

# MUNICIPAL P3s

The challenge of building a municipal constituency.

By Tim Murphy

The evolution of public-private partnerships (P3s) in the Canadian political environment has been nothing short of astounding. Just a few years ago, the P3 model was vilified and campaigned against. Now, it is fast becoming the default choice for procuring infrastructure projects in many jurisdictions.

That said, the battle hasn't been won yet.

The federal government's recent fiscal update outlined its plan to start applying a P3 screen to its infrastructure developments. Reports out of Ottawa suggest that it wisely intends to establish a P3 office inside the government to ensure that the policy gets implemented.

At the provincial level, B.C. has enthusiastically embraced P3s, with Partnerships BC having brought a number of projects to financial close in recent years. B.C. Premier Gordon Campbell recently announced that his government would ensure that every project over \$20 million is assessed from the perspective of looking to the private sector as a potential partner. Significantly, the B.C. provincial auditor broke through the normal reticence on P3s to report that the Sea to Sky highway project saved taxpayers money by using the P3 model.

Ontario's largely-successful experiment with Infrastructure Ontario has laid the groundwork for a major expansion of what Ontario calls Alternative Financing and Procurement (AFP) after a rocky road through the last election. A set of principles has been established to guide AFPs, which state that public interest is paramount, projects must demonstrate value for money, appropriate public control and ownership must be preserved, accountability must be sustained, and all processes related to the project must be fair, transparent and efficient. Ontario is looking at infrastructure as a crucial tool for the province's economic development and is eyeing with some interest the pools of pension money interested in helping.

Quebec has also ventured along this route, recently announcing P3 initiatives for hospitals and highways. While this may be unsurprising from a government lead by Premier Jean Charest, it builds on an act to both encourage and channel P3s passed by the previous Parti Quebecois government.

There is one level of government however, with few exceptions, that has not caught the P3 bug – municipalities. Looking at everything from public transit to waste water to roads to hockey rinks, Canada's cities and towns are the last bastion of bureaucratic procurement.

This is in part because the experience of a number of municipalities has not been pleasant. The head of the Federation of Canadian Municipalities, Gloria Kovach, provides a sobering example. At a

recent conference, she described how she couldn't sell the P3 idea after a local disaster on a project.

Second, municipalities often lack the expertise or the depth to negotiate and deal with the private sector players across the table. While the city of Ottawa, for example, has very successfully established a P3 office and has a number of innovative projects under its belt, it is the exception. Toronto, for example, has largely eschewed this method of delivering public services.

Third, a number of unions that are opposed to the idea find their greatest source of power at the municipal level. As a result, many municipal politicians unsurprisingly do not want to stick their necks out to support a model that may have powerful local unions focus their energies on defeating them. (That said, there are some very supportive unions – including some that have their own pension funds – engaged in financing public-sector development.)

The challenge of building a municipal constituency for P3s is a crucial one. Bad municipal experiments could poison the well for the other levels of government. If cities and towns don't get it right, public opinion could turn against this model of delivering public infrastructure. However, there is an opportunity to turn the experience around on the horizon.

All governments, municipal in particular, are looking at the new accounting standards that the Public Sector Accounting Board has instituted and which take effect on January 1, 2009. These new

standards will obligate municipalities to report on the full accrual cost accounting of their capital assets. As a result, we will get a good handle on the size and scope of the infrastructure deficit.

These rules also create opportunity. If councils view their capital assets through the lens of what generates a revenue stream, each asset – and its replacement over time – can be assessed from the perspective of how private sector money can be used to refurbish and rebuild it.

To make this work, city and town officials need help – the kind of experience that has been built up in Infrastructure Ontario and

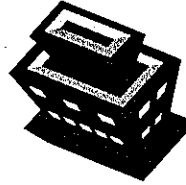
Partnerships BC, for example. Most municipalities face a steep learning curve on things such as RFP procurement design, selecting among various P3 models (build/finance, design/build/finance, design/build/finance/operate) and developing optimal allocations of project risks between the public and private sector. However, municipalities should also be able to benefit from the experience acquired in their sector to date.

Experienced firms have seen benefits; transaction costs associated with P3s decrease as lawyers, technical advisors and other participants become experienced with the P3 model. Negotiations are more focused as project, construction and service agreements become standard.

Second, partners are now better able to allocate the risks and manage the timing associated with the projects.

Third, familiarity with the process and increasingly-standardized project documentation is reducing the time from project inception

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to completion. Finally, Infrastructure Ontario, for example, has shown a willingness to discuss project risk allocation with private-sector participants, including members of the financial community, and has in a number of cases reflected this in project documentation. This has resulted in more readily-financeable projects and, with very large pools of capital available in the major pension funds in Canada and elsewhere interested in these projects, financing costs and hence the cost to government, should drop over time.

Action now through the leadership of the provincial government should create a new opportunity for the next wave of P3 development. There is much opportunity for municipalities to leverage the experience of entities such as Infrastructure Ontario and Partnerships BC and take advantage of the efficiencies so that municipal P3 projects can be brought to market sooner, and on terms that have already gained a level of market acceptability. The departments of finance, municipal affairs and infrastructure renewal, in cooperation with the Association of Municipalities of Ontario (AMO) should build on the fall's Infrastructure Forum and create a similar forum for city and town officials. Looking ahead, AMO could even act as a central purchasing agent for municipalities, greatly reducing both risks and costs.

With smart leadership now taking advantage of growing experience and large pools of eager capital, Ontario and Canada should see an infrastructure boom for the next decade. We fought and beat the federal government deficit and there is no reason to believe we cannot do the same for the infrastructure deficit. ♣

Tim Murphy is a partner at McMillan Binch Mendelsohn LLP in its Infrastructure and P3 practice.

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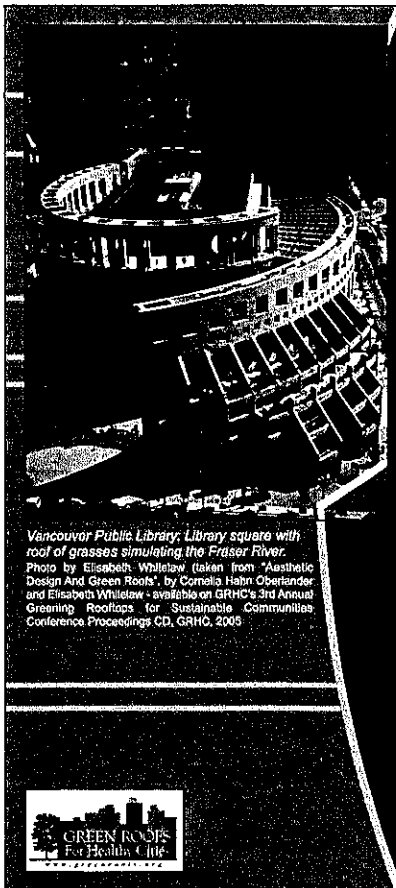
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Vancouver Public Library: Library square with roof of grasses simulating the Fraser River.  
 Photo by Elisabeth Whitlew (taken from "Aesthetic Design And Green Roofs", by Cornelia Hahn Oberlander and Elisabeth Whitlew - available on GRHC's 3rd Annual Greening Rooftops for Sustainable Communities Conference Proceedings CD, GRHO, 2005)

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