

PUBLIC-PRIVATE PARTNERSHIPS COUNCIL POLICY FRAMEWORK

**The City of Calgary
Finance & Supply
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PUBLIC-PRIVATE PARTNERSHIPS COUNCIL POLICY FRAMEWORK

1. Introduction

Public-Private Partnerships (P3s) are increasingly being pursued by all orders of government as an alternative financing source and delivery model for infrastructure and services. While P3s can provide some significant benefits, there are some significant risks that arise with P3s.

The City is facing over \$18 billion in identified capital needs over the next decade, over half of which is unfunded. Growth needs alone represent almost \$12 billion of this total, with only \$5 billion currently funded. While the majority of P3 projects tend to be focused on new growth infrastructure, there may also be some opportunities to evaluate P3s for some of The City's lifecycle needs.

With such large capital needs and funding gaps, there is a need to investigate all sources of funding for infrastructure and services. P3s should be considered one option for delivering infrastructure and services. In some cases, access to grants from the other orders of government (such as the Federal Government's Building Canada Fund) may be contingent on the project considering a P3 as a method of delivery.

However, not all infrastructure and services are suited to P3s, and other factors such as market conditions will impact the viability of P3s for that infrastructure and services which would normally provide opportunities for successful P3s. Great care needs to be taken in the evaluation and structure of any P3 The City undertakes in order to ensure the maximum benefit accrues to The City, while minimizing the risks. It is also necessary to clearly articulate the goals of the P3 and how the performance of the P3 will be measured. The goal of the P3 policy is to set out the criteria for considering P3s and the evaluation process that will be applied consistently throughout the corporation.

This process involves three levels of assessment for P3 delivery. The screening assessment is the comparison of capital projects against relevant high-level criteria to determine if a project is a candidate for a P3 delivery model. The strategic assessment may be thought of as a preliminary delivery model business case. The value for money assessment attempts to quantify the difference in risk-adjusted cost to The City between traditional procurement (i.e. the public sector comparator) and P3 procurement and builds on the strategic assessment.

The evaluation of potential P3s involves a number of complex tasks that require resources from multiple Business Units and disciplines. A clear governance structure is therefore necessary in order to perform these evaluations in a consistent manner that minimizes the potential risks to The City. While there are significant differences in the governance structure among other governments, one unifying factor is a dedicated role for a P3 function that assists in the evaluation of all (or most) P3 projects. An administration policy will be developed that will address the internal governance structure.

P3 delivery models should be considered as an alternative to traditional procurement, with suitability determined on a project by project basis. It is important for The City to ensure consistency in its approach to P3 procurement across all Business Units, and establish a reputation as a reliable and "bankable" sponsor of P3 projects, so that projects will attract competition from the market of service providers. It is important to avoid failed P3 procurements, which typically occur because insufficient analysis and

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consensus-building among stakeholders has been done prior to initiating the process. Failed procurements can increase the private sector's perceived riskiness of partnering, which will ultimately result in a higher risk premium and thus higher cost of P3s.

1.1 Policy Development Process

In 2007, The City retained Deloitte as consultants to provide expert advice regarding the approach toward P3s. In November, the consultants delivered presentations to City management giving a broad overview of P3s. Subsequently, Deloitte prepared a draft P3 policy framework.

This policy has evolved from expert advice regarding the approach toward P3s provided by Deloitte and involved representatives from various business units and the Mayor's Office. The policy is based on the following guiding principles adopted by Council in September 2008:

1. The public interest is paramount
2. Appropriate public control must be preserved
3. Accountability must be maintained
4. The project must be a priority as determined by the capital plan.
5. The project must be approved within both the capital plan and the projected operating budget of the relevant business unit.
6. The P3 procurement process must be competitive, equitable, transparent, accountable and timely.
7. The selected P3 delivery model must provide best value for money over the project lifecycle with appropriate consideration of risk transfer, opportunities for innovation, and community issues.

Although there is no common definition of a P3, The City has adopted the following definition for P3s for the purpose of the P3 policy and evaluation framework:

A Public-Private Partnership is a contractual agreement between a public authority and a private entity for the provision of infrastructure and/or services in which:

- i. The private sector participant assumes the responsibility for financing part or all of the project; and/or*
- ii. The City seeks to transfer risks that it would normally assume, based on the private sector participant's ability to better manage those risks; and/or*
- iii. The arrangement extends beyond the initial capital construction of the project.*

A more detailed analysis of P3s can be found in Schedule 1. Some examples of P3s in Calgary and other municipalities can be found in Schedule 2.

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2. Identifying and Evaluating P3s

The process of identifying and evaluating P3s for infrastructure and service delivery begins with a clear articulation of the goals of the project. The goals should focus on the desired outcomes of the project (i.e. the infrastructure and service provided). Based on those goals, an assessment of how a P3 can assist in achieving those goals can be performed. However, the base case for comparison should always be the traditional delivery. Only if the P3 provides an increase in total risk-adjusted value should the P3 proceed. This assessment of value is therefore an extremely important task that requires a great deal of care in performing.

2.1 Identification of P3 Opportunities

Not all projects are suitable for P3 delivery. Significant resources are needed to evaluate a project as a potential P2. Therefore, only projects that are of sufficient value should be evaluated. Projects should be considered for P3 delivery when grant funding is contingent on evaluating a project. As well, any projects with a value of \$100 million or greater should be considered for P3 delivery. The project value may be for a standalone project or for a bundle of projects that could be packaged together as a P2. Projects which are the subject of an unsolicited proposal for a P3 should be evaluated provided the project is identified as a priority in the capital budget. Prior to evaluation of P3 delivery for other projects, consideration should be given to the resources needed for the evaluation and weighed against the cost of the project and potential benefit of P3 delivery.

2.2 Delivery Model Assessment

According to the approach developed by Deloitte, based on best practices, there are three levels of assessment that may be applied to determine if a project should be approved for P3 delivery, described as follows:

Assessment Level	Description	Possible Outcomes
1 - Screening Assessment	High-level comparison of project characteristics against criteria to assist in determining potential suitability of a project for P3 delivery.	<ol style="list-style-type: none">1. Flag as potential P3 project2. Flag for traditional procurement
2 - Strategic Assessment	A more detailed examination of the risks, costs, market of service providers, and objectives and constraints to identify, at the strategic level, if a project should be procured as a P3, which P3 delivery model(s) is most suitable, and whether or not further assessment is justified.	<ol style="list-style-type: none">1. Recommendation for traditional procurement2. Recommendation to procure project as a P3, including recommended P3 delivery model.3. Recommendation to undertake Value for Money Assessment prior to deciding on delivery model.

