondents were roughly split on whether more planning would’ve improved a P3 outcome.

With that information in mind, we’ve crafted some simple best practices to consider when developing or weighing a P3:

» *Invest time in preplanning.* Review the campus master plan to ensure aspects affecting P3 sites are properly updated. Consider a mini master plan update or a sector plan prior to proceeding with the P3 RFP.

» *Clearly define goals.* This includes defining goals for the project and the campus in precise detail for the RFP. Include prescriptive minimum requirements, design guidelines, and also desired added-value goals. At the CSU event, one of the most important lessons learned was making sure to “repeat, repeat, repeat” goals and objectives (CSU Facilities Management Institute 2015, University of Kansas slide 18).

Another best practice discussed at the CSU event was the need for decision makers to pay ample heed to recognizing the “primacy of the institution’s mission” or missions, such as “educating students, conducting research and delivering services to the community” (CSU Facilities Management Institute 2015, California State University slide 10).

At UC Merced, one of the overarching goals of its P3 is that the new parts of the campus blend into the existing campus so there will not be “an old and a new campus,” Feitelberg said. Another big goal is that the new spaces are designed with a mixed-use mind-set, paying heed to the university’s desire for classrooms and residence halls to be intimately connected, he noted.

» *Explore options.* By having a financial model for a non-P3 approach, you’ll have a good baseline for comparison. This provides valuable insight when considering P3 options and proposals. P3 critics often point out that a P3 project may actually cost more given that the public entity may be in a stronger borrowing position than the private sector entity. In our survey, “disagreements on financial terms” was most often listed as the biggest obstacle in a P3.
Heed maintenance. It can be a big part of ongoing costs. Estimating the life-cycle costs of maintenance for a building or other structure may be crucial to crafting accurate financial terms. “Having a capital budget that provides for design and construction costs is not enough,” Feitelberg noted. “A focus on lifecycle costs is necessary to avoid future deferred maintenance and ensure that facilities are durable over the long-term.”

Think outside of the site. Be sure you define goals and requirements for the campus areas adjacent to P3 sites as well as the P3 sites proper. The more detail included in predesign efforts, the better.

Do your homework. Have a clear understanding of your state’s policies, processes, and construction standard requirements for P3 procurements.

Use experts. It may behoove you to involve your master plan consultant in evaluating P3 proposals.

Focus on long-term objectives. In evaluating options, these should be a big part of the discussion along with the project or site. No piece of land should ever be given over without a long-range assessment of what will be fully lost for years and even generations. Several years ago, Boise State University called off a private equity deal with a developer for a large residence hall partly because of worries about signing an 85-year deal and limiting future options, a New York Times article noted. “Who knows what the university may need to use its land for in that kind of a time frame?” the university’s architect was quoted as saying (Kaysen 2012, ¶ 21).

Phillip Ray, vice chancellor for business affairs for the Texas A&M University System, suggested colleagues “never rush” when considering a P3 because the deals are so complex and different.

“If you’ve seen one P3, you’ve seen one P3,” said Ray in a telephone interview on January 26, 2017. “If there’s something in the back of your mind that doesn’t sit right, talk about it. Talk about the tough stuff and talk about it early.” P3s have helped enable that university system’s expansion while it maintains a Triple A bond rating, Ray said. “We take that very seriously,” he added.

FURTHER EVOLUTION

Simon Fraser University in British Columbia (figure 3) had to look for a solution other than a P3 because government restrictions don’t allow it to take on any debt—and even an occupancy guarantee would count as such, said Alison Blair, the university’s associate vice president of finance, in a telephone interview. As a result, it is pursuing what it says may be one of the first deals of its kind in higher education.

The aim is to get five residence halls built to house 1,696 students, Blair said. The university plans to build the halls itself using working capital. Then, investors would replenish that money through an upfront lease payment in exchange for rental income from the halls. The university would also control daily maintenance and residential life features. Future rents would be set by the university at market rates with input from investors, which might include pension funds and other institutional investors, Blair said. The investors assume all occupancy risk.

The biggest risk to the university, Blair said, is underestimating construction costs. The halls will be built in five phases with each one priced separately. That should reduce the risk that construction costs will be higher than anticipated.

Leases are likely to run 60 to 99 years. Since the university is paid upfront, some risk is mitigated should the investment group falter. Contracts will also include protections for the university should investors fall short on future maintenance.
The solution “allows us to build residence halls, not take on debt, but still remain in control,” Blair said. Another plus? The investor is in the background and students still engage with the university, not an outside property manager.

Even with the multitude of P3 models at their disposal, other institutions are electing not to pursue P3 delivery. A decade ago, Florida State University (FSU) considered P3 delivery methods to add to its housing stock but “rejected them all,” said David Sagaser, director of facility services for university housing, in a telephone interview. University officials “felt we could control the financials much better” with traditional bond financing, Sagaser said. Consideration of a P3 approach also raised “concerns about the end product,” especially given FSU’s stringent campus design standards. Many of the existing halls are built in the Collegiate Gothic style. “The university has signature buildings ... and we prefer to make design decisions in house,” he noted.

The university has taken a long-term view of its housing assets, which has resulted in successful outcomes for both housing and the campus, Sagaser said. FSU has systematically planned, financed, and implemented over $325 million of investments in its housing system. Since 1993, it has renovated or built a total of 17 residence halls at costs ranging from $2.1 million to almost $40 million. Two additional $30 million projects are under construction.
So far, the university has been able to successfully access the bond markets. Florida governor Rick Scott has been aggressive about cutting state borrowing in a bid to improve the state’s financial health. Still, FSU won approval to bond the last two projects. Bond terms were set for 20 years, down from 30 years as had been typically the case, Sagaser said.

CONCLUSION

The Simon Fraser plan and FSU’s systematic approach and ability to access bond markets are just two of the ways institutions are funding facilities. P3s are another way. Done well, they are a viable alternative and, given a Trump administration, likely to get even more attention. In his joint address to Congress in February, Trump even noted plans to ask Congress to approve legislation to boost investment in infrastructure—“financed through both public and private capital.” What’s more, the financial contraction facing many institutions is unlikely to abate any time soon. Even though some states have begun to restore deep cuts made during the recession, funding for public two- and four-year colleges is still nearly $10 billion below what it was just prior to the recession when adjusted for inflation, the Center on Budget and Policy Priorities reported in August 2016 (Mitchell, Leachman, and Masterson 2016). Meanwhile, our nation’s campuses wrestle with outdated and aging facilities.

It is imperative to view a P3 as a holistic and interrelated subsystem of an institution and not as a single entity. Campuses are, after all, no less than small, and sometimes not so small, cities. They have hearts, histories, and architectural and cultural bones. They should be celebrated and treasured as unique and precious elements of the built environment. Placing a new building is a decision that impacts a place for decades. Proper planning serves the institution regardless of the project delivery method. It is critical that a P3 be well crafted so that it serves the university, its students, and the community for decades, even generations. That can be achieved through proper planning—the fourth P added to the P3 process.

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REFERENCES


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