AN ALERT FROM THE BDO PRIVATE EQUITY PRACTICE

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CONTACT:

SCOTT HENDON
National Private Equity Industry Group Leader
214-665-0750
shendon@bdo.com

DESPITE HEADWINDS, U.S. INFRASTRUCTURE IS OPEN FOR BUSINESS

U.S. middle-market private equity infrastructure funds are seeking deal opportunities domestically, despite the uncertainty surrounding the government's plans to jumpstart infrastructure investments. These funds will invest in all types of infrastructure assets, from gas pipelines and renewable energy, to toll roads and bridges.

Of course, these private equity firms will not be able to modernize the nation's infrastructure on their own. After all, there is a huge need to revamp infrastructure in the U.S. – the American Society of Civil Engineers figures there's a $2 trillion investment gap to bring the nation's infrastructure up to date.

While the government has had many discussions about encouraging infrastructure investments, these don't seem to have translated into action.

The Trump administration had announced that it would seek to combine forces with private investors to pour $1.5 trillion into modernizing infrastructure, but those specific plans appear to have stalled. In response, House Transportation and Infrastructure Committee Chairman Bill Shuster announced a proposal in July to authorize incentive grants that would encourage public entities to lease their infrastructure to the private sector and use the capital raised to improve other public infrastructure. It remains to be seen if this proposal will reignite the infrastructure discussion.

More recently, the White House has been reportedly planning to expand its "Buy America" provisions to require that infrastructure projects developed in the U.S. be built with U.S.-made materials, which could make these projects more expensive to build and cause delays in deliveries due to constraints in the U.S.-made material markets.

A nascent trade war adds yet another hurdle for infrastructure investors in the U.S. Tariffs on steel and aluminum, for example, could also make project development costlier.

With all these headwinds affecting infrastructure in the U.S., it is important for private equity firms raising infrastructure funds or already making acquisitions to make sure they are prepared to structure their deals in a way that will help them mitigate any pitfalls that may arise at any point in the transaction process. Here are some of the items that should be on any fund's to-do list:

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FEASIBILITY STUDIES

For firms seeking to invest in greenfield projects, a feasibility study is of utmost importance. These studies will uncover historical information regarding the property where the project is to be developed as well as its adjacent areas.

After the data compiled is analyzed, the investors and developers will obtain a clear picture that will allow them to determine whether the property is fit for the planned development. It will also provide clarity on the types of permits needed, what the development will cost, what kind of environmental impacts and risks it may have.

TARIFF AND TAX ISSUES

Infrastructure investors will have to keep an eye out for changes to taxes and tariffs to determine the ultimate costs of their target assets. For one, firms investing in infrastructure that serves the oil and gas industry are already expecting to be hit by the tariffs on steel and aluminum, as they could put a damper on exploration and production activity.

But it's not just the tariffs on steel and aluminum that infrastructure investors need to be aware of. For example, the Trump administration has slapped a 30 percent tax on solar power imports—excluding the first 2.5 gigawatts of solar cell imports following the order—and is set to last for four years.

While the tariff will be reduced by five percent each year, eventually dropping to 15 percent in 2021, there is no doubt that it will impact the business decisions of solar power developers and the investors backing them. Some analysts predict that it may cause as much as a 13 percent drop in U.S. solar power installations over the next five years.

POST-ACQUISITION PREPAREDNESS

In the infrastructure space, it is important to also be prepared to address unforeseen environmental issues and challenges, including remediation costs and allocations, financial and cost accounting, and environmental claims analyses. While it is critical to address potential environmental issues in the feasibility stage, investors must also be prepared to address situations that could arise after a deal is completed. After all, accidents happen. However, there a variety of strategies to mitigate and control the costs of environmental remediations.

But infrastructure deals are also subject to problems that can impact any other type of M&A deal, such as post-closing purchase-price adjustments and earn-out calculations, have the potential to appear after a deal is thought to be completed. Usually, these problems are the result of differing interpretations of purchase agreement terms. The best way to avoid these disputes is to ensure that all contracts are as explicit as possible and tailored to the specific deal.

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