



IIGR

**2015 State of the
Federation
Conference**

***“Canadian
Federalism and
Infrastructure”***

Recycling Public Assets: An idea whose time has come?

Presentation by Michael Fenn

June 5, 2015

**Donald Gordon Conference Centre
421 Union Street
Kingston, Ontario**

Who will pay for growth and infrastructure?...

- No public support for raising taxes and fees any time soon, even for much needed infrastructure
- Not winning the hearts and minds of voters for more money from taxpayers' pockets
- If no new revenues from citizens and businesses for to public infrastructure, what can we do?
- “Public asset recycling” – leveraging or disposing of all or part of governments' legacy assets

Paying for new infrastructure with asset dispositions –

- “Recycling” public assets and GBEs – use vestigial public investments to fund future public needs
- Not overstretched taxpayer and with greater returns to pension plans
- Ontario Government spends over \$10 billion each year for debt service
- Paying with asset dispositions – rather than borrowing and using taxes to pay debt-service costs

Paying for new infrastructure with asset dispositions –

- **Mowat Centre: “*Recycling Ontario’s Assets: A New Framework for Managing Public Finances*” (2014)**
- **“Advanced countries have been slow to sell or make better use of their assets. They are missing a big opportunity.” *The Economist* January 11 2015**
- **Some public assets worth more to the taxpayer in private hands**
- **Could we sell some government enterprises and monopolies and still earn the same net revenues and advance public policy goals?**

Paying for new infrastructure with asset dispositions –

- **Governments and citizens need to assess critically the billions of dollars in assets that we own as a society...**
 - **From government enterprises to infrastructure – including public lands and buildings**
 - **Valuable “intangible” data and technology assets**
 - **Does it still makes sense to own them?**
 - **Sell asset in whole or in part, including monopolies, to pay for infrastructure we need now for the long-term?**
- **Our public-sector pension funds can certainly point-out some good examples. Maybe we should test the market seriously before we reject the idea?**

The promise of public asset recycling

- Sale proceeds or avoided costs allow us to build desperately needed new and refurbished public infrastructure.
- Not a case of selling furniture to pay for groceries. More akin to selling your used car to help pay for your new car, or selling ATV to pay for your teenage daughter's dental braces. It's all a question of setting priorities.
- Historically low-interest-rate environment: value of public assets likely never greater than today, in current dollar terms.
- Across the world, pension funds and sovereign wealth funds are investing in infrastructure and in a range of public assets, from publicly operated business enterprises, to information technology

The promise of public asset recycling

- Many of these capital investments provide ‘public goods’ that would otherwise not be available to debt-ridden and cash-starved governments and public agencies.
- Other transactions designed to produce one-time revenues or streams of revenues to build or restore public infrastructure, while reducing taxpayers’ obligations to pay-down deficits or to fund capital borrowing.
- Leveraging assets does not have to be a political minefield
- Levering assets can facilitate governments’ ability to meet their current and future economic, fiscal and programmatic objectives, without resorting automatically to the overburdened taxpayer or adding to public debt or deficits.

Resistance to P3s

- Public entities in Ontario preferred to be active participants in delivering services and building facilities, rather than simply causing them to be provided to communities and consumers.
- Rooted in history, ideology or self-interest; public purpose not achieved without government control and ownership; revenues flowing to government from government-owned operations.
- Assertion that capital is inexpensive for the public sector in Ontario, and readily available for public projects and public enterprises – if there is willingness to take-on public debt.
- Governments need to be smart about the asset recycling process – matter of design of the deal, not principle of asset recycling

What's the record?

- Sale of the land-registry service Teranet has been a great financial success for the Government of Ontario
- Private operation of Bruce Power nuclear facilities has helped Ontario to assure our electricity future.
- Both asset-dispositions earn solid returns for 450,000 pension-fund members in Ontario
- Detractors can always find examples of failed efforts at involving private sector in government assets, depending on their definition of failure.
- It's all a matter of the terms and conditions, and effective negotiations, based on due diligence and learning from experience.

What's the record?

- The need to leverage public assets is both pressing and opportune
- By using yesterday's capital investments to fund today's and tomorrow's public priorities, governments can dislodge themselves from the vice-grip of a weak economy and crumbling infrastructure, and a lack of fiscal and political capacity to act in ways that are decisive, and even visionary.

Australian Finance Minister Joe Hockey's April 2014 Budget Statement:

- *"...I also want to emphasise that the Government will not fall into the trap of cutting back on infrastructure spending as the United States and many European countries have been forced to do as their fiscal positions have deteriorated.*
- *"Instead, the Government will boost infrastructure spending, including through my work with State and Territory counterparts on an asset recycling initiative.*
- *"This ground-breaking policy will see the Commonwealth provide financial incentives to States and Territories that sell assets and recycle the proceeds of these sales into new productive infrastructure...*

The 'cycling' of public assets

- Policy governing public assets dynamic and cyclical
 - not static or ideological
- By leveraging existing public assets, governments at all levels can 'unlock' the wealth of legacy assets
 - from land and infrastructure, to government enterprises and intangible assets like information technology –
- Recycled public assets can pay for urgently needed new or deteriorating public assets, from roads and bridges to educational facilities and environmental projects
- Private sector builds / delivers new public assets on-time, on-budget – or provides services traditionally provided directly by public agencies
- When vestigial public assets no longer required to fulfill some significant public purpose, can be returned to society as taxpaying enterprises and / or managed effectively and efficiently by private or non-profit sectors as facilities or services to meet community and consumer needs.

