



Learning Facilities

Minister's Symposium on Schools Implementation Plan

Recommendation Subcommittee Reports



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Minister's Symposium on Schools Implementation Plan

Alternate Procurement Opportunities (P3s) Subcommittee Report



Alternate Procurement Opportunities (P3s)

SUBCOMMITTEE STAKEHOLDER REPRESENTATION

- Alberta Finance
- Alberta Learning
- Alberta Municipal Affairs
- Alberta School Board Association (ASBA)
- Apex Corporation
- Calgary Board of Education
- Churchill Corporation
- Cohos Evamy
- Genstar Development Company
- Grande Prairie Public School Division
- Pricewaterhouse Coopers
- O & Y Enterprise
- Alberta Infrastructure

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Alternate Procurement Opportunities (P3s)

EXECUTIVE SUMMARY

It is an often overlooked truism that the success of a public-private partnership is sealed well before the selection process begins. If the core policy issues are not addressed, if the objectives are not articulated and, most of all, if the political will is not there, chances are the process will fail, the partner selected will be inappropriate or the entire process, even if it ends in a successful project, will not be a true P3.

This report, therefore, starts with an examination of the problems, perceptions and processes encountered at the crucial early stages. The impediments in legislation, practice or public perception are the context within which a new form of infrastructure delivery, the P3, must operate if it wishes to flourish. We have identified at least ten impediments that have surfaced in the Alberta experience.

But for each of these impediments, there is a response. A new process, a change in policy or advocacy itself may be needed, but each one can be addressed. We have attempted to summarize these responses to lay the groundwork for more detailed work that must follow to give order and substance to a coherent P3 initiative.

Because so much of the success of P3s, especially in a sensitive area such as schools