Pay more, get less. P3s

FACT SHEET

What's wrong with Public-Private Partnerships?

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What is a Public-Private Partnership?

Public-private partnerships or P3s are a relatively new form of privatization, which was pioneered in the United Kingdom in the 1990s under the label Private Finance Initiative (PFI). While the public sector has always partnered with private companies to design and build public facilities, under a P3, the private sector designs, builds, operates and, in some cases, finances a public infrastructure project as part of a 20 to 40-year contract. The private consortia will provide some or all of the up-front funding required to build the project and the government then reimburses the private partner with regular payments over the life of the contract. In some cases, the public sector may even have to buy back the facility from the private consortia at the end of the contract.

P3s cost more than traditional public sector procurement

Why do P3s cost more? First, it is more expensive for the private sector to borrow money than it is for the government. Interest rates are 30% to 50% higher for P3 projects than the rates for conventional public borrowing.[1] Public sector borrowing costs have become even more attractive as a result of the financial meltdown. Second, there are also significant legal, accounting and financial analysis costs that are incurred as a result of the complex, time-consuming P3 transactions. Third, costs for P3 projects are driven up in order to secure an acceptable profit margin for investors.

P3s do not speed up construction

Proponents boast that P3 projects are more likely to be delivered on time and on budget. The reality, however, is that P3 procurement process is usually lengthy, bureaucratic and complex because of the negotiations involving a large number of commercial, financial and legal practitioners and advisors. Project supporters often do not count the period prior to the signing of the P3 contract, which can be years, when declaring their P3 project "on time." Sometimes, P3 partners actually charge a premium to "guarantee" that projects finish on time.

In a tacit admission of the red tape and delay involved with P3 projects, the B.C. government recently raised its threshold for capital projects requiring a mandatory P3 review from $20 million in provincial funding to $50 million "to accelerate capital infrastructure projects."

P3s do not effectively transfer risk to the private sector

P3 boosters argue that the ability to transfer risk from the public sector to the private sector more than compensates for the private sector's higher cost of borrowing. However, the methods used for calculating "risk transfer" are typically never identified. A 2002 British Medical Journal study of U.K. PFI hospitals found little clarity in how risks were measured, and "in over two thirds of the business cases for hospital PFI schemes the risk could not be identified."[2]

A Sauder School of Business study concluded, "Our analysis of the Canadian P3 evidence indicates that the willingness of private sector firms to bear user risk declines with the level of user risk. Private sector firms will not participate in a P3 if it bears cost risk and large revenue risk." The authors of the study continue, "Thus it is not surprising that emerging case study evidence from the U.K.…and Australia…have found that government have not been particularly successful at shifting risk to private partners. Nor is it surprising that contract negotiations associated with attempts to shift risk were extremely costly."[3]

Many contracts have exempted P3 consortia from capital improvements and repairs. In the mid-1990s, Philip Utilities Management Corp., which operated the P3 sewage treatment plant in Hamilton/Wentworth, refused to accept any liability for sewage spills and floods, forcing the city to pay for the clean-up. In the worst-case scenario, such as the bankruptcy of the P3 consortium, there is no risk transfer to the private sector, since the government would be obligated to step in and cover the remaining costs.[4]

P3s reduce public accountability

P3 deals are also typically shrouded in secrecy. The financial information that is necessary for the public to assess the merits of a P3 proposal are typically withheld on the grounds of commercial confidentiality. The Ontario Health Coalition was tied up in a four-year court battle just to get public disclosure of cost comparison information for the Brampton P3 Hospital project. In the case of Partnerships B.C., forensic chartered accountants Ron Parks and Rosanne Terhart found that "critical information and documentation in support of the Value for Money reports was for the most part denied in response to Freedom of Information requests. In our view this suggests a general lack of transparency and public accountability."[5]

When it is released, financial information is not made available in a timely fashion to allow the public to evaluate these proposals. Value for Money reports, which used flawed and biased methodology, are typically released after the "point of no return" when the P3 contract has already been signed and construction has already begun.

P3s put profits ahead of community needs

P3 projects put profits ahead of community needs and control. Despite a looming childcare crisis, the Alberta government announced last fall that preschools and daycares would not be allowed in the new Calgary P3 schools, because providing space for these services could "strain" the private partners ability to build and maintain the schools.[6]

P3 partners that aim to maximize profits do so by cutting corners on construction, preventive maintenance and cleaning, and by cutting jobs, reducing staff salaries and benefits. The drive for profits has also led P3 schools, recreational facilities and transportation projects to hike user fees.

P3s do not allow governments to avoid debt

In the early 1990s P3s were pitched to governments as a way of keeping the debt off public books by letting the private partner incur the infrastructure-related debt. In recent years, this "off-book financing" argument in favour of P3s has been effectively negated by accounting and financial experts. Credit rating agencies, auditors-general, and many governments are now counting P3 debt as government debt. Even P3-booster Kevin Falcon, B.C.'s Minister of Transportation, stated in 2005, "…how the accounting profession looks at P3s and how debt is treated has actually been evolving since 2003…the capital costs of our P3 projects will be treated as assets and liabilities on the [government's] books."[7]

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[1] Hugh Mackenzie, Doing the Math: *Why P3's for Alberta Schools Don't Add Up, A Case study of the Alberta Government's plan to privatize financing and long term maintenance of new schools for Calgary and Edmonton*, prepared for CUPE Alberta, December 2007, p.4.
[2] As cited in Stuart Murray, *Value for Money? Cautionary Lessons About P3s from British Columbia*, Canadian Centre for Policy Alternatives – B.C. Office, June 2006, p. 24.
[3] Aiden R. Vining and Anthony E. Boardman, *Public Private Partnerships in Canada: Theory and Evidence*, U.B.C. P3 Project – Working Paper 2006-04, December 5, 2006.
[4] Murray, p.24.
[5] Blair Mackay Mynett Valuations Inc., *Evaluation of Public Private Partnerships: Costing and Evaluation Methodology*, prepared for Canadian Union of Public Employees, January 5, 2009, p. 5.
[6] Sarah McGinnis, "P3 schools off limits for preschools, day cares; Long-term leases with outside parties barred," *Calgary Herald,* September 10, 2008.
[7] As cited in Murray, p. 18.