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# DELIVERY OF MUNICIPAL INFRASTRUCTURE AND OTHER PUBLIC PROJECTS USING A P3 MODEL

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# A. ESSENTIAL FEATURES OF A P3 PROJECT

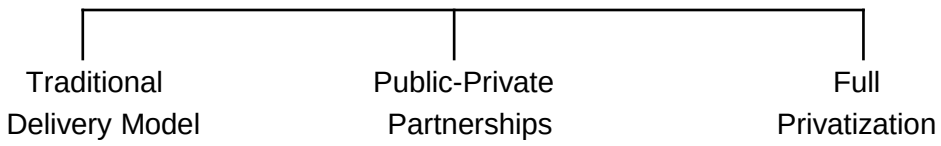
# 1. Introduction

- Great Need, Great Challenges and Great Opportunities
- There are numerous areas in which municipalities deliver infrastructure, including:
  - public transit
  - roads, highways, and bridges
  - sports and entertainment centres, convention centres, and conference centres
  - public utilities (water, wastewater, energy)
  - community and recreation centres
  - social housing
  - parking facilities

# 1. Introduction (cont'd)

- Municipalities have limited financial resources
- Limitations on Legal Authority
- Need for Senior Government Funding and/or Private Finance
- Municipalities have to be conscious of all stakeholders in a project

# 2. Spectrum of Project Delivery Options




- Types of Models
  - Design Build (DB)
  - Design Build Finance (DBF)
  - Design Build Operate Maintain (DBOM)
  - Design Build Finance Operate Maintain (DBFOM)
  - Build Own Operate (BOO)
  - Build Own Operate Transfer (BOOT)



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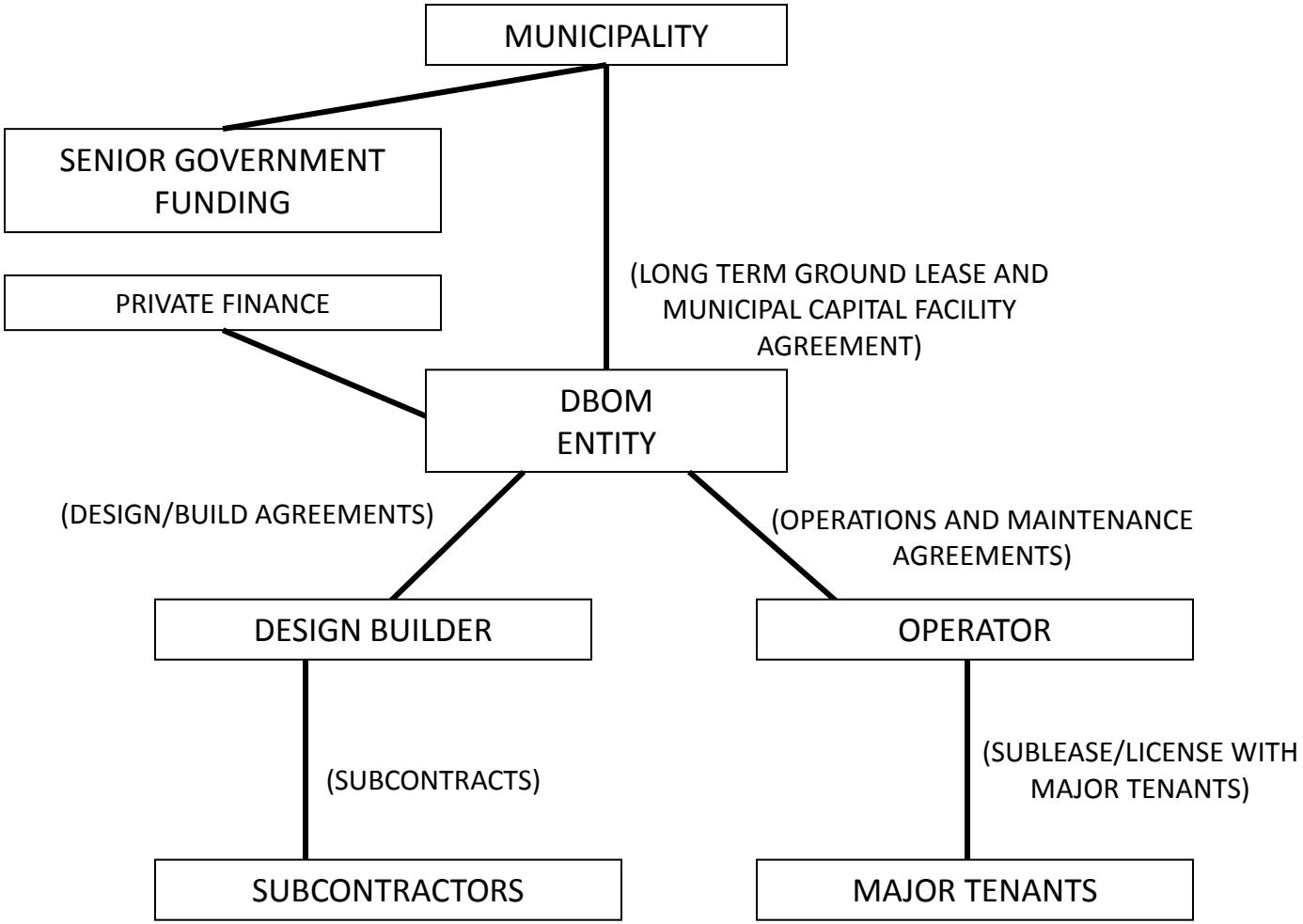
# 3. Differentiating Characteristics of the Models

