

5 Tips For Managing Megaprojects

By **Liz Hoffman**

Law360, New York (February 03, 2012, 5:51 PM ET) -- When infrastructure or development drags on for decades, parties must limit project fatigue, keep the money flowing, respond to scope and regulatory shifts, and manage turnover of key personnel.

The difficulties that come along with any project can multiply as its life span grows, and setting the stage to deal with these hiccups starts early, experts said.

"A lot of what happens in the 30-year life of a project can depend on what happens in the first three months," said Jacob Worenklein, co-chair of Akin Gump Strauss Hauer & Feld LLP's project finance practice. "It is so much about setting the tone and developing trust."

Here are some tips project finance attorneys and other experts offered for helping to keep megaprojects on the right track.

Build Relationships, Not Just Assets

When project sponsors and lenders will be working together for decades, setting a tone of trust and good faith early on will avoid headaches and potential disputes down the road, experts said.

Parties that feel they're trusted and kept in the loop will be more willing to take chances. Lenders will grant waivers, shareholders might go along with a higher level of debt and public partners might extend some political cover for hiccups in the project, experts said.

Worenklein recalled a deal early in his career, a billion-dollar sale-leaseback of a nuclear power plant where last-minute negotiations had left the parties with a midnight tax deadline and hundreds of pages of document revisions coming in late from the printer.

The equity investors Worenklein represented had a choice: miss the deadline and lose certain tax benefits, or sign the contract without reading the final draft, trusting that they would be able to fix any mistakes later.

"A deal where the two sides didn't trust each other would have died," he said. "That deal closed, and it was because we'd spent months building trust in the way we negotiated with each other."

Once an asset moves into operation, it can be even more important to keep lines of communication open and constructive. As lenders get replaced or public involvement ends, keeping “institutional knowledge” alive is key, said Allan Marks, a finance partner in Milbank Tweed Hadley & McCloy's Los Angeles office.

Contracts can play a big role in encouraging dialogue — or stifling it, attorneys said. Reporting provisions should be tight enough to catch problems early, but not so onerous that they drag down productivity. Time frames to cure defaults should account for technical issues — for instance, it's a lot faster to fix an above-ground turbine than a transmission line buried beneath it — but keep operators in check.

“No one wants a project that's economically sound and operating smoothly where the contracts turn into an administrative burden,” Marks said. “You have to strike a balance that works for the particular project.”

Know Your Client

Some clients just want to build the mine or refinance the power plant. But some have other motives, and listening for those things is important, Worenklein said.

What seems like an enthusiasm for equity investors could be fear of rejection by the credit markets, he said. A lending client that seems wary about public fanfare might be worried about overshadowing other projects the bank is backing. Others might want to curry favor with regulators or win public relations points.

For example, Bank of America Corp. recently entered a deal to back solar panel installations on military housing. While the project was solid with bankable cash flows, it also offered an important side benefit: public goodwill in a year when the company faced regulator lawsuits and a plummeting stock price. A series of TV commercials made the point.

“Without coming off like a therapist, you have to really understand what you're client is trying to get out of a project,” Worenklein said.

Project finance professionals should also try to understand their clients' financial assumptions, Hill said. Today's lawyers are far more financially savvy than in generations past, but still, too few really roll up their sleeves and dig into financial models, he said.

If a solar project has little wiggle room in its weather model, project developers might want to consider photovoltaic performance insurance. Locking in an overrun facility up front may ease the sting if questionable soil in an early study turns out to be solid bedrock.

“Getting into the financial model of a project could be the most valuable three hours of a lawyer's time spent with a client,” Worenklein said. “Get some help from the client's financial analyst if you need it, but look at the model to really understand the project.”

Bring the Public Along

From battles with local unions to traffic jams, nothing will sink a project faster than opposition from a community set against it, Paul Hastings LLP partner Charles Thornton said.

Thornton is working on Bayview-Hunters Point, a project that will transform the area around San Francisco's old shipyard into 700 acres of housing and commercial space. The project could take up to 35 years and is wrapped up in public issues like affordable housing and the prospects for a stadium for the NFL's 49ers.

