legal notes

P3s and the procurement process

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THE TERM "PUBLIC-PRIVATE partnership" (P3) describes any cooperative venture involving a public sector buyer and a private sector participant in the provision of a public service, the provision or operation of capital assets for public uses, and the financing of public ventures. P3s involve an allocation of the risks associated with the venture between the public and private sector partners. Key to success is the transfer of individual risk to the partner best able to absorb and mitigate it. Too often little thought is given to the most efficient method of risk allocation when creating P3 ventures.

P3s can be categorized referencing the extent of public and private sector involvement, the degree of risk assumed by each party, or the type of responsibility that each party assumes. The last method of classification provides a clear illustration of the many forms of P3s. Others include:

- Contracts for operation and management of capital assets.
- Contracts for the design, building and operation of capital facilities. The public partner provides the financing; the private partner builds and operates the facility and assumes all other aspects of ownership, getting the advantage of lower cost of funds. The public benefit might be a more experienced builder and operator for the facility.
- Contracts for the financing, designing, building and operating capital facilities.
- Sale and leaseback arrangements, which allow the public partner to free up the equity invested in its capital assets and divert the proceeds generated to some other public purpose while retaining use of the asset through the lease.
- Pooling and splitting of common costs. For instance, if a municipality needs a new City Hall and a major business needs a new head office, they may reduce their combined cost of building by consolidating both their requirements into a single building and splitting the cost.
- Revenue generation. Suppose a municipality enters into a lease with a golf course operator to build and operate a golf club on surplus municipal land. The municipality derives a revenue stream from the income thereby generated. If the land goes up in value over the term of the lease, then there is further upside potential.
- Facility expansion. For instance, a municipality may wish to include a parking garage in a new public building and it also wishes to increase the available parking in an area of town. So, the municipality considers over-building the parking facility and offering the surplus parking to the operator of a nearby private sector building.

In principle, a successful P3 builds on the experience and expertise of each partner to meet a clearly defined public need on a more efficient basis than is possible through traditional service delivery. In many P3 arrangements, the municipality may have little involvement in its day-to-day operation. Standards for operation will be set out in the terms of the lease or other agreement with the P3 partner. Provided the operator meets those standards, it essentially has free rein.

However, if government is funding (in whole or in part) the provision of a public service, taxpayers will likely expect that any purchase or other procurement of goods or services in relation to that public service will be conducted in accordance with the same principles of "open, fair and transparent" purchasing that characterizes the public sector. This could lead to problems:

- There can be difficulties in reconciling the P3 approach with the normal standards applicable to government procurement, e.g., the open tender process.
- There may be reluctance from the private sector entities regarding the disclosure of information about their activities. The potential impact of the *Municipal Freedom of Information and Protection of Privacy Act* should be clarified and understood before the agreement is reached.
- The public sector approach does not necessarily result in minimized cost and thus there is a substantial risk to any profit potential for the private sector partner.
- If the private sector partner is left in charge of procurement, its buyers may be unaware of the considerable differences that exist in the way in which public and private facilities are operated (e.g., open access to public facilities). Clear protocols must be in place to ensure public standards apply.

Using a P3 approach requires thorough consideration of all implications. Often an RFP will be issued without sufficient preparation work, such as determining local demand, or consideration of alternative ownership options.

Sometimes, the P3 approach may not be viable. Take the construction of a new City Hall as an example. In principle, there are advantages to locating certain types of private sector offices in the same building as government offices. However, if there is surplus office space in the municipality, rents for existing space are likely to be low making it unlikely that there will be many takers for space in a new City Hall. As well, concerns could extend into the areas of compatibility of use and shared expectations relating to utilization. Where a municipality proposes to lease an office building as its City Hall, it is likely to find that a standard commercial lease contains dozens of provisions that are inconsistent with the practical working requirements of a legislative building. Public authorities need a considerable degree of control over the type of business that locates within the same premises. A proposed private sector partner may not understand this sort of concern.

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