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3 - Value for Money Assessment	An extension of the Strategic Assessment, including quantification of project risks and a preliminary comparison of the relative cost of traditional procurement and P3 procurement through cash flow modelling.	<ol style="list-style-type: none">1. Recommendation for traditional procurement2. Recommendation to procure project as a P3, including recommended P3 delivery model.
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2.3 Screening Assessment

Delivery model screening is the comparison of capital projects against relevant high-level criteria to determine if a project is a candidate for a P3 delivery model. If the screening indicates that a project may be suitable for P3, then it may be examined in greater detail in the strategic assessment. Projects should be screened against the P3 delivery model screening criteria early (ideally, as they are identified and added to the queue of potential projects in each business unit's capital plan) so that a shortlist of potential P3 projects can be maintained, and so the delivery model business cases can be conducted in a timely manner that is integrated with the capital planning process.

The criteria against which each project should be screened include high level descriptions of factors such as the stability of demand for the infrastructure, the service life, the market for bidders and legal considerations. A more complete description of the screening criteria is presented in Schedule 3.

Some of the screening criteria are quite straightforward, based on a comparison of readily-available project characteristics as developed through the traditional capital project planning process. However, some of the screening criteria require an understanding of a range of P3 delivery models, knowledge of the market of P3 service providers, and judgment based on experience. Therefore, it is recommended that a person who has a thorough knowledge of P3s be included in the screening assessment.

As a result, it may take some time for a sponsoring business unit¹ to build the experience "in-house" to successfully apply the criteria on a routine basis and come to the appropriate conclusion. In the meantime, consultants and advisors experienced in P3 projects (P3 advisor) can assist in the application of the criteria. Technical advisors (engineers, architects, quantity surveyors) may also provide useful input to the application of screening criteria.

2.4 Strategic Assessment

The strategic assessment may be thought of as a preliminary delivery model business case. It requires the project to be relatively well-defined, and a planning-level cost estimate (order of magnitude) should be available. The main components of the strategic assessment are listed in Schedule 3.

¹ The sponsoring business unit is the City business unit responsible for the project, e.g. for a water P3 project the sponsoring business unit is Water Services

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During this assessment, a communications and engagement strategy should also be developed and implemented. The level of engagement, in particular, will depend on the nature of the project.

Depending on the characteristics of the project, and the findings of the strategic assessment, it may be very clear which delivery model (i.e. traditional, or a specific P3 model) is most suitable for the project, and to therefore proceed to procurement.

However, it may be determined that more definitive information is required to finalize the decision between traditional delivery and the preferred P3 delivery model. This may be the case for very large, highly strategic, or publicly-sensitive projects, where selection of a delivery model that is new to The City needs the most support possible. It is also more relevant for P3 models that include a component of private financing (i.e. DBFM and DBFO).

2.5 Value for Money Assessment

The value for money assessment builds on the strategic assessment. The term “value for money” is used to describe the difference in risk-adjusted cost to The City between traditional procurement and P3 procurement. The premise of value for money assessment is that by including the cost of all risks to The City under each model, they can be compared on a financial basis to determine the optimum approach². However, the value for money results should be considered alongside the strategic findings, because while the value for money approach is a highly illustrative tool, it is not perfect and should not be considered in isolation. The value for money assessment will be one of the main indicators used to determine if the project should proceed as a P3. As such, it is extremely important that it be done carefully and as objectively and transparently as possible as there is significant potential for this to become a politically sensitive issue.

The value for money assessment should be based on the best available cost estimates, and may warrant some additional engineering, architectural, and costing work depending on the state of the project’s estimates. The need to improve upon existing estimates must be examined on a case-by-case basis, but ideally the project would have been life cycle costed at the preliminary design level or better. However, caution should be exercised in over-advancing project designs, because design costs can be made partially or fully redundant if a project proceeds as a P3. More detail regarding the methodology for a value for money assessment can be found in Schedule 3.

Value may not necessarily mean a savings in cost over traditional procurement; cost savings are just one of the factors to be considered when determining an appropriate delivery model. Non-cost factors such as increased quality or reliability may be equally important in the assessment of value. As well, differences in the social and environmental impacts of the project as a P3, relative to traditional delivery, need to be considered. In this way, a Triple Bottom Line approach to the value-for-money comparison can be taken.

² For additional information on the process for quantifying project risks, refer to *Section 3.6 – Risk Assessment and Quantification*

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2.6 Risk Assessment and Quantification

As discussed earlier, the ability to share and allocate risk between the public and private sectors in service delivery is a key characteristic of P3s. Because of the importance of appropriate risk identification and transfer to the success of any P3, a brief discussion of the risk assessment process contained within the strategic and value for money assessments is warranted.

The initial identification and assessment of project specific risks under both a traditional and P3 delivery model (undertaken in the strategic assessment phase), followed by a quantification of all measurable and material risks to the project under both delivery models will facilitate the value for money analysis.

Developing the list of risks specific to the project (referred to as the “Risk Register”), as well as determining the appropriate risk transfer and estimating the risk valuation parameters (likelihood of risk occurrence and potential effect) is typically conducted during a risk workshop. A list of risk register categories can be found in Schedule 4.

While many of the project specific risks will be known to the project sponsors (as managers of The City’s assets), detailed knowledge of P3 agreements and of similar projects is useful to ensure the Risk Register is comprehensive and that the likely risk allocation for the P3 model is well understood. For this reason, risk workshop participants may include the following:

- Sponsoring business unit representatives; and
- Internal and/or external advisors including finance, procurement, legal, technical and cost consultants.

