UNIVERSITY OF TORONTO
Department of Geography
and Programme in Planning

100 St. George St. Room 5047
Toronto, Ontario Canada
M6G 3S3
Telephone: (416) 978 3375
Fax: (416) 946 3886

April 4, 2014

Committee on Transportation and Infrastructure
U.S. House of Representatives Testimony
April 8, 2014

Context

In recent years, public-private partnerships (PPPs) in Canada have received considerable international attention as a model that could be emulated abroad. There are some good reasons for this attention. Canada now has an active marketplace and established track record planning and delivering infrastructure PPPs. The current approach to PPPs in Canada can be dated to the mid 2000s, and primarily involves hospitals and health care facilities, followed by transportation infrastructure, prisons and courthouses, waste and water treatment assets, and education buildings. On projects delivered since the mid 2000s, Canadian PPPs have a strong reported record of projects coming in on-time and on budget; and to date there have been few of the forced contract renegotiations, public buyouts of failing projects, or outright project bankruptcies that have occurred with PPPs globally.

Key Success Factors

The success of the recent Canadian PPP approach lies in the application of partnership models that seek to leverage the comparative strengths of the public and private sector partners, and assign risks and responsibilities to the partner that is best able to manage them. This contrasts with PPP practices that are more explicitly designed to reduce the role of government and privatize infrastructure planning and provision. The Canadian approach to PPPs has a number of specific characteristics that contribute to its success.

First, in Canadian PPPs, government retains a significant role in identifying project priorities, developing performance specifications for projects that meet the public interest, and typically owning the underlying asset throughout the operating concession period. As well, PPPs in Canada are not seen as a one size fits all model where the same partnership approach must be used for all projects. Rather, various models of partnership and concession bundling have been selected for use depending on the characteristics of the project. This ranges from design-build-

finance type contracts where all private investment is repaid following the substantial completion of construction, to design-build-finance-maintain and design-build-finance-operate-maintain type deals that include long-term concessions lasting anywhere from 25-50 years.

Second, Canadian jurisdictions have set up special purpose agencies with the sole responsibility of evaluating the merits of PPPs for specific projects and procuring PPPs. These agencies are staffed with highly skilled procurement experts that have the experience to structure and manage complex deals. The agencies have also developed standardized procurement processes, bid documents and legal contracts that can speed up procurement and make the market more transparent, predictable and attractive to prospective bidders.

Third, PPPs are not being widely used as a way for cash strapped governments to raise new money for much needed public infrastructure. The overwhelming majority of PPPs in Canada do not include new user fees or other types of revenue raising tools that can directly repay all of the private sector capital investment and operating costs on the project. This is even the case in the highway sector, where tolls have been more common internationally. Rather PPPs are primarily a financing mechanism not a funding strategy, with initial private sector capital investment and operating costs repaid through government sponsored availability payments. The continued public investment in PPP projects means that Canadian governments can use PPPs to deliver all types of infrastructure that meet the public interest, rather than only a narrower range of projects that are able to recover their own costs through user fees.

Fourth, since Canadian PPPs are not primarily being driven by the objective of raising new private money for infrastructure, instead the leading motivation is achieving value for money. It is proposed that the public value of using PPPs is driven by a number of factors, including the realization of private-sector led innovation through the PPP procurement process; ensuring appropriate construction and project maintenance over a long-term operating period by only paying for performance; and perhaps most significantly, transferring project risks from the public to the private sector partner. To date, Canadian PPPs have focused primarily on transferring construction and asset availability risks to the private sector concessionaire, in an attempt to stem the trend of infrastructure mega-projects being plagued by endemic cost overruns and delays. Conversely, Canadian governments have commonly retained demand and revenue risks. By retaining demand and revenue risk, Canadian governments have been able to focus on integrating PPP infrastructure into the wider community, and reduce a common source of tension between the partners on PPPs internationally.[1]

Outstanding Issues with PPPs

Despite the identified strengths with Canadian PPPs, there remain some outstanding questions regarding their overall merits. First relates to the question of whether PPPs actually deliver value for money as compared to traditional project delivery and government financing. Based on a study that I conducted with Naeem Farooqi of government produced cost estimates of 28 Ontario PPP projects worth $7 billion, we found that PPPs have risk free base costs that are on average

[1] For a more thorough discussion of the impacts of transferring demand risk, see Siemiatycki, M. and Friedman, J. (2012). The Trade-offs of Transferring Traffic Demand Risk on Transit Public-Private Partnerships. Public Works Management and Policy, 17:2, 283-302.

16 per cent more than a comparable project would cost using conventional tendered contracts.[2] This is mainly because private borrowers typically have higher financing costs than governments. Transaction costs for lawyers, consultants, management costs and project monitoring also add 2-5 per cent to the final cost. And the private sector concessionaire charges a premium on facility construction and operations in order to take on the added risk of events that could lead to rising costs that would be their responsibility. A more detailed breakdown of estimated project costs and revenues for PPPs and a comparable traditionally procured project is provided for a sample of Canadian infrastructure assets below.