The 'cycling' of public assets

- Even where public assets actually meet an express public policy goal or need, non-government sector can play a role in efficient and customer-focused delivery (such as Bruce Power nuclear energy), or to generate better financial returns to government (such as the Teranet land-registry system).
- Properly structured, 'asset recycling' can be used at each stage of asset's lifecycle, from asset acquisition through P3s or concessions, through to asset management by private operators, and on to full or partial sale, lease or joint venture as part of government disposition of non-core public assets.
- In all three phases of their lifecycle – from acquisition, through operation, to disposition – public assets can be 'levered' to generate better performance, risk-transfer, and financial returns to governments and public agencies (including reduced express or implicit subsidies)

“The devil’s in the details”

- Done properly, cycling of public assets through their three phases can reduce their burden on society by:
 - Reducing public debt,
 - Attracting new investment and economic activity,
 - Providing competitive returns for pension funds and public investments, and
 - allowing new needs and priorities to be met from legacy assets.

- While the concept of public asset recycling may sound simple, there are many hurdles to its effective implementation. But they’re hurdles worth challenging, because potential benefits are very significant.

- Lessons to be learned from Australia, Canada and elsewhere

- Success depends on creating conditions that favour government support for recycling assets, and by matching those efforts with a clear-eyed approach to removing barriers to private investment

What are “winning conditions” for the public sector?

11 hurdles to clear from path of inherently risk-averse governments and public authorities:

- Recognize and enhance value of public assets.
- Right people in charge of the disposition program.
- Formal asset-recycling framework or policy
- Enlist public support – market the idea effectively before you start
- Establish a capital Fund or Trust for infrastructure and other capital assets. Public and auditors want guarantees against governments succumbing to other “fiscal temptations”
- Balance need for political oversight against risks and real costs of “political interference”

What are “winning conditions” for the public sector?

- **Begin with assets with financial impact & precedent-setting value – don’t be seduced by well-intentioned advice to start slow or small**
- **Identify new public assets that will improve productivity, create new economic activity and improve quality of life. Use those same criteria in deciding which assets to divest.**
- **Focus regulation on outcomes – specify the end-results you want to see, don’t try to ‘regulate your way to success’**
- **Recognize influential role of public employees – the success of disposition may depend on them.**
- **Make sure the accounting, budgeting, accountability and transparency rules support, rather than impede, achieving public objectives in changing circumstances**

“Winning conditions” for investors, private & non-profit partners in any asset-recycling initiative

- “Asset recycling” not merely a strategy for government needs, including protecting and advancing public interest
- Any asset-recycling policy and program must also meet needs of private and non-profit sectors
- They must be persuaded to play a meaningful role, to invest their capital, and to accept risk transfer

Baker’s dozen preconditions:

- Give full weight to perennial private-sector concerns about “politics” – anxiety about use of state power and government’s ability (and periodic temptation) to change rules of the game

“Winning conditions” for investors, private & non-profit partners in any asset-recycling initiative

- **Avoid one-offs – make a clear government commitment to a “pipeline” of public assets scheduled for disposition**
- **Take measures to enhance certainty about government funding commitments, over time**
- **Recognize investors’ expectations for reasonable, risk-adjusted returns, including pension funds. Fiscal impacts and policy goals are government’s priorities; investors’ priorities are good returns and successful operations**
- **Are projects appropriately structured? Don’t guess: get good advice and candid market sounding**

“Winning conditions” for investors, private & non-profit partners in any asset-recycling initiative

- **Avoid complex, expensive and inconsistent transaction processes; investors should get used to your way of doing business, so they can reduce their transaction costs and avoid pricing-in uncertainty costs.**
- **Ensure government side has specialist expertise and promotes processes that attract counterparty expertise in more than simply deal-making**
- **Do a realistic evaluation of value of infrastructure in private hands; value it from the investors’ perspective, not just the government’s**
- **Recognize that “greenfield” projects (without a track-record) have special risks for investors and private operator. If you need to do greenfields projects, be ready to absorb discount or to provide guarantees, but demand a share on “up” side, too**

“Winning conditions” for investors, private & non-profit partners in any asset-recycling initiative

- **Recognize and understand private-sector perspectives on regulatory, liquidity and industry pressures**
- **Reform tax, accountability and accounting regimes to encourage asset recycling and to favour public interest in their success.**
- **Monitor and respond to changes in investment climate and conditions facing both potential and existing private and non-profit partners.**
- **Respect role, contributions and impact of public-sector trade unions. Labour relations prominent in minds of potential private-sector and non-profit sector bidders and partners**

Conclusions...

- **“Recycling” public assets – especially government business enterprises – offers opportunity to use past and vestigial public investments to fund current & future public needs**
- **It makes it possible with less call on overstretched taxpayer and with greater returns to pension plans and other domestic investors**
- **Public asset recycling – a timely fiscal policy idea for Canada and its governments**



IIGR

**2015 State of the
Federation
Conference**

**“Canadian
Federalism and
Infrastructure”**

Note: The comments and data of the presenter represent his own opinions and may not represent the views of the organizations cited or the organizations with which he is associated.

Recycling Public Assets: An idea whose time has come?

Presentation by Michael Fenn

**Michael Fenn
Fenn Advisory Services Inc.
2141 Caroline St., Unit 5
Burlington ON
L7R 1L7**

**Business phone and BlackBerry: 905.699.1776
mfenn@cogeco.ca**

"Navigating issues...Leading change"