

PUBLIC-PRIVATE PARTNERSHIPS

by Mark de St. Aubin

SGR represents public owners, developers, contractors, financing sources and other parties in the design, construction, financing, maintenance and operation of infrastructure. Drawing on its expertise in public and private project financing, real estate, construction and other areas, SGR is well suited to provide guidance to both public procurement authorities and private entities partnering to deliver such projects.

What is a public-private partnership?

The term “public-private partnership,” or “P3,” is commonly misunderstood and can mean different things to different people. P3 is a method for the procurement of public infrastructure (e.g., roads, courthouses, mass transit, public university buildings, airport rental car facilities, among others) using the resources of the private sector. On a typical infrastructure project – for instance, a high-speed rail line connecting two cities – the government selects an engineering firm to design the project, then raises funds for the new train through the issuance of bonds. Next, the government entity awards a contract for construction of the project to a general contractor, typically the one with the lowest competitive bid. Upon completion, the government repays the bonds with the revenues generated by the project, and operates and maintains the facility for its useful life.

A P3 procurement of a public project is substantially different. The public entity advertises its interest in a certain type of project and then requests proposals from private firms interested in designing, constructing, financing, operating and maintaining the project for a term of anywhere from 30 to 50 years. The more open-ended nature of a request for proposals allows the private sector an opportunity to present the governing authority with innovative concepts for the design, construction, financing and other aspects of the project. Often, though not always, the private sector can present the public decisionmaker options with which it would not otherwise be familiar or able to introduce on its own.

How is a public-private partnership project structured?

P3 projects are structured through long-term contracts between the public governing entity and the private firm that has agreed to deliver, finance and operate the project for compensation. At the end of the contract, often referred to as the “concession period,” the asset returns to the public sector. The contractual basis for the relationship permits the public entity to impose key performance incentives on the private firm responsible for the project, from on-time delivery at the outset of the project to requiring the maintenance of state-of-the-art amenities for end users during the term of the project.

The P3 method is often touted for quality incentives that make sense for the private firm and result in the design and construction of a better-performing asset for the benefit of the end user and the public entity to which the project is returned at the end of the concession period. For example, a private firm that designs and builds a new basketball arena for a state university has an incentive to design to the highest quality standards so that the cost of maintenance during the life of the project is decreased, since that same private firm owes the public entity a maintenance obligation for, say, the first 40 years of the project’s useful life.



What are the primary benefits to using a P3 method of delivery?

There are many benefits to P3. Risk can be transferred to the party best positioned to bear that risk. For instance, LaGuardia Airport is currently renovating a major terminal, and continuing to operate during the course of the renovation. The risk of providing air travelers secure, timely flights while building a busy terminal at the same time is one that the New York and New Jersey Port authorities decided could be better addressed by a consortium of private firms with extensive experience in airport design and construction. Capital costs are not paid on the front end of a project, freeing up borrowing capacity for other public infrastructure needs better suited to standard public project financing and procurement methods.

The private firm or concessionaire provides the public entity a single point of responsibility for design, construction and operation risk. Overall delivery times for P3-procured projects are typically shorter, bringing new public assets online sooner than would be the case if conventional procurement were used. When the concessionaire or private operator’s compensation relies on user-based revenue, there is a strong incentive for the private firm to design, operate and maintain a facility that offers state-of-the-art features.

Similarly, the taxpayer dollar, whether in the form of a user fee or other means of compensation to the private operator, results in greater value for the money, since the operator with the most efficient, value-driven concept should be awarded the project. Finally, with proper contract terms, the public entity can negotiate for greater transparency and high levels of accountability in the project on the part of the private operator.



Are certain project types better suited to P3 procurement than others?

Not necessarily. But there are certain types of projects that are developing a track record of general success in the U.S. Transportation projects, student housing projects on public university campuses, and airport consolidated car rental facilities, among others, have seen sufficient repeated success. A jurisdiction that has not used P3 before can take on similar projects with a lesser degree of risk, as there are numerous private players with experience in such asset types and colleagues in other states to share lessons learned. If a public entity is considering a P3 procurement, it would be wise not to attempt a P3 with an asset type that has never before been delivered using the P3 approach.



What are the drawbacks to the use of P3 for public infrastructure?

While P3 procurement has been successfully used in the U.K., Australia, Canada, South America and elsewhere around the world, it remains relatively new to the U.S. P3 is late arriving to the U.S. because public money for infrastructure has typically been plentiful and cheap through the use of tax-exempt debt financing. However, as the need for new and renovated infrastructure is spiking and the states' ability to fund new projects shrinking, states will inevitably have to look more closely at using P3 procurement as an alternative. That means that P3 projects will need political champions, and those champions will need to expose themselves to the risk of doing business in a new way for a public that has grown accustomed to having the best infrastructure in the world. Finding public officials to champion P3 delivery will be an ongoing challenge. These P3 project champions have to demonstrate leadership not only to the public, but also within public agencies that have grown accustomed to one way of doing business.

P3 deals are more complex for public agencies than the conventional method of delivery. These projects are more complicated, involve far more advisers and take much more time to bring to financial close. State, county and local governments that do not have the skill sets required for P3 procurement should proceed cautiously, recognizing the cost, resource and time commitment that accompanies successful P3 procurement. Because the complexity and cost of such deals is greater than for standard public project procurement, the size of the project is important to attracting qualified private bidders. The rule of thumb used in the industry is that a project value in excess of \$100M is needed to attract the interest of multiple sophisticated bidders, though smaller scale projects have certainly succeeded across the U.S.



Mark de St. Aubin's practice is concentrated in the area of construction law, but he also represents clients in complex commercial matters. Focusing primarily on resolving both national and international private project disputes through arbitration, mediation and the courts, he has also represented his clients in public contracting matters involving state and federal government agencies. mdestaubin@sgrlaw.com.