“You can almost always find more funding,” Thornton said. “But if the plan is to redevelop this huge stretch of San Francisco Bay, and San Francisco decides it doesn't want you there, you're going to be in trouble.”

Hunters Point's developer, home builder Lennar Corp., sponsored a ballot initiative that committed them to keep at least a third of the housing in the new community below market-rate. It passed with nearly 70 percent of the vote.

“That was gutsy in some ways, but it was an enormous boost to the project,” Thornton said. “There was a public, quantifiable support that we could lean on going forward.”

This lesson goes beyond sponsors' obligations to meet with zoning boards and submit community health assessments, experts said. Voluntary gestures go a long way, experts say. Examples might include holding a forum with community members, showing up in the office of the borough president or even sponsoring a little league team.

And while it might be tempting to muzzle executives in the face of controversial work, project leaders should be encouraged to take their case directly to the public.

“The senior executive responsible for a major project should be a face people know,” Worenklein said.

Project leaders should identify stakeholders early and think broadly about who might be affected, said Sean Coffey, a Burns & Levinson LLP project attorney in Rhode Island.

During a Pawtucket wastewater project in 1999 that involved turning the plant over to a private operator, the group waited too long to sit down with union officials and nearly had an employee walkout on their hands. Today, seniority and pension contributions are laid out in term sheets, he said.

“You have to keep a broad definition of 'impact' in your mind,” he said. “There are constituencies beyond the normal ones you think of.”

Roll with the Punches

Even the best-laid plans hit bumps in the road. PricewaterhouseCoopers LLP capital adviser Peter Raymond calls it “project-specific risk,” and it includes things like rare bird migrations or Native American burial grounds or even market assumptions that turn out to be dead wrong.

For example, when Cheniere Energy Inc. started building the Sabine Pass LNG import terminal in 2005, natural gas prices were near \$15 per million British thermal units. Today, they're around \$3, an unforeseen price drop that decimated the group's plans to import natural gas and sell it to utilities at sky-high prices.

But instead of tanking the project, Cheniere has reimagined the plant as an export facility. The company is securing financing for re-engineering and construction, and has locked in four key export agreements in recent weeks.

“Responding to scope changes makes or breaks projects,” said Raymond, who did not comment on any particular projects. “It's not a matter of if, but when” tweaks will be necessary, he said.

And it's how developers respond that counts, he said. Intrasponsor agreements can set out which party is responsible for ensuring market demand, who is the primary point of contact for subcontractor delays and whose approval is needed for small siting changes.

Project developers shouldn't shy away from the unpleasant possibilities, either, experts said. The ability to respond well in a worst-case scenario can turn a tragic or potentially project-ending event into an opportunity to show competence.

On Super Bowl Sunday 2010, an explosion ripped through the Kleen Energy power plant in Connecticut, killing six workers, injuring dozens, and causing millions in construction costs and repairs to the project, which was almost 90 percent complete.

But under a Bingham McCutchen LLP team, the project responded quickly. The lenders kept lending, the insurance companies paid quickly, the company cooperated with investigations and the project got back on track. No criminal charges or fines were assessed, and the plant was finished last summer.

Embrace Washington

With aggressive regulation and shrinking public budgets, sponsors might find it easier today to stay as far away from the Beltway as possible. But public funding and political backing, especially if it survives a regime change and more than one annual budget, can be a lifeline for a project.

“For most of the largest projects, people are looking for a commitment on the part of the public sector to get it done,” Raymond said. Political rhetoric isn't enough, he said — speeches have to be matched with spending.

Find programs that offer funding matches or credit guarantees. Big projects can dream big; the Transportation Infrastructure Finance and Innovation Act can help investment-grade projects secure credit access. Section 129 loans are a useful, often underemployed option for smaller funding needs, experts said.

“There's a sense sometimes that public financing, whether it's state or federal, will tie a project down,” Thornton said. “But in the end, you'll end up getting much more than just the funding.”

--Editing by Elizabeth Bowen.