AMERICAN PUBLIC POWER ASSOCIATION
Powering Strong Communities

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# Private Equity Firm Bernhard Capital Partners Continues to Approach Public Power Utilities

## Overview

Bernhard Capital Partners Management LP (BCP) is a private equity management firm based in Louisiana that has approached several public power communities with proposals to enter into financial and operational agreements with municipal electric, water, and wastewater systems in the southeastern U.S.

In 2018, BCP approached the city of Lafayette, Louisiana, with a proposal to manage the electric division of Lafayette Utilities System. BCP also announced the firm's broader strategy to invest $10-$15 billion in municipal utilities throughout the southeastern U.S. and to manage the public power utilities through a subsidiary called NextGen Utility Systems. States noted include Alabama, Arkansas, Florida, Louisiana, Mississippi, North Carolina, South Carolina, and Tennessee.

While BCP's efforts in Lafayette were unsuccessful, they have continued to approach public power communities in each of the targeted states with similar proposals. They have also hired lobbyists in the targeted states and have registered as a legal entity in at least one state.

While BCP has publicly stated its interest in public power utilities, we expect other private investment firms may approach public power communities.

This issue brief outlines the likely deal structure, the potential impacts, and factors to be considered in such a deal.

## Likely Deal Structure

BCP has proposed long-term concession agreements/leases. These are agreements in which a private entity takes over the operations and maintenance of an existing utility and receives the right to collect revenues associated with the system in exchange for an upfront fee to the governmental entity.

Possible terms:

- The term of the contact is typically 30-40 years.
- The private investment firm provides an upfront cash payment to the municipality and/or may agree to an annual payment to the city.
- The private investment firm earns a return on all existing assets and new capital additions over the term of the contract. BCP is seeking an approximately 8% return on investment.
- BCP claims the utility assets will remain owned by the city and managed and operated by existing employees of the city.
- The private investment firm assumes control of rates and investment in the system over the term of the contract.
- There may be a repurchase payment required on the part of the municipality at the end of the term to compensate the private investment firm for their investment in new capital additions. The community must plan ahead if it wants to maintain the ability to run the utility once the term of the lease ends.

## Impacts and Risks

While BCP has approached several public power utilities in the southeast over the last three years, no deals have come to fruition to date. However, there has been significant activity in the water industry. In the Public Interest, a national nonprofit research and policy organization that studies public goods and services, has studied the impacts of private investment and privatization of water systems and is collaborating with APPA on the development of a white paper on the impacts of private investment in utilities which will be available in May 2021.

These arrangements typically do not provide long-term benefits to the community. Cities faced with a deal should take care to ensure elected officials weigh the potential long-term impacts on the community and the customers against the short-term influx of cash.

### Loss of local control

Under the terms of a deal such as what was proposed to Lafayette, the community would no longer have the ability to make decisions related to their utility thereby inhibiting local input into critical decisions that are in the best interest of the community such as generation mix, environmental concerns and the effects of rate changes. Due to the long length of the contracts, and the long-term nature of utility decisions, this could mean the community would be living with decisions from outside interests for generations.

### Reduced long-term revenue for the city

Public power utilities provide significant payments and contributions to state and local governments in the form of property-like taxes, payments in lieu of taxes, transfers to the general fund, and free or reduced-cost services for municipal facilities and functions. These payments and contributions will likely be lost in a lease arrangement and should be considered in the analysis.

### Decisions driven by profit potential

Private investors demand a rate of return. To achieve the desired rate of return, either revenues will need to be in increased (e.g., higher rates) or expenses reduced (e.g., staff reductions, limits on infrastructure investments, etc.).

### Rate increases for customers

While the private investment company may claim that rates will remain at current levels, there is no guarantee of such a claim over the life of the contract. The city will no longer have control over setting electric rates and the utility budget. Further, the utility may no longer have access to lower-cost financing through tax-exempt municipal bonds, potentially placing upward pressure on rates.

### Reduced reliability

In an effort to reduce costs, the private investment firm may choose to reduce ongoing investment in the system. A decrease of investment in critical or aging infrastructure or in replacement and repair projects will have a negative impact on reliability.

### Reduced safety and local employment

Cuts related to the workforce, such as reducing staff, salaries, benefits and/or training for employees will have a long-term impact on safety and on the financial health of the employees and the community as a whole.

### Economic development impacts

The private investment firm may promise that it will locate new facilities within the city limits. It may promise to employ local residents and to purchase equipment and supplies from local merchants. However, such promises are often broken.

## Factors to Consider if Approached

Public power utilities provide long-term value to their communities, so there must be compelling reasons—beyond the short-term cash value of the assets—to consider giving up those benefits. These utility assets not only reflect the investments of its past and present customer-owners over many years, but they can continue to provide benefits year after year. The lease of such a valuable asset is a complex issue and should be examined carefully.

Lease agreements have the potential to impose hidden costs on the community, lost opportunity for revenue, degradation of service quality and reliability, and loss of control over the system. Often it comes down to the rights and responsibilities of each party and how tightly those responsibilities are drawn in the contract.

There are several factors to be considered if approached by a private investment firm with a long-term concession agreement.

### Financial analysis

There should be a robust organizational and financial analysis that clearly evaluates the costs, benefits, and risks over a long-term horizon. This should include an open and transparent process recognizing the financial and qualitative value your utility provides to your community.

### Legal analysis

There should be a legal analysis to examine new and existing contractual obligations, liability/indemnification provisions, impacts on the tax status of the municipality, and any outstanding debt.

### Seek clarity on key issues

There should be clarity and buy-in on key authorities and priorities, including:

- Rate setting
- System maintenance
- Capital planning and investment
- Reliability
- Safety
- Impact on employees

## Additional Resources

Long-term concession agreements/leases can be precursor to the sale of the utility, which would have a permanent impact on the community. APPA offers many resources to public power utilities and stakeholders evaluating whether to sell their community-owned electric utility or to retain public ownership. Contact EducationInfo@PublicPower.org for more information and resources.

The American Public Power Association is the voice of not-for-profit, community-owned utilities that power 2,000 towns and cities nationwide. We represent public power before the federal government to protect the interests of the more than 49 million people that public power utilities serve, and the 93,000 people they employ. Our association advocates and advises on electricity policy, technology, trends, training, and operations. Our members strengthen their communities by providing superior service, engaging citizens, and instilling pride in community-owned power.