- Does the Public Sector prescribe exactly what it wants?
- Who owns the asset?
  - Difference between Privatization and P3
- Who controls/ operates/ maintains the asset?
- What happens to the asset at the expiry of term?
- Is the Project publicly funded or privately financed?

# 4. P3 Structure and Diagram



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# 5. Canadian P3 Models

- Partnerships B.C.
- Infrastructure Ontario
  - AFP
- Role of PPP Canada Inc.
- Criticisms of the use of P3's

# 5. Canadian P3 Models (cont'd)

- Reluctance of some municipalities to embrace the P3 concept
- "One Size does not fit all"
  - Varies depending on which public sector entity it is and where in Canada the project is
  - Public sensitivities in certain infrastructure sectors (e.g. safe drinking water)

# 6. What is Ontario's AFP Model and How Does it Work?

- Alternative Financing and Procurement ("AFP") is the name given to the form of P3's developed by the Province of Ontario for the finance and procurement of large infrastructure projects
- The Ontario Infrastructure and Lands Corporation (commonly referred to as Infrastructure Ontario or IO) was incorporated in 2005 to deliver large-scale, complex infrastructure projects using the AFP Model

# 6. What is Ontario's AFP Model and How Does it Work? (cont'd)

- AFP is effectively the use of Provincial Funding to pay out private financing on substantial completion of the project
- Under AFP, the project sponsor (e.g. the municipality) establishes the scope and purpose of the project, while the design and construction work are financed and carried out by the private sector. In some cases, the private sector may also be responsible for operation and maintenance of the asset

# 6. What is Ontario's AFP Model and How Does it Work? (cont'd)

- Sample Guiding Principles that must be satisfied by any public project (articulated by the Province of Ontario in July, 2004)
  - The Public Interest is Paramount
  - Value for money must be demonstrable
  - Appropriate public control/ownership must be preserved
  - Accountability must be achieved
  - All processes must be transparent, fair and efficient

# 6. What is Ontario's AFP Model and How Does it Work? (cont'd)

- All AFP project documents, structure and governance must satisfy these guiding principles
  - Sectors where AFP has been most prevalent in Ontario.
  - Use of AFP for municipal projects
- Role of Infrastructure Ontario in the procurement of a private sector partner for an AFP project

