

PANDEMIC AND EPIDEMIC EVENTS: ADDRESSING THE RISK IN P3 PROJECTS

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Public private partnership ("P3") project agreements in Canada contain a litany of supervening event types and formulations, as well as emergency and change in law provisions, that are significantly more detailed than CCDC standards used for construction projects. Nonetheless, very few project agreements expressly grant any form of relief during a pandemic or epidemic event, while others are ambiguous as to how such events are treated. As a result, private partners are struggling to make sense of their performance obligations in the middle of the COVID-19 crisis, which could potentially leave them liable for delays, cost overruns and service deductions. At the same time, private partners are having to reconcile such contractual obligations against their legal, civic and corporate social responsibilities relating to health and safety, particularly with respect to social distancing and isolation measures.

The COVID-19 crisis has prompted P3 participants to explore ways to address the challenges currently facing the industry,^[1] but it is also a stark reminder that a recalibration of P3 risk allocation is required going forward. The public sector should expressly assume the broader risks associated with outbreaks of disease, pandemics and epidemics more generally. At the same time, private partners can be asked to take on certain quantifiable and controllable risks associated with future pandemic events where such risks (or risk assumptions) are identified and specified at the initiation of the procurement process.

Allocating the Risk

As is evident in the name, P3s represent a "partnership" between the public sector authority and the private sector partner. Central to all P3 arrangements is a contractual allocation of risks and liabilities to the party best able to manage them efficiently and effectively.^[2] Project agreements are structured around the premise that private partners take on project execution and similar quantifiable risks, while the procuring authority takes (or shares) the risk of delays (and sometimes costs) due to events that are not in the private partner's control, not quantifiable, or not insurable. It is critical that project risks are appropriately identified and allocated among the parties to encourage efficient pricing and value for money. A project agreement which does not allocate the risks appropriately can result in project failure or drive up overall costs of the project, which are in turn passed on to taxpayers.

As such, almost all P3 project agreements contemplate, at a minimum, certain force majeure events (e.g., war, terrorism, embargos, and similar acts of God) that entitle the private partner to some form of limited relief. Yet most project agreements exclude outbreaks of disease, pandemics and epidemics from their finite list of supervening events, notwithstanding that such events are also outside of the private partner's control and are neither quantifiable nor insurable.

COVID-19 has provided the market with a glimpse of how a pandemic event can affect the private sector. It can lead to unpredictable and varying government restrictions, labour shortages, financial market volatility and supply disruptions. It affects the industry indiscriminately and in most cases, the private sector is unable to meaningfully mitigate these impacts. The effects of COVID-19 are unquantifiable, unforeseeable, uninsurable and cannot be differentially mitigated by industry participants – a bona fide supervening event. Asking the private sector to price these kinds of risks does not support the spirit of risk allocation upon which P3 contracts are based, and does not adhere to the value for money principle that the P3 model strives to achieve. As such, the risk of disease outbreaks, pandemics and epidemics, like other supervening events which already exist in project agreements, should be borne by the public sector. The private partner should be entitled to relief to the extent such events demonstrably increase costs, impact progress or interrupt performance under the Project.

This is not to say that there is no opportunity for some risk sharing between the parties. Specific events which may be incidental to the pandemic event itself and that are quantifiable and controllable can be allocated to the private partner and, with the right assumptions and parameters, produce accurate and tightened pricing during the bidding process. Based on the lessons learned from COVID-19, there is potential to develop more specific and detailed frameworks for dealing with, and allowing bidders to evaluate and price, certain aspects of health and safety and pandemic management planning that may become permanent or recurring features of the industry. Where such risks (or risk assumptions) are identified and specified at the initiation of the procurement process, the private partner is better able to price and bear such risks.

Structuring the Relief

Relief with respect to outbreaks of disease, pandemics and epidemics cannot be narrowed to the incidence, spread or location of the virus. The COVID-19 crisis has shown that measures taken by governments and the general public to control and minimize the effects of the virus can be more disruptive than the illness caused by the virus itself. The general fear and anxiety in the general public and the labour force, manufacturing shut-downs throughout the world, closure of international and interprovincial borders, and governmental orders, guidelines and directives all contribute to slowing down construction or maintenance performance activities, cause labour shortages and disrupt the supply chain.

Supervening event relief should address all such correlated factors to ensure a fair and reasonable allocation of

risk:

- Project documents must include better appreciation for the multi-tiered nature of global catastrophes like pandemics and epidemics. For example, a shutdown in one jurisdiction can have significant effects on the supply of materials, equipment and labour for a project in a different jurisdiction. Existing project agreements (and even many procuring authorities who are exploring relief measures for pandemics in future project agreements) often ignore the consequences of a global, highly-integrated supply chain and the relationships between local, national and international project participants.
- At minimum, relief should cover an extension of time for delay during the construction period and no incurrence of service failure deductions during the operating period.
- Relief should include payment of the private partner's direct costs as well as accrued debt service and foregone equity distributions. This is particularly important to ensure pricing efficiency and bankability of projects which are contemplated to close during an ongoing supervening event.

Again, there is some potential for risk sharing in the relief framework as well. For example, certain risk sharing mechanisms such as cost allowances can be utilized, concurrently with express supervening event relief, for contingent events and their consequences, allowing the participants the necessary flexibility in balancing productivity with health and safety measures.

Looking Beyond Pandemics and Epidemics

Aside from the immediate need to address COVID-19 impacts in ongoing procurements, it is important for the P3 industry to clarify contractual language for future procurements to deal specifically with similar global and local supervening events. The COVID-19 crisis has accelerated and brought to the forefront issues related to risk allocation that have been lingering under the surface for quite some time. As projects in the Canadian market have become more complex and larger over time, disputes over material claims have risen, and many private sector participants have voiced concerns over a trend towards shifting more and more risk to the private sector.^[3] As the P3 industry works together to balance the interests of its stakeholders in light of the COVID-19 crisis, they should seize the opportunity to collaboratively assess the existing risk allocation model, using the lessons learned and the benefit of current experience.

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[1] See, e.g., Tim Murphy and Drew Fagan, "[Canada's Infrastructure Bank: An Opportunity to Step Up and Rebuild Canada's Post-Pandemic Economy](#)" McMillan Vantage Policy Group Bulletin (May 6, 2020).^[ps2id id='1' target='']

[2] Timothy J. Murphy, *Public-Private Partnerships in Canada: Law, Policy and Value for Money* (Toronto:

LexisNexis Canada, 2019) p. 143.[ps2id id='2' target='']

[3] See, e.g., Lucy Saddleton, "[Contractors call for changes to P3 model to address issue of risk transfer](#)", The Canadian Lawyer Magazine (5 March 2020).[ps2id id='3' target='']

a cautionary note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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