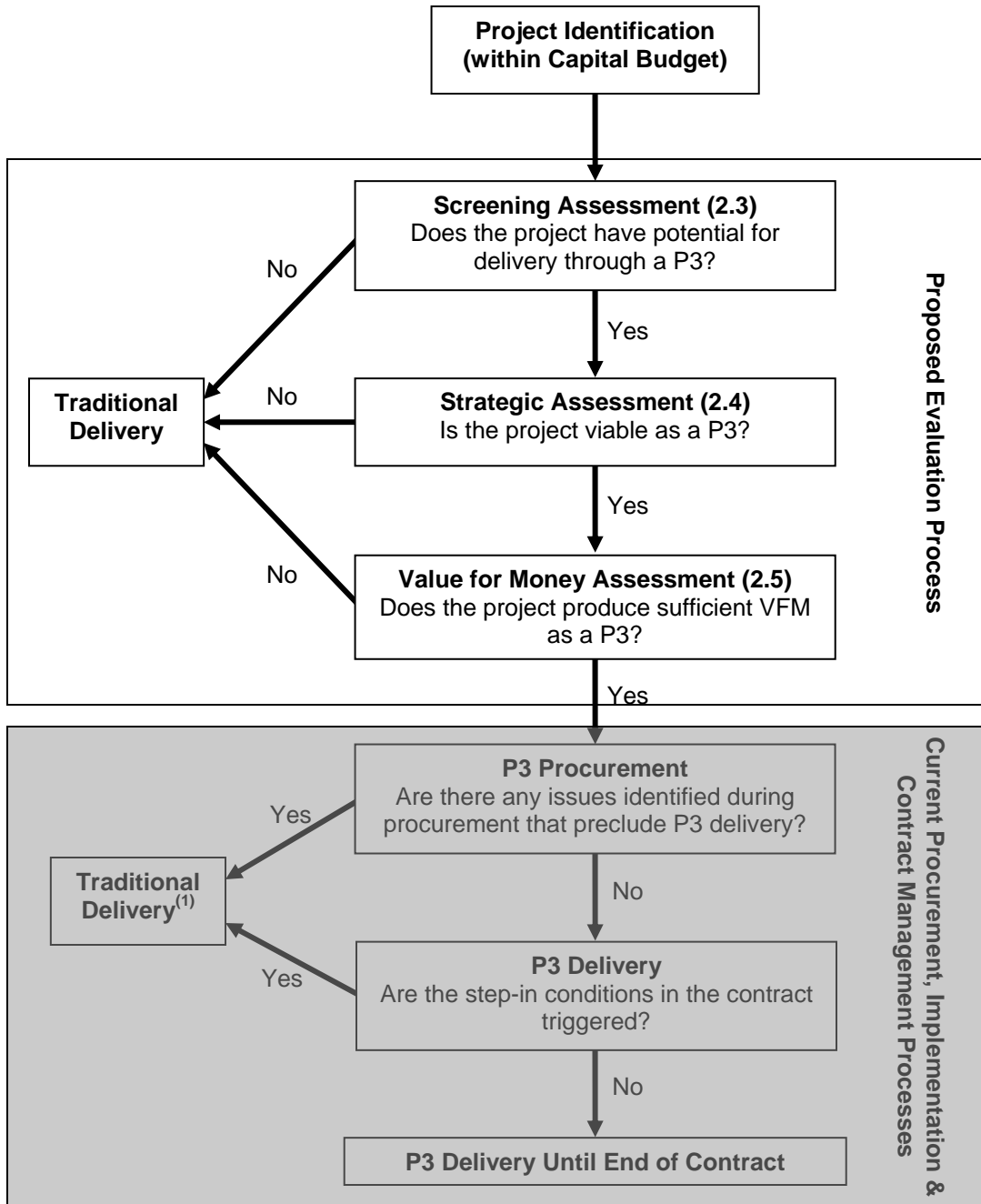
2.7 Procurement, Implementation and Contract Management

Once the evaluation process is complete and a decision to move forward with a P3 has been made, the P3 essentially becomes another contract to be awarded using The City’s current procurement processes. To ensure an efficient and competitive process, all P3 projects should involve fair, open and transparent public tendering process. Included in this process is a request for qualifications (RFQ) stage and a request for proposals (RFP) stage. More detail regarding the P3 procurement process can be found in Schedule 5.

As with any contract, any P3 will require on-going monitoring to ensure that the terms of the contract are being met. The implementation and contract management would proceed as is currently done with City contracts, whereby Supply works in partnership with the sponsoring Business Unit. Supply is responsible for monitoring the overall contract, while the sponsoring Business Unit is responsible for monitoring the technical provisions. Due to the long-term nature of these contracts, continuing resources must be available during the monitoring phase. The contracts will typically include step-in conditions that, if triggered, would most likely result in The City terminating the P3 and moving back to traditional delivery.

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Proposed Decision Process: P3 vs. Traditional Delivery



(1) Form of traditional delivery model depends on when step-in rights are triggered.

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3. Unsolicited Proposals

It is not uncommon for municipal governments to receive unsolicited proposals to deliver capital projects in a manner, that although may not be identified as a P3 per se, is for all City intents and purposes a P3. The City will accept unsolicited capital project proposals, usually through a P3 Unit or the Business Units, and handle them through the following framework which is based on The City's principles for assessing and approving P3 delivery of a project (see Section 4).

3.1 Assessment of Unsolicited Proposals

The following steps will be undertaken to assess the value to The City of the unsolicited proposal.

- The need for the project must be clearly demonstrated and must reflect City priorities (i.e. the project is in the capital budget or a business unit's capital plan).
- A screening assessment must be conducted to validate the use of a P3 delivery model for the project.
- If the screening assessment validates a P3 delivery model, a strategic assessment must be conducted to evaluate the risk allocation offered by the unsolicited proposal.
- A value for money assessment may be required depending on the outcome of the strategic assessment.
- The qualifications (financial, technical, etc.) of the proponent to enter into the proposed P3 arrangement must be assessed and confirmed.

3.2 Acceptance of Unsolicited Proposals

If the assessment leads The City to determine that the unsolicited proposal has value and is worth (potentially) accepting, the following steps will be undertaken.

- The City will determine whether other proponents are interested in entering into a competitive process to provide the same facility or service. To do so, the P3 Unit or sponsoring Business Unit may issue a Request for Expressions of Interest (REOI). The REOI will protect the initial proponent's proprietary information.
- If there are other interested proponents, the sponsoring business unit will advise the proponent that a competitive procurement process will be followed, and the project will proceed as dictated by the capital plan.
- If no other proponents are interested the business unit will undertake a value for money analysis (if not already completed) and business case.
- The capital budget will be updated accordingly for timing and costs.
- Upon the decision to proceed with negotiations, The City's procurement policy will guide negotiations with the proponent using the value for money analysis and business case as its benchmarks.