# 6. What is Ontario's AFP Model and How Does it Work? (cont'd)

- Template documentation developed by Infrastructure Ontario over time for use with AFP projects
- The market is familiar with Infrastructure Ontario's template documents, which leads to reduced negotiations
- Will Infrastructure Ontario deviate from its template documentation in Municipal Projects?
- Excellent recent article: Fenn, Michael "Infrastructure Ontario: A Key Agency to Implement the Long-Term Infrastructure Plan", September 2017 (This Report is available on the website of the Residential and Civil Construction Alliance of Ontario (RCCAO) at www.rccao.com

# B. PLANNING AND STRUCTURING THE PROJECT, RISK ALLOCATION AND PROJECT DOCUMENTS

# 1. Planning and Structuring the Project

- Municipality should not engage the Private Sector until it has done its homework
- Importance of a Business Case
- Define Project, contract scope and timing
- Determine Project structure
- Who will own the Project assets (land, buildings, etc.)?
- What role will the Municipality perform?
- What role will the Private Sector perform?

# 1. Planning and Structuring the Project (cont'd)

- Good governance
- Transparency
- Accountability
- Legal authority of the Municipality to undertake the Project
- Senior Government Funding or Private Financing?

# 2. Procurement

- Municipalities usually have a procurement by-law and a procurement or supplies and services department
- A proper procurement process
  - ensures appropriate pricing and costs
  - helps satisfy the value for money requirement
  - fosters efficient and fair communications
  - facilitates timely and comprehensive project definition
  - places the responsibility of:
    (1) disclosure and project definition on the municipality and
    (2) due diligence on the private sector

# 2. Procurement (cont'd)

- Need for transparency in the procurement process
- By-laws or policies of the municipality
- Good faith and fairness
- Use of fairness monitors or process advisors
- Choosing the right procurement model for the project
  - Tender
  - RFEI
  - RFQ
  - RFP

# 2. Procurement (cont'd)

- The importance of properly defining the project and communicating the project's requirements to the private sector in an appropriate and fair manner
- A properly planned and implemented procurement process increases dramatically the likelihood of picking the right partner and forming the right type of partnership

# 3. THE IMPORTANCE OF STAFF REPORTING TO COUNCIL AND OBTAINING REQUIRED LEGAL AUTHORITY

- The need for complete and accurate reports to Council
- Factor in timing for completion of reports, adequate review time and Council's schedules when completing negotiations and finalization of documents
- When and when not to go "in camera"
- Analyze and be aware of the restrictions on municipal authority

# 4. Risk Allocation

- Need for "Optimal Risk Allocation"
  - "Allocation of Risk to the party best able to address and manage the risk"
- In order to achieve optimal risk allocation, project documentation must:
  - Clearly and comprehensively identify and define all risk
  - Allocate each risk without any ambiguity or uncertainty
  - Provide for compensation to the party assuming a risk
  - Equip the party assuming a risk with the power and authority to manage the risk

# 4. Risk Allocation (cont'd)

- Challenges to achieving optimal risk allocation
  - Will the project generate sufficient revenue so that the private sector can be compensated for risks it assumes?
  - Can sufficient power and authority be transferred to the private sector to enable it to manage the risk?
  - Does the project lend itself to defined performance standards to serve as benchmarks for performance bonuses and penalties?

- Five major categories of risks:
  1. Risks typically retained by the municipality
     - Political risk
     - Change in law
     - First Nations claims or cultural/heritage issues

# 4. Risk Allocation (cont'd)

2. Risks typically assumed by the Private Sector
   - Delivery "on time and on budget"
   - Designing, constructing, commissioning and operating to defined standards
   - Industrial relations and labour issues
3. Risks that can be undertaken by either the Municipality or the Private Sector
   - Depends on what makes the most sense and is economically justifiable
   - A good example is responsibility for existing site conditions
     – Allocation of risk will depend on
       (a) the likelihood of adverse conditions and the specifics of the project site
       (b) number and extent of existing site studies
       (c) who can rely on the existing site condition studies and
       (d) time available to private sector to conduct due diligence and carry out its own required studies

# 4. Risk Allocation (cont'd)

4. Risks that are shared
   - Usually because neither party has full control over the risk
   - A common example is "force majeure"

