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Government and contractors are working together to examine the future of public/private partnerships in Alberta

Public authorities throughout the world are increasingly looking to the private sector to finance, construct and maintain assets. The broad spectrum of potential opportunities for public/private sector joint ventures and partnerships has spawned an equally broad array of contractual and business models. This contracting out takes many forms and is in place for toll roads and bridges, lease-back arrangements on government office buildings and the operation of health centers, educational institutes, waste disposal facilities, penal institutions and airports, to name some examples.

Construction is Alberta's fourth largest industry. In 2008, it accounted for eight per cent of Alberta's gross domestic product, or \$23.3 billion. At its peak in August 2008, more than 227,000 people, or roughly one in nine Albertans, were employed in the industry.

Until recently, the Alberta government followed a traditional procurement model for acquiring its physical assets. This is a pay-as-you-go approach, in which government underwrites 100 per cent of capital costs for the roads and buildings it owns, or helps finance through capital grants to school boards, health authorities or post-

secondary institutions. Under the traditional procurement model, government staff direct and co-ordinate extensive design, bidding and building processes that result in public ownership of the asset and full responsibility for future maintenance.

In 2003, the Alberta government approved a policy to recognize alternate project financing. The scope included public/private partnerships – known as P3s – as well as capital leases, capital bonds and other forms of borrowing.

This allowed the government to supplement traditional construction procurement with accelerated scheduling for “major and complex capital projects” that had “significant ongoing maintenance requirements.” The policy sought to have new facilities and services brought on-stream on time, on budget and with “sufficient quality to remain high standard throughout their life.” A key objective was to bind contractors “into long-term operational contracts and carry the responsibility for the quality of work” being done.

While these objectives make good sense, consider the challenges of bringing together government, finance, construction and maintenance interests under a single partnership arrangement.

Legal, financial, technical, administrative and pursuit of project dynamics can become much more complex under P3s, compared to traditional approaches.

Large projects in Edmonton and Calgary initially served as pilot projects for P3 methodologies. The first “pure” P3 was the southeast leg of the Anthony Henday Drive as part of the Edmonton Ring Road. This project was built at a capital cost of \$365 million and included an additional \$128 million for maintenance over a 30-year contract (total value \$493 million).

In 2007, three major P3 projects were announced: the 21-kilometre northeast section of Stoney Trail in Calgary (\$936 million), the 21-kilometre northwest leg of Anthony Henday Drive (\$1.42 billion) and 18 K-9 schools. This latter project comprised bundles of nine schools in each of Edmonton and Calgary (\$634 million). The Alberta government estimated that building the two latter projects as P3s saved Alberta taxpayers \$358 million, compared to the estimated total costs it would have incurred using traditional procurement approaches.

Consulting with Industry

The Alberta government’s three-year capital plan, covering 2009-2012, contains \$23 billion in direct capital spending and capital grants. This makes the province one of the most significant purchasers of Alberta construction services. Suffice to say, a change in procurement policy can dramatically affect the industry.

Over the years, many contractors working in specific industry segments developed considerable capacity and expertise while working with the Alberta government and its capital grant recipients. This is especially the case for construction and maintenance of roadways, bridges, schools and hospitals throughout the province. Much of their expertise and operational capacity was built on long term familiarity with traditionally financed design/specify/bid/build procurement procedures. Hence, when the province expanded its use of P3s, many wondered about the effect this change would have.

In response, the Merit Contractors Association initiated a consultation



P3 IN ACTION: Steel girder construction on the future 66th St. interchange at Anthony Henday Drive.

between government and industry partners to explore ways government and industry could work together to review the recent experience with P3 projects and, where consensus could be reached, recommend adjustments. In January 2009, Merit and the Alberta Construction Association brought together more than 120 industry experts from architecture, engineering, civil construction, finance and insurance, and general and specialty contractor sectors to examine delivering P3 projects in Alberta.

The session was comprised of two parts. The first part consisted of presentations. The Hon. Jack Hayden, who was then Minister of Infrastructure, opened the forum, followed by senior government officials. Design, finance and construction managers with experience executing P3 projects then provided their perspectives.