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4. Governance Structure

The evaluation of potential P3s involves a number of complex tasks that require resources from multiple Business Units and disciplines. A clear governance structure is therefore necessary in order to perform these evaluations in a consistent manner that minimizes the potential risks to The City. This governance structure needs to articulate the roles and responsibilities for the different resources required, in particular the responsibility for decision-making. Without a clear delineation of roles and responsibilities, experience from other jurisdictions has shown there is a greater likelihood of P3s not reaching financial close, due to the intensity and resource demands of P3 project lifecycles (planning, transaction and operations). A failed P3 can have a very detrimental effect on subsequent projects and The City's approach to subsequent projects.

While there are significant differences in the governance structure among governments, one unifying factor is a dedicated role for a P3 function that assists in the evaluation of all (or most) P3 projects. At minimum, the P3 function needs to monitor the evaluation process to ensure that all assessments are completed in a consistent manner. A stronger role is envisioned in which the P3 function provides the necessary expertise and the coordination of resources to complete the evaluations which leads to a recommended delivery model. Administration should therefore identify a Corporate P3 function and clearly define the roles and responsibilities of the different resources required in the P3 evaluation and procurement processes.

A P3 Steering Committee is also recommended. This committee performs an oversight role throughout the evaluation and decision-making process, particularly in terms of the strategic and policy implications of the project, consistent with best practices. The ALT, or another subset of the Senior Management Team, could act as the P3 Steering Committee, although legal, financial and procurement expertise and involvement of the Sponsoring Business Unit are also recommended.

City Council has a vital role in the decision to deliver infrastructure through P3s. Council approves all projects to be included in the capital plan and should approve P3 delivery for projects and the initiation of the P3 procurement process. Council may wish to appoint an independent External Advisory Panel, composed of leading experts from industry, academia and other areas to provide advice on the Business Case and assist in the decision-making process.

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5. Summary

P3s provide the opportunity to deliver some infrastructure projects, although they are not a panacea for solving all of The City's capital funding issues. In order to realize the potential benefits of P3s while minimizing the risks to The City, a comprehensive evaluation of the project is necessary. This is a time and resource intensive exercise; however failure to commit to the evaluations diligently and follow a rigorous public procurement process exposes The City to a significant risk of being encumbered with costly long-term contracts that have high public profiles. The evaluation process presented in this document follows best practices to mitigate this risk. Because of the high cost of the evaluation process, it is necessary to be selective in the projects that are evaluated.

The Council P3 policy outlines the evaluation process. A more complete Administration policy will need to be developed that details the analysis that needs to be done for each stage of the process and clearly delineates the roles and responsibilities within the Corporation to ensure that the evaluations are completed in a consistent and comprehensive manner.

Schedules

The following schedules provide more detail regarding topics presented in this paper:

- Schedule 1: P3 Models
- Schedule 2: Municipal P3s
- Schedule 3: Evaluation Process
- Schedule 4: Risk Register Categories
- Schedule 5: P3 Procurement Process

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Schedule 1: Public Private Partnerships

Governments have a long history of working with the private sector under the traditional model for government service delivery. The City's traditional "delivery model" for capital projects is to treat the design, tender, construction, and operation and maintenance stages of a project as separate components. In each component, The City may or may not involve the services of the private sector (e.g. consulting engineers, architects, construction contractors, etc.).

In contrast, P3 delivery entails combining two or more of the project stages into a single bundle, and utilizing a single private sector bidder to deliver the bundle. In addition, the private sector may finance some or all of the capital required, rather than The City issuing debt or using other financing sources. P3s also tend to be long term arrangements, and may include incorporating not just the initial construction of a facility, but its ongoing maintenance and/or operations and/or service to the public, depending on the nature of the project. The City has increasingly bundled the design and construction (i.e. Design-Build discussed below) for infrastructure delivery, but has limited experience with the other aspects of P3s. While the focus is often on using P3s for the capital infrastructure, an important component of certain P3s can also be the delivery of programs and services.

Definition of P3s

Currently there is no common definition of a P3. The Canadian Council for Public-Private Partnerships defines P3s as follows:

"A cooperative venture between the public and private sectors, built on the expertise of each partner, that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards."

However, this definition does little to assist in the identification of P3s as opposed to traditional delivery. As a result, there is no clear delineation between a traditional delivery model and P3. In general terms, a P3 will transfer more of the risks and responsibilities to the private sector, but this still does not provide a distinguishing characteristic that defines a P3. The City has adopted the following definition for P3s for the purpose of a P3 policy and evaluation framework:

A Public-Private Partnership is a contractual agreement between a public authority and a private entity for the provision of infrastructure and/or services in which:

- iv. The private sector participant assumes the responsibility for financing part or all of the project; and/or*
- v. The City seeks to transfer risks that it would normally assume, based on the private sector participant's ability to better manage those risks; and/or*
- vi. The arrangement extends beyond the initial capital construction of the project.*

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P3 Models

There is a broad spectrum of possible models that could be considered P3s, although there is not universal agreement on all models. Design-Build (DB) is a model in which the private sector designs and builds infrastructure to meet public sector performance specifications, often (though not necessarily) for a fixed price so the risk of cost overruns is transferred to the private sector. Many do not consider DB's to be within the spectrum of P3s and DB's would not fall under the proposed definition for The City.

The following terms are commonly used to describe partnership models in Canada that would be considered P3s under The City's definition, although this should not be considered a definitive or complete listing³:

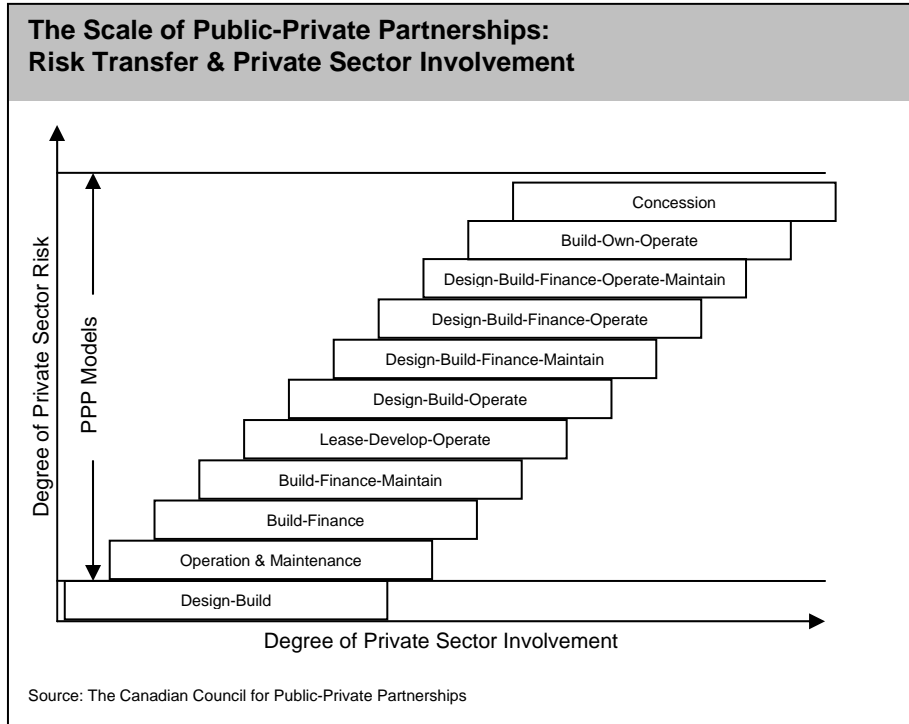
- Operation & Maintenance Contract (O & M): A private operator, under contract, operates a publicly-owned asset for a specified term. Ownership of the asset remains with the public entity.
- Design-Build-Finance (DBF): The private sector designs, finances and constructs a new facility under a long-term lease. The private partner transfers the new facility to the public sector at the end of the lease term.
- Design-Build-Finance-Operate (DBFO): The private sector designs, finances and constructs a new facility under a long-term lease, and operates the facility during the term of the lease. The private partner transfers the new facility to the public sector at the end of the lease term.
- Build-Own-Operate (BOO): The private sector finances, builds, owns and operates a facility or service in perpetuity. The public constraints are stated in the original agreement and through on-going regulatory authority.
- Build-Own-Operate-Transfer (BOOT): A private entity receives a franchise to finance, design, build and operate a facility (and to charge user fees) for a specified period, after which ownership is transferred back to the public sector.
- Buy-Build-Operate (BBO): Transfer of a public asset to a private or quasi-public entity usually under contract that the assets are to be upgraded and operated for a specified period of time. Public control is exercised through the contract at the time of transfer.
- Operation License: A private operator receives a license or rights to operate a public service, usually for a specified term. This is often used in IT projects.
- Finance Only: A private entity, usually a financial services company, funds a project directly or uses various mechanisms such as a long-term lease or bond issue.

The names of the various models indicate the scope of the services that are bundled together under each structure. These models distinguish between operating and maintaining the infrastructure. In terms of P3 models, the difference between maintain

³ Canadian Council for Public-Private Partnerships.

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and operate is that maintain restricts the role of the private partner to physical maintenance of capital asset (e.g. a fire hall), but does not have the private partner delivering programs, products, or services (e.g. firefighting) to the public or The City. The appropriateness of a P3 model, particularly operate versus maintain will vary with each project. The different arrangements therefore result in varying degrees of risk and responsibility that the private sector assumes, as shown in the following figure:



Benefits of P3s

The advantages P3s offer stem from the bundling of tasks together, the appropriate transfer of risk and the creation of incentives that do not naturally occur within the public sector. These benefits can include the following (depending on the nature of the project, and the form of the P3 model):

Potential Benefit	Description
Bring Construction Forward	P3s enable the public sector to spread cost of infrastructure investment over the lifetime of the asset. The Private sector has strong incentive to complete the project ASAP because they need the stream of revenues to repay the capital costs.
On-Time & On-Budget Delivery	Payments are aligned to the delivery of project objectives thus P3s have a solid track record of on-time or early construction completion. Changes to scope, a key factor driving cost overruns and delays, are more difficult and costly and therefore less frequent.

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Potential Benefit	Description
Ensure Assets are Properly Maintained	Well-structured P3s help maintain infrastructure by transferring maintenance requirements for a facility to the private partner, making maintenance a contractual obligation of both The City (payment) and the private partner (execution of maintenance). A more complete lifecycle perspective is therefore taken from the outset.
Cost Savings	Shifting long-term operation and maintenance responsibilities to the private partner creates an incentive to ensure long term construction quality, as the partner is responsible for those costs many years down the road. Experience from several countries has also demonstrated savings from P3s during the construction phase of the contract.
Strong Customer Service Orientation	Private sector infrastructure providers may be made responsible for the customer interface and/or rely on user fees from customers for revenue, and if so have a strong incentive to provide superior customer service.
Enables Public Sector to Focus on Outcomes & Core Business	Properly structured P3s enable governments to focus on outcomes, instead of inputs. Governments can focus leadership attention on the outcome-based public value they are trying to create.

The ability to capture these benefits within a P3 relies on the ability to establish performance benchmarks and appropriate incentives within the arrangement. These benefits are not necessarily exclusive to P3 delivery; however, the incentives to achieve them tend to be stronger within P3 delivery.

Concerns of P3s

In addition to the benefits associated with P3s, there are several concerns that underline the need to proceed cautiously with P3s. These concerns can include the following (depending on the nature of the project, and the form of the P3 model):

Potential Concern	Description
Higher costs	Financing costs for the private sector participant tend to be higher than the financing available to The City when viewed in isolation of the risks retained and/or transferred by the City.
Long term commitment	P3s can create a long term liability to The City, thereby reducing The City's debt capacity. Borrowing bylaws may be needed for P3s.
Reduced control/flexibility	Scope changes become costly, reducing The City's flexibility as the project proceeds. P3s can fail when the public sector participant changes the scope.
Resistance to private sector participation	There may be considerable resistance to private sector participation in the provision of traditional public services.
Reliability of operator	There may be concerns with the loss of control over the private sector operator in terms of changes to the ownership and/or the operations or a loss of control in the setting of fees.
Employee displacement	P3s may displace public sector workers.
Potential for conflict	Any contract that has performance incentives and/or penalties can result in disputes of whether these provisions are triggered.
Accounting Treatment	As public sector entities in Canada move to update their accounting practices to PSAB compliant, there is the need to reflect the true extent of all potential liabilities on the balance sheet, and whether they are tax supported or not, which will

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	depend on the specific details and structure of the project itself.
Evaluation Process	Evaluations require a significant dedication of resources and are very time consuming.

Most of these concerns can be mitigated by carefully structuring and monitoring the contract. There is also a trade-off between the concerns raised and the benefits outlined above. This underlines the need to carefully evaluate and structure any P3 to ensure that the benefits from the arrangement outweigh all concerns and costs.