	Durham Courthouse, Ontario[3]		**Chief Peguis Trail, Manitoba[4]**		**Canada Rapid Transit Line, British Columbia[5]**	
	Traditional	PPP	Traditional	PPP	Traditional	PPP
Base Costs (CapEx/OpEx)	247	334	105.5	127.9	1,822	1959
Transaction/ Admin Costs	8	17	6.2	3.5	98	120
Financing Cost Premium	N/A	N/A	N/A	N/A	0	130
Revenue	N/A	N/A	N/A	N/A	(433)	(581)
Risk-Free Project Cost	**255**	**351**	**110.98**	**131.34**	**1,487**	**1,628**
Retained Risk By Government	157	25	67.8	16.4	263	30
Risk Adjusted Project Cost	412	376	178.78	147.8	1,750	1,658

In these comparative evaluations of PPPs and traditional procurement models, it can be seen that it is only after calculations of estimated risk retained by the government associated with each procurement model is considered that PPPs are assessed as providing better value than traditional procurement alternatives. Yet the 'risk premiums' assigned to the traditional procurement option when Canadian governments carry out *ex ante* value for money assessments have varied in size and sometimes been very high. For instance, the average risk premium added to the conventional procurement model in my study of 28 PPP projects in Ontario was 49% of the risk free base cost, making the PPP the better value on paper in every case examined. There is no publicly available empirical evidence that shows that this is the likely amount of risk based on past conventionally delivered projects. While it is advantageous to have cost certainty in project delivery, both politically and from a policy perspective, it appears that Canadian governments are paying a high price to achieve this in the absence of empirical evidence that can be publicly verified.

[2] Siemiatycki, M. and Farooqi, N. (2012). Infrastructure Public-Private Partnerships: Delivering Value for Money? Journal of the American Planning Association, 78:3, 283-299.
[3] Infrastructure Ontario. (2007). Value for Money Assessment Durham Consolidated Courthouse. Retrieved March 5, 2014, from http://www.infrastructureontario.ca/What-We-Do/Projects/Project-Profiles/Durham-Region-Courthouse/
[4] Deloitte and Touche. (2011). Chief Peguis Trail Extension Project Value for Money Report. Retrieved June 7, 2013, from http://www.winnipeg.ca/publicworks/MajorProjects/ChiefPeguisTrail/PDF/2011-11-25-CPTEP-ProjectReportFinal.pdf
[5] CLRT. (2006). Canada Line Final Project Report. Retrieved June 7, 2013, from http://www.partnershipsbc.ca/files-4/documents/Canada-Line-Final-Project-Report_12April2006.pdf

There are other concerns that my research has identified with Canadian PPPs that I would like to briefly highlight. First, public accountability and engagement in decision making can be problematic during PPPs. Commercial confidentiality is often invoked to protect the integrity of the bidding process of the PPP procurement, and the capacity of the government partner to negotiate the best deal. This has made it difficult for members of the public to meaningfully assess the merits and trade-offs of projects in their communities while they are being planned.

Second, PPPs can be accompanied by a loss of public policy flexibility, even when the public sector partner retains demand and revenue risk. In cases where PPPs involve long-term concession agreements of anywhere from 25-99 years, this can lock in future public policy decisions. In particular, it can become difficult or costly to make changes to the facility structure or programing in the future, regardless of shifting community needs or the advent of new unforeseen technologies.

Third, there have been questions about whether PPPs are being presented as the 'only game in town' for governments of all level seeking to realize their infrastructure projects. In Canada, some agencies and municipal governments feel that they will not receive federal or provincial funding for their infrastructure projects unless they are structured as PPPs as opposed to other procurement alternatives. This is problematic because PPPs may deliver value in some setting but not others, and the choice of procurement model should be based on a project-by-project assessment.

Fourth, despite the important emphasis placed on PPPs as a driver of innovation, it is often unclear what improved innovations and efficiencies have been realized through the PPP procurement process, and whether these actually deliver public value. The value for money reports produced to assess the merits of each project do not commonly identify the specific innovations that were generated through the PPP procurement process, and how much savings or social benefit they deliver. Moreover, there are questions about whether similar innovations could be identified through a competitive design-build procurement process that involves the same private design and construction firms as when projects are delivered through bundled PPPs.

Conclusion

In sum, I see PPPs as a tool for delivering large-scale infrastructure projects, when appropriately designed and used in the appropriate settings. The key is determining in what settings PPPs make sense, and when traditional procurement or other alternative approaches should be used to provide better value. To enable such assessments, it is critical that United States policy makers have rigorous data on the frequency and magnitude of risk events on past infrastructure projects, specific project innovations that have been developed through PPPs, and the extent to which PPP procurements meet the public interest for transparency, community engagement in decision making, and long-term flexibility. As more PPP projects move through the delivery process and into operations, there is now a growing evidence base that policy makers and practitioners can draw on to learn the lessons from past experience, and tailor the next generation of PPP delivery to ensure that it delivers public value.