5. Risks that are transferred at a defined point in the project
   - An example is risk of damage or destruction to the infrastructure from an insurable event

# 5. Project Documents

- Project Agreement
- Ground Lease
- Municipal Capital Facilities Agreement
- Construction Contract
- Operation and Maintenance Agreement
- Funding Agreements
- Financing Agreements

# C. FINANCING AND FUNDING ALTERNATIVES

# 1. Impact of P3 Financing

- Enables municipalities to leverage limited resources
- Construction period - incent the private sector to complete construction on time/on budget by:
  - delaying substantial payment until project completion
  - ensuring a fixed price bid – delays, cost over runs, change orders-alterations of scope erode the private sector's profit margin

# 1. Impact of P3 Financing (cont'd)

- Operations/maintenance term, monthly payments – incent the private sector to meet the municipality's contractual requirements by:
  - motivating the adoption of good quality work during the design and construction period to reduce future costs
  - imposing rewards and penalties to ensure the private sector meets and possibly exceeds the municipality's project specific requirements

# 1. Impact of P3 Financing (cont'd)

- Financial Statements – 'Off-the-Books'?
- Municipal P3s do not constitute 'off-the-books' financing
- Infrastructure projects that are dependent on ongoing municipal funding are to be shown as such in the municipality's financial records (Financial Information Returns, Debt and Financial Obligation Limits)

# 2. Cost of Private Finance vs Public Finance

- Municipalities can often borrow funds at a lower cost than the private sector
- Private sector should assume risks under the private sector's control
- The assumption by the private sector of risks beyond the private sector's control may not be in the best interests of the municipality

# 3. Sources of Funding – Non-Exhaustive

- Canada Infrastructure Bank
  - Purpose is to invest, and seek to attract investment from private sector investors and institutional investors
  - The federal government has committed $35 billion and is looking to the private sector for additional funding
  - Focus will be on large projects that are revenue generating
  - Will have wide array of financial tools available to it, including loans, loan guarantees and equity investments
  - Will collect and disseminate data, in collaboration with federal, provincial and municipal governments, in order to better inform infrastructure project investment decisions

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Examples of Specific Infrastructure Grant Programs
  - Federal Government
    - New Building Canada Fund
    - Federal Gas Tax Fund
    - Public Transit Infrastructure Fund (PTIF)
    - Clean Water and Wastewater Fund (CWWF)
  - Ontario Government
    - Ontario Community Infrastructure Fund (OCIP)
    - New Connecting Links Program
    - Gas Tax for Transit

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Municipal Sources
  - Property Taxes
  - Dedicated Property Tax Levy (Infrastructure Levy/ Capital Surcharges)
  - User Fees
  - Development Charges

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Municipal Sources (cont'd)
  - Area Rates/ Local Improvements
  - Reserves
  - Debt
  - New Revenues

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Municipal Sources (cont'd)
  - Investment Income – Prudent Investor Provisions
  - Under Section 418.1 of the *Municipal Act, 2001,* which is not yet in force, eligible municipalities can by by-law 'opt in' to the prudent investor regime (the by-law cannot be revoked)
  - If a municipality is not eligible to 'opt in', the existing 'legal list' of prescribed authorized investments continues to apply (O.Reg. 438/97)
  - Applicable conditions and obligations will be in the regulation

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Municipal Sources (cont'd)
  - Under Section 418.1 a municipality must exercise the care, skill, diligence and judgment that a prudent investor would exercise in making such an investment
  - A municipality exercising investment powers under Section 418.1 is required to obtain advice that a prudent investor would obtain under comparable circumstances

# 3. Sources of Funding – Non-Exhaustive (cont'd)

- Municipal Sources (cont'd)
  - In planning investments, municipalities are to consider the following 5 criteria (in addition to other relevant criteria):
    1. General economic conditions
    2. The possible effect of inflation or deflation
    3. The role that each investment or course of action plays
    4. The expected total returns from income and appreciation of capital
    5. Needs for liquidity, regularity of income and preservation or appreciation of capital
  - A municipality is required to diversify investments in light of general economic and investment market conditions

# QUESTIONS?

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