Success Factors for P3s

P3's can be a successful tool in achieving these goals; however, certain key structures should be in place before embarking on this direction. The below key success factors are based on research from the experiences of other jurisdictions:

- Regulatory environment – there is certainty around the policy and legislative framework that guides the overall P3 development process, as well as in the sector-specific regulation for a proposed project;
- Performance-based approach - the project is focused on the performance needs rather than exact specifications of what is to be built in order to allow the maximum amount of technical innovation on the part of the private partner;
- Transparent process – there is clear process in place, the availability of accurate information, and strong public involvement , including a clear rationale as to why the project is being considered under non-traditional procurement;
- Risk capital financing – the ability of the private partner to secure non-government sources of financing once all the risks are understood and allocated will demonstrate the strength and marketability of the project business case; and,
- Lifecycle perspective – understanding of the impact of the project on existing infrastructure systems, the regulatory environment, costs to operate and maintain over time and other potential peripheral costs and benefits;

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Schedule 2: Municipal P3s

City Experience with P3s

The City has had some limited experience with using P3s for infrastructure and service delivery. The success of The City's experience has been mixed. These partnerships have at times raised issues related to public access and the appropriate role of the municipal government. The majority of these projects can be considered examples of the Operation License and/or Operation & Maintenance P3 models. The level of risk transfer and private sector at-risk capital appears to be minimal. In addition, none of the projects discussed above formally went through the rigorous evaluation process described later in this policy paper.

<u>Regional Recreation Centres</u>	<ul style="list-style-type: none"> ▪ 3 regional recreation centres, Westside, South Fish Creek and Cardel Place under “P3” arrangements ▪ involve partnering with a not-for-profit community-based organization (NFPO).
Westside Recreation Centre	<ul style="list-style-type: none"> ▪ \$25 million capital contribution from The City ▪ \$2 million raised by the community for a capital maintenance reserve. ▪ built by The City and then turned over to the NFPO to operate under a 15-year license of occupation ▪ automatically renewed for another 15 years unless the termination conditions are triggered ▪ operates on a full cost recovery basis, ▪ characterized as a well-run facility
South Fish Creek Recreation Centre	<ul style="list-style-type: none"> ▪ \$25 million capital contribution from The City ▪ \$15 million raised by The City through other means ▪ required significantly more assistance from The City ▪ eventually The City contracted with the YMCA to operate the recreation facility through a 99-year lease ▪ operated as a YMCA, including the fee assistance program ▪ arena is operated by the NFPO ▪ houses a Separate high school and a public library ▪ long planning and negotiation process between all groups before the facility was built, with considerable assistance from The City
Cardel Place	<ul style="list-style-type: none"> ▪ \$35 million capital contribution from The City ▪ additional \$10 million raised through The City in the form of grants and naming rights ▪ NFPO operates the facility, but follows The City's fee assistance program ▪ lengthy planning and negotiation process.
<u>Large Sporting or Cultural Centres</u>	<ul style="list-style-type: none"> ▪ The City has partnered with community groups in providing sports centres and cultural facilities ▪ The City typically provides the land and also may provide some grant funding ▪ The NFPO is responsible for the capital and the operations of the facility ▪ The City may fund some or all of the lifecycle costs

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<u>Outdoor Pools</u>	<ul style="list-style-type: none"> ▪ The City transferred the outdoor pools to a NFPO ▪ NFPO hired a private contractor to operate and maintain the pools ▪ The City provides an annual subsidy
<u>Leisure Centres</u>	<ul style="list-style-type: none"> ▪ The City has received unsolicited proposals from the private sector to operate and maintain Southland and Village Square leisure centres ▪ after value-for-money assessment, proponents were no longer interested in Village Square ▪ The City rejected the proposals
<u>Energy performance Contracting</u>	<ul style="list-style-type: none"> ▪ private sector operator replaced building equipment ▪ funded through realized energy cost savings resulting from the project ▪ disputes with respect to the terms of the contract have resulted in on-going litigation
<u>Louise Crossing</u>	<ul style="list-style-type: none"> ▪ an agreement between The City and the La Caille Group ▪ integrates a fire station into a parking structure and an affordable and at-market housing complex ▪ greater investment in the up-front planning and negotiation process ▪ expectation of lower costs on a per square foot basis ▪ the project offers benefits in terms of a high density development and the achievement of highest and best use of the land ▪ no tangible benefits realized yet
<u>Portrait Gallery of Canada</u>	<ul style="list-style-type: none"> ▪ The City recently submitted a P3 bid for the Portrait Gallery of Canada ▪ not a P3 for City infrastructure or services ▪ The City is providing the land for the Gallery and essentially played the role of a facilitator for a P3 between the federal government and a private sector participant ▪ provides an example of the resource coordination required to evaluate P3s (resources from Planning, Law, Finance, Supply and Corporate Properties were involved) but the risks faced by The City were relatively minimal ▪ P3s for City infrastructure and services will require significantly more resources dedicated to the evaluation and procurement processes

Other Municipal P3s

Several other municipalities have had experience with P3 delivery of infrastructure.

Ottawa	<ul style="list-style-type: none"> ▪ several sports fields and recreation facilities ▪ seniors residence and long-term care facility ▪ paramedic service headquarters ▪ arts centre
Toronto	<ul style="list-style-type: none"> ▪ created Enwave - a joint venture between the private sector and the city to provide deep water cooling district energy infrastructure
Winnipeg	<ul style="list-style-type: none"> ▪ built one bridge through P3 ▪ currently tendering the replacement of another bridge ▪ building a new Police station through a P3.

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The new federal infrastructure funding program Building Canada will also require the consideration of a P3 delivery model for projects that include municipal funding partners where the federal contribution is at least \$50 million.