In the second part of the session, participants formed working groups according to industry sector to discuss a series of pre-selected questions. Aided by facilitators, each group formulated recommendations on how the Alberta government might consider delivering future P3 projects. The results of these discussions and recommendations follow.

Industry Findings

Construction contractors generally agreed that under appropriate project and market conditions, P3 approaches aid government in obtaining greater certainty in scheduling, completion dates, construction costs and lifecycle maintenance costs. Standardizing requirements on large scale project bundles, or suites, enables economy of scale efficiencies. And, when specifications and/or operational standards are clearly established at the outset, the risk

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to the public owner for costs of changing specifications while the project is under construction is reduced.

Contractors also felt that the Alberta government potentially benefitted from having access to large national and transnational construction expertise and finance capital for large projects – especially when local markets are operating at capacity, as they were in 2007 and 2008. Increased private sector involvement, with its focus on financial bottom line results, also provides additional oversight to projects in a manner that might not always be available to resource-strained, public sector projects.

At the same time, participants raised concerns about how projects were bundled, and how transferring certain risk elements from the public to the private sector could result in the Alberta government failing to realize potential cost efficiencies that may be available from traditional or mixed procurement and financing models.

In particular, bundling similar structures to create an exceptionally large-scale project can result in fewer contractors with expertise in local market conditions and fewer relationships with local sub-contractors and/or suppliers who are capable, or willing, to compete in the process. It was also submitted that misunderstanding local conditions could result in higher risk premiums being incurred. Higher capital costs would also be incurred when commercial terms are not reasonable, risks are disproportionately allocated to industry, or when completion schedules or cost expectations are unachievable.

And while industry participants were unable to reach consensus on the extent to which the Alberta government should use P3 approaches, there was consensus that, when executed properly, these approaches were an important policy mechanism for the

government to meet construction and maintenance service needs.

There was also a general consensus that incorporating longer term maintenance into the government's strategy for new construction procurement was a positive development. The rationale was that holding proponents responsible for maintaining the capital asset until ownership is returned to the public encourages innovation, including design and equipment selection geared to life-cycle optimization from the outset. It also ensures that funding is dedicated for ongoing maintenance – a practice not always adhered to by governments facing fluctuating revenues.

Recommendations

Within the context of a framework calling for refining its P3 policy to provide best value for taxpayer-funded projects in

a manner supporting the capacity, capital investment and expertise of Canadian and Albertan construction companies, a series of 21 technical and process related recommendations were made.

In broad terms, it was recommended that the government regularly consult with industry to:

- Determine the appropriate balance between traditional, mixed and pure P3 approaches to procurement and maintenance of capital assets.
- Examine ways and means of improving the traditional procurement model.
- Refine its P3 approach, particularly with respect to the appropriate levels and risk elements being allocated between government and the private sector.
- Ensure its procurement approaches are based on securing competitive bids and participation from the widest possible array of contractors and suppliers.

Recommendations were also made regarding types and sizes of projects that



CALGARY VIEWS: Construction on Stoney Trail NE at McKnight Boulevard.

industry felt lent themselves well to P3 approaches. There was also general consensus within industry that, as with other types of projects, P3 construction projects were delivered more cost effectively when they concentrated on a municipal or regional basis in proximity to larger urban municipalities.

Considerable attention was also attached to how risk in P3s is often “allocated to the party best able to manage and price it.” The government’s current P3 approach effectively transfers all risk and

related liabilities to the private sector partners. Industry participants suggested that this, perhaps, assumes that the private sector was more capable or willing to attach lower cost premiums to deal with the risk that uncertain conditions bring to any construction project.

It was suggested that, in certain circumstances, the Alberta government and the agencies it funds were better able to con-

trol, or have influence over, certain critical pre-project activities that can significantly hamper scheduled completion dates. This includes acquiring development permits and certifying environmentally compliant sub-surface conditions. By assuming responsibility for these types of uncertainties, it was suggested that the overall process would be more efficient, quicker and result in lower overall costs. 

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