SUMMIT
CANADA'S MAGAZINE ON PUBLIC SECTOR PURCHASING

The role of advisors in successful P3s

by John Chenery

www.jupiterimages.com

As governments at all levels increasingly look to partnerships with the private sector to deliver public infrastructure and services, the impacts are rippling throughout Canada's business, legal and financial communities. Among the growth industries generated by the move to public-private partnerships (P3s) is a group of specialists variously known as "process advisers," "transaction advisers" or in some cases "P3 advisers."

P3S ARE OFTEN large, invariably complex deals that tend to require substantial input from consultants on both the owner's and the bidder's side of the deal table. The list of participants in any given P3 negotiation can include legal, financial, business and tax advisers, experts in engineering/design (in the case of construction projects) and tolling (for roads) environmental and communications consultants, and the ever-present fairness monitor to make sure everyone gets a fair shake.

While more and more private sector partners now engage independent process advisers, it is public sector transaction advisers who have the most input and impact on the transaction and provide the glue that holds these big, complicated processes together. Their work starts during the project's initial modeling stage and continues until, and usually beyond, financial close.

Partnerships BC, the government-owned organization that runs that province's hugely successful P3 program, is a big believer in the value added by transaction advisers. Sarah Clark, vice-president, Partnerships Development and Delivery, says that every Partnerships BC project includes an independent transaction adviser.

"We rely on them for their financial expertise, their negotiating expertise, their exposure to other P3s around the world and their knowledge of different deals that we have not been exposed to. We also use them in setting up and completing our bid evaluations, they assist with strategy and with the development of the concession agreement – the whole gamut really."

P3 specialist Robin Johnston, principal of the Vancouver-based technical management consulting firm Collings Johnston Inc., says that although the transaction adviser's role is changing as the market matures, some things will never change.

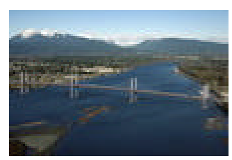
"No matter how many deals we do, how similar they might be and how much progress we make in standardizing the documents and the process, there will never be a cookie-cutter approach," he says. "Every deal is different – with partners who have different expectations and requirements and projects that present different challenges and opportunities.

"The transaction adviser's role is to somehow bring all these different elements together, get the legal and financial teams from both sides around the table and just beat the thing to death until you end up with a package that is marketable."

...it is public sector transaction advisers who have the most input and impact on the transaction and provide the glue that holds these big complicated processes together.

For the transaction adviser, the "beating to death" process usually begins when the project is still a twinkle in the owner's eye, as happened when Johnston's company was hired as technical manager on the $1.1 billion Golden Ears Bridge project (slated to open June 14, 2009) east of Vancouver. "We started on Golden Ears in 2002 with the owner TransLink saying, "We don't know what it is or what it will look like, we just know we need a crossing [over the Fraser River] and we want a P3 of some kind."

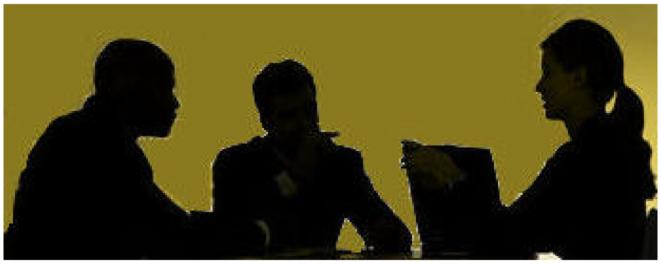
Johnston's role at that early stage was to look at the big picture, working with TransLink and Partnerships BC as they considered the various P3 models and risk transfer options, determining which ones could best serve the purpose and then investigating the costs and affordability of those schemes, based on projected traffic demand and toll revenue modeling.



To learn more about the Golden Ears Bridge project: www.goldenearsbridge.ca

They eventually settled on a design-build-finance-operation (DBFO) delivery model for the design, construction, financing, operation, maintenance and rehabilitation of the bridge and service roads with a separate design-build-operate-maintain (DBMO) contract for the tolling system. One of the unusual features of the Golden Ears deal was TransLink's decision to retain the toll revenue risk and pay the developer from those revenues.

The transfer of project risk to the partner most likely to manage it effectively is one of the cornerstones of the public-private partnership delivery model – no risk transfer, no P3. Yet it remains one of the main areas of contention in negotiations between government departments and agencies and the companies and consortia that bid on P3 offerings.



"Unfortunately, governments aren't always on board with the risk transfer idea," says Johanne Mullen, senior vice-president and director for the Advisory Services Group of PricewaterhouseCoopers at the Montreal office. "They think that the objective of a P3 is to get the private sector to take all the risks.

Ultimately, that has proved to be inefficient. As an independent adviser having worked on both bid-side mandates and with the private sector, our role is to ensure that what is being brought to the market for the private sector to bid on is what we call 'market standard.' So we are trying not to push risks on to the private sector or incorporate terms and conditions that will end up costing the government more in the long run."

Mullen cites archaeological risk – the chance of delays caused by the discovery of ancient artifacts on a construction site – as a classic example of a risk that should be retained by the government. "If we ask a private partner to take that risk, they will need to price a buffer into the overall cost of the project because they have no way of predicting what the significance of that risk could be. So we would always advise governments to take that risk because they are better able to control it."

For Mullen, the risk transfer issue is closely linked to another key aspect of the P3 delivery model that continues to be a hurdle in negotiations – performance-based contracts with the overriding focus on outcomes.

"When we get down to discussing the details of the contract," she says, "some people in government expect to see thousands of pages of specifications and what they get instead is a few dozen pages of synthesized information that simply articulates the objectives. For example, we don't specify exactly how we want a room built – the number and size of bolts in each wall, the number of light bulbs and how many watts – but we do specify that the room must meet exact standards, for soundproofing, lighting, humidity and so on.

"As you can imagine, this can cause a tremendous amount of unease for governments, and the architects and engineers they hire to advise them. It's a steep learning curve and it's a big part of my job – making everyone feel comfortable about the focus on performance and outcomes and pointing to examples where it has worked in other jurisdictions."

On her current project, Mullen even went to the trouble of bringing in some architects and compliance engineers from BC to explain to their Quebec counterparts how the process is working out west, the successes achieved, lessons learned and to provide guidance on adapting to the new way of doing things.

"It has been an interesting exercise," she said. "The professionals from BC told me that it had taken more than a year to get comfortable with the new approach, but I am noticing that on my current project, the professionals are moving along in their thinking far more quickly. Success breeds success and as the deal flow increases and more projects are completed everyone's comfort level will increase greatly."

Robin Johnston gives Partnerships BC a lot of the credit for the solid progress that has been achieved in his part of the world. "They've done a good job educating their public sector clients that they can't just dump every risk on the other side of the table and that if you do, then the project will be considerably more expensive than it needs to be. The public sector is much more willing to accept that logic now."

Sarah Clark of Partnerships BC agrees and believes that as more deals get done, the deal-making gets easier. "The overall process and roles haven't changed significantly, but it doesn't take as much time," she says. "A lot of our clients are now on their second or third transaction so people are used to how the concession system works and a lot of the basics have been covered."

But, says Clark, no matter how many projects are completed successfully, the next deal coming down the pike will have nuances and features that no one has had to deal with before. "We can streamline the process but there will never be a one-size-fits-all approach," she says. "That's why we will always need the experience and expertise of independent advisers who have been exposed to many different kinds of projects in different parts of Canada and overseas."

John Chenery is a consultant to The Canadian Council for Public-Private Partnerships.