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Schedule 3: Evaluation Process

Screening Assessment

Following are the criteria that each project should be screened against:

Criteria Category	Criteria	Resources Required	Note
Demand	<ul style="list-style-type: none"> Are the long term operation or service needs relatively stable and/or predictable? 	<ul style="list-style-type: none"> Sponsoring business unit 	1
Duration	<ul style="list-style-type: none"> Is the service life of the capital asset at least 20 years? Is there a long term maintenance, operation, or service need associated with the capital project? 	<ul style="list-style-type: none"> Sponsoring business unit 	1
Innovation	<ul style="list-style-type: none"> Is there scope for innovation in the design of the solution and/or the provision of operation, maintenance, and services? 	<ul style="list-style-type: none"> Sponsoring business unit Technical advisor P3 advisor 	1
Legal Barriers	<ul style="list-style-type: none"> Are there any legislative or regulatory prohibitions to a P3 approach for the project (that cannot be changed in the short term)? What are the opportunities and challenges from a legal perspective? 	<ul style="list-style-type: none"> Legal advisor 	1
Market	<ul style="list-style-type: none"> Are there likely to be at least 3 bidders for the project if it is procured as a P3? Are there precedent projects (examples of similar projects) in other jurisdictions? Has The City received unsolicited proposals for P3-style delivery of the project, or similar projects? Does the private sector have the expertise to deliver on the performance specification? 	<ul style="list-style-type: none"> Sponsoring business unit P3 advisor Technical advisor 	2
Payment	<ul style="list-style-type: none"> Can payment be tied to measured performance? Is there a potential revenue opportunity for the private sector participant? 	<ul style="list-style-type: none"> Sponsoring business unit P3 advisor 	1
Project Risk	<ul style="list-style-type: none"> Are there risks associated with traditional procurement that might be better managed by a private partner? 	<ul style="list-style-type: none"> Sponsoring business unit P3 advisor Technical advisor Legal advisor 	1
Project Size	<ul style="list-style-type: none"> Is the estimated capital cost significant enough to attract the market? <ul style="list-style-type: none"> \$100M or more, market has definite interest Between \$20M and \$100M, market interest may vary based on the asset class (e.g. water projects, buildings may be suitable) Can the project be bundled with one or more other similar projects to achieve a larger project size more suitable for P3? 	<ul style="list-style-type: none"> Sponsoring business unit P3 advisor Technical advisor 	2
Specifications	<ul style="list-style-type: none"> Can the capital asset and related services be defined in a performance or output specification? 	<ul style="list-style-type: none"> Sponsoring business unit P3 advisor Technical advisor 	1
Land	<ul style="list-style-type: none"> Is the land for the project being provided by The City? 	<ul style="list-style-type: none"> Sponsoring business unit Legal advisor 	1
Current State	<ul style="list-style-type: none"> Is the project new build or greenfield? Renovations are, in general, less suitable for P3, however every case is different. 	<ul style="list-style-type: none"> Sponsoring business unit Technical advisor 	1
Integration	<ul style="list-style-type: none"> Is the project relatively independent of other City projects, infrastructure, or control systems? 	<ul style="list-style-type: none"> Sponsoring business unit Other relevant Business Units Technical advisor 	1
Human Resources	<ul style="list-style-type: none"> Does the project, if delivered by a private partner, obviate any current City staff positions? 	<ul style="list-style-type: none"> Sponsoring business unit HR department 	1

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- 1 Resources identified to undertake assessment apply criteria to determine answer
- 2 Additional research / undertaking may be required, including conducting preliminary market sounding to determine private sector interest for project scope and size; identifying similar projects in other jurisdictions, including relative successes/failures; and determining whether private sector has ability to deliver project requirements.

If the balance of the answers to these criteria is positive toward P3 delivery, then the project may be suitable for a P3 delivery model and worthy of more in-depth analysis in the strategic assessment. It may be possible at this stage to identify the most likely suitable P3 model as well.

Strategic Assessment

The main components of the strategic assessment are as follows:

- Project description through the full life cycle (design, construction, operations and maintenance, and decommissioning if applicable);
- Description of cost components, and estimates if available, for each phase of the project life cycle;
- A preliminary list of P3 models to be considered for the project;
- A review of any project-specific objectives or constraints The City may have with respect to the project;
- A *qualitative* risk assessment⁴, which:
 - identifies which risks are of importance in selecting a delivery model for the project
 - assesses the risk (i.e. likelihood and severity) the *project* is exposed to under both traditional delivery, *and* the P3 models under consideration
 - applies each P3 model's risk allocation to assess the risk to The City under each model
- A review of the market of service providers and assessment of the likely interest of the market in bidding competitively for the project (and optionally, a market sounding as described under Value for Money Assessment);
- A review of any relevant precedent projects or similar projects;
- A preliminary comment on the potential for cost savings, based on precedent/similar projects, other relevant experience of The City and its advisors, and the findings of the qualitative risk assessment;
- A determination of the preferred P3 delivery model; and
- A distillation of the above into a determination of preferred delivery model for the project (i.e. either traditional, or the preferred P3 model).

Value for Money Assessment

⁴ For additional information on the process for identifying and assessing project risks, refer to *Section 3.6 – Risk Assessment and Quantification*

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The general methodology for a value for money assessment is as follows:

- Determine the full schedule of the project and, through cash flow modelling, the life cycle cost of traditional delivery of the project (including design, construction, operations, maintenance, recapitalization/renewal, service provision, and financing) to provide the “raw cost estimate.” This may be a high-level order of magnitude estimate or more a detailed estimate, depending on the project profile;
- Quantify the risks (i.e. determine expected cost) to The City of traditional delivery, which when added to the life cycle cost provide the “risk-adjusted cost estimate⁵”;
- Using the raw cost estimate as the baseline, estimate the costs to The City if delivered under the P3 model(s). This is done through cash flow modelling of the private partner’s financial approach, and may consider expected private sector efficiencies in capital and operating costs, as well as the cost of private financing. The results are known as a “shadow bid”; and
- Compare the risk-adjusted cost estimate to the shadow bid to determine the value for money, if any, offered by the shadow bid.

The value for money assessment should reflect, and attempt to price, the project based on The City’s expected service standards.

The main components of the value for money assessment, in addition to those that are part of the strategic assessment, are as follows:

- The preferred potential P3 model, as determined by the strategic assessment (i.e. the value for money assessment should be focused on one specific P3 model in most cases);
- A quantitative risk assessment, which builds on the qualitative risk assessment done in the strategic assessment, and:
 1. Quantifies as best possible the likelihood and impact of all risks that The City faces under traditional procurement; and
 2. Quantifies as best possible the likelihood and impact of all risks that The City faces under P3 delivery (the likelihood and impact will change due to risk transfer to the private partner).
- A market sounding of relevant service providers (i.e. discussion of the project characteristics, costs, schedule, etc.) to obtain direct market input on issues of risk allocation, financing, procurement concerns, and competitive interest that affect the value for money assessment and/or the overall conclusions. This may sometimes be done as part of the strategic assessment;
- Development of a cash flow model for the “raw cost estimate”;
- Development of the “risk-adjusted cost estimate”;
- Development of a cash flow model for the “shadow bid”;

⁵ The risk-adjusted cost estimate is often referred to as the public sector comparator (PSC)

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- An analysis of the difference between the risk-adjusted cost estimate and the shadow bid, resulting in an assessment of value for money; and
- A distillation of strategic factors and value for money to select the recommended delivery model, which may be traditional or a P3 model.

The final step discussed above is key in cases where important considerations identified in the strategic assessment either balance or complement the primarily financial results of the value for money analysis.

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Schedule 4: Risk Register Categories

Following is a table of risk register categories (including sample risks within each category), as they relate to a capital project from the planning through to the procurement, construction and operations/maintenance phases. Each project will require its own risk register, as every project is different, and depending on the delivery models being assessed, certain risks may be managed / mitigated differently. The key resources required to identify and cost the risks in each category are also included. The cost base for each risk refers to the costs that are at risk (i.e. the costs that would be impacted if the risk materialized).

Risk Register Category	Sample Risks	Cost Base	Resources Required to Identify Risk and Determine Value
Policy & Strategy	<ul style="list-style-type: none"> • Risk of delay in procurement process • Risk of procurement process failing 	Total contract value (excluding financing)	Sponsoring business unit, representatives from finance & supply, integrated risk management ("IRM"), legal
Design	<ul style="list-style-type: none"> • Risk that technology proves inadequate to meet project requirements • Risk that design is insufficient to deliver services at required levels 	Design + construction	Sponsoring business unit, representatives from IRM, technical/design advisor
Site Information	<ul style="list-style-type: none"> • Risk that geotechnical and/or environmental information provided to bidders is incomplete • Risk of unforeseen geotechnical and/or environmental conditions 	Design + construction	Sponsoring business unit, representatives from IRM, technical advisor
Procurement	<ul style="list-style-type: none"> • Risk that lack of interested bidders results in smaller number of bids • Risk that RFP documentation is incomplete • Risk of resource capacity within City to undertake/oversee procurement • Risk that City projects compete for bidders 	Design + construction	Sponsoring business unit, representatives from finance & supply, IRM, legal, P3 and technical advisors
Construction	<ul style="list-style-type: none"> • Risk of construction delays • Risk of cost overruns • Risk of latent defects • Risk of City-initiated change orders 	Design + construction	Sponsoring business unit, representatives from IRM, legal, P3 and technical advisors
Permits & Approvals	<ul style="list-style-type: none"> • Risk of not receiving building permits, environmental approvals 	Design + construction	Sponsoring business unit, representatives from IRM, legal, technical advisor
Commissioning	<ul style="list-style-type: none"> • Risk of late delivery 	Design + construction	Sponsoring business unit, representatives from IRM, P3 and technical advisors
Life-cycle and Residual (Maintenance)	<ul style="list-style-type: none"> • Risk of asset being run down • Risk of higher-than-expected maintenance costs 	Maintenance	Sponsoring business unit, representatives from IRM, finance & supply, P3 and technical advisors
Operations	<ul style="list-style-type: none"> ▪ Risk of not meeting performance specifications ▪ Risk of higher-than-expected operating costs ▪ Labour supply risk ▪ Risk of professional/legal liability 	Operating	Sponsoring business unit, representatives from IRM, finance & supply, legal, P3 and technical advisors
Political	<ul style="list-style-type: none"> ▪ Risk of public resistance to private sector involvement in infrastructure/service delivery 	Total contract value	Sponsoring business unit, representatives from IRM, finance & supply, legal, P3 and technical advisors
Reputation	<ul style="list-style-type: none"> ▪ Risk of P3 failing 	Total contract value	Sponsoring business unit, representatives from IRM, finance & supply, legal, P3 and technical advisors

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Schedule 5: P3 Procurement Process

To ensure an efficient and competitive process, all P3 projects should involve fair, open and transparent public tendering process. Included in this process is a request for qualifications (RFQ) stage and a request for proposals (RFP) stage. More detail regarding the P3 procurement process can be found in Schedule 4.

The RFQ should be published in widely available public media. The primary purpose of the RFQ stage is to market the project to a wide audience to encourage participation and competition. In order to narrow the field of high-quality proponents that will receive the RFP, the RFQ should have respondents demonstrate their technical and financial capabilities to deliver the project, as well as their experience and approach in delivering the various aspects of the project. The RFQ stage also has several other purposes, including:

- Signalling the intent of the Department to proceed with the project in order to heighten its profile;
- Presenting an overview of the proposed scope and structure of the transaction; and
- Allowing Interested Parties to assemble the requisite resources and form teams as appropriate.

Based upon established evaluation criteria, the top respondents are invited to respond to the RFP. In order to maintain both competition and manageability, the top three or four respondents should be invited to respond to the RFP. Sole source contracting of P3 projects is not recommended in any situation.

The RFP stage is designed to ultimately lead to the selection of the private entity that will deliver the project. This stage allows proponents the opportunity to develop their technical and financial proposals, and comment on the draft agreement that will be signed by the winning bidder. It does so by allowing proponents access to all relevant project related information and providing proponents the opportunity to demonstrate their understanding of the project, as well as their respective role and responsibilities.

A selection committee composed of senior Administration staff from relevant business units should be formed to make a final decision on the successful project bidder. As well, a process consultant/fairness auditor should be hired to ensure that the selection process adheres to the highest standards of fairness and transparency. It may also be advisable to form an expert advisory committee that includes independent external experts to review the business case and the results of the procurement process.

The selection of the winning bidder should be based on a multi-stage process whereby the bidding entities' technical proposals that will be evaluated on a pass/fail basis, or scored according to criteria set out in the RFP document. Subsequently, bidders will submit a financial proposal based on a Net Present Value (NPV) total project price. In order to maintain consistency and objectivity, as well as deliver value to taxpayers the winning bid should be the lowest net present value bid, unless there are significant differences between bids in terms of the expected social and/or environmental impacts that offset the financial basis for awarding the bid. However, for projects in which criteria other than the lowest NPV are taken into account, it is important that the evaluation criteria and weighting are provided in the RFP document and are adhered to by the

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selection committee. As well, the reasons for adopting this type of approach should be recorded in the project documentation.

The terms of the finalized contract will be based on the specifications identified during the evaluation process and the procurement (RFQ and RFP) process. However, any changes made during the procurement process need to be evaluated in terms of the impact on the value for money assessment. During the procurement process, issues may arise that cause The City to abandon the P3 and move back towards a traditional delivery model. An important consideration in this decision is the impact on future P3s.