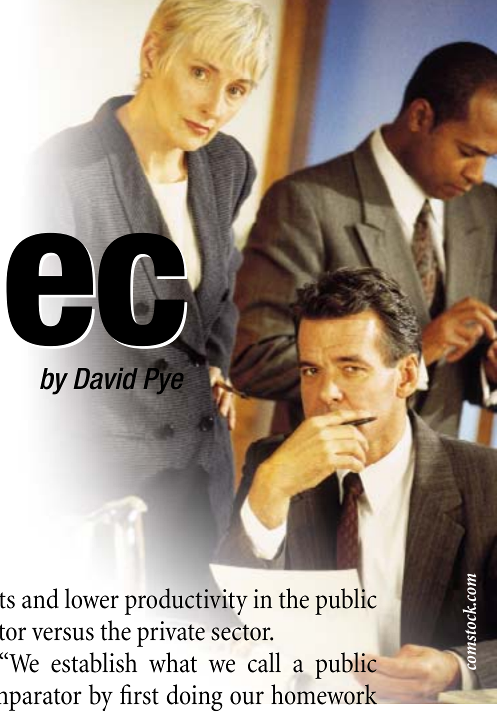
P3s à la Québec



by David Pye

Quebec cautiously approaches public-private partnerships

On December 15, 2004, the Quebec Liberal government passed *Bill 61* – an *Act* respecting the Agence des partenariats public-privé du Québec (Quebec Public-Private Partnership Agency) – marking the province's formal if cautious entry into the world of P3s. Quebec is determined to apply due diligence to every piece of the P3 puzzle.

"It will evolve over time. We've identified several decisional steps and have established a policy framework and a business guide to help the various ministries identify potential projects," says Pierre Lefebvre, CEO of the agency. "We're looking at public-private partnerships as one of many tools in the shed that can deliver infrastructure to underpin public services."

On April 18, 2005, a handful of P3 projects were tabled by Quebec's Treasury Board president Monique Jerome-Forget, including two Montreal university hospital projects valued at $1 billion each and the construction and maintenance of two major toll highways. The proposed construction of the Balmoral cultural complex – a facility that will house the Montreal Symphony Orchestra and a new music and dramatic arts conservatory – has also been identified as a potential P3 project.

The province's approach to P3s places a strong emphasis on public awareness, including consultations with labour organizations in a province boasting the highest rate of unionized workers in North America. The process includes contingencies for the public filing of all documents signed with private partners, as well as the appointment of a process auditor (often referred to as fairness monitors/commissioners/supervisors) to oversee the implementation of P3 procedures. *Bill 61* also dictates that all P3s will generate in-depth public reports explaining why the government found it advantageous to enter into the agreement in the first place.

The P3 process begins with a request for qualifications (RFQ), where potential bidders must establish their credibility and demonstrate their ability to deliver. Then the Quebec government sends qualified bidders a request for proposal (RFP) that provides a detailed explanation of the project and its deliverables.

"We use the RFQ – an assessment of operational abilities, experience and financial solidity – to identify the top three or four bidders," explains Lefebvre. "Then we send them a draft RFP and concession agreement and organize a series of multilateral meetings, as well as bilateral meetings with each of them."

According to Sylvain Vincent, managing partner of the Transaction Advisory Services Group of Ernst & Young, international studies show that P3s have a higher tendency to meet cost estimates than do conventional public sector projects. Recent studies in the UK suggest that 80 percent of public sector projects are delivered late, resulting in serious cost overruns and other secondary effects caused by a failure to deliver.

"The ultimate goal of P3s is to improve the quality of services to the population and to provide taxpayers with a good return on their tax dollars," says Vincent. "Generally speaking, going with the private sector should provide some cost savings."

Analyzing those savings isn't as simple as comparing bottom line capital costs however. Several risk factors weigh in on the equation, including long-term maintenance expenditures, fluctuating material costs and lower productivity in the public sector versus the private sector.

"We establish what we call a public comparator by first doing our homework to assess what we feel a project would cost to build and operate," explains Lefebvre. "Then we compare our internal assessment to the bids, not only in terms of quantity, but also from a quality point of view."

As an example of the price-quality analysis, Lefebvre explains that while the government might table a project to construct a 100 square foot building at a cost of $1,000, a qualified bidder from the private sector may propose a 200 square foot building at a cost of $1,100. While entering into the agreement means a capital cost increase of 10 percent, the return on investment will be double.

"The goal is not to arrive at the cheapest building, but rather to arrive at a solution that makes the most sense from a price-quality perspective," says Lefebvre. "It's about maximizing the return on capital expenditures without ever sacrificing quality."

But straight forward financials are only one piece of the P3 pie. Not only do cost overruns result in capital losses, but they can also trigger ripple effects with negative values. A case in point is the extension of Montreal's subway service into the city of Laval – a public sector project that has incurred dramatic cost overruns. Since assessing the initial cost at an amount not exceeding $179 million, the project budget has been increased to $547 million – some observers claim it could go as high as $800 million. In addition to the current capital cost overrun, there are hidden costs associated with such things as additional wear and tear on roads linking the two cities.

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"In the case of P3s, the private sector partner assumes responsibility for cost overrun, which is a risk that the government is transferring," explains Vincent. "The private sector partner faces penalties for late delivery and usually must answer to shareholders, bankers, etc."

The transfer of risk, is an integral part of the overall equation and can include factors such as maintenance cost increases due to rising prices. P3s put that risk in the hands of the private sector, while allowing the government to dictate quality standards that must be met. Another risk factor is the cost of long-term maintenance – an expenditure that tends to fluctuate dramatically in the public sector due to budgetary constraints.

"Governments rarely have enough money when it comes to road maintenance, so the thinking is always short-term," explains Vincent. "The private sector will tend to use higher quality materials and careful techniques to ensure the durability of a project for the next 20-30 years."

Lefebvre agrees that conventional public sector projects tend to over-focus on capital costs, making risk transfer to the private sector a logical choice.

"If a government spends hundreds of millions of dollars building infrastructure, it's rational to assume that they should guarantee that the asset will be maintained properly," he says. "With a [P3] not only can we contract for the capital cost of the asset, but also for maintenance throughout its useful life."

For now, the province is approaching P3s as the exception rather than the rule, using case studies from the UK and British Columbia (which is pushing ahead with P3s) as benchmarks. They have established a policy infrastructure that paves the way for the various government ministries to get on board, but it may take some time before potential projects are identified. In the meantime, the Quebec government is inching forward with its initial slate of P3 projects, taking time to ensure that the process is properly structured.

"It's not a case of the government encouraging as many [P3s] as possible," says Lefebvre. "The procedures will only be implemented in cases where the ministries have identified projects as being practical and relevant to the P3 process."

The Quebec government has earmarked $20 billion in capital expenditures for infrastructure projects over the next ten years, including the construction of a new prison facility and the revamping of the province's long-term care facilities. Many of the proposed projects may not be a P3, but Vincent says, "I think that the Province of Quebec is doing quite well, given the circumstances. P3s are new to the Quebec population – they have been in effect for at least a decade in the UK – therefore the government wants to move very slowly to be sure that the public understands what it is all about."

David Pye is a freelance journalist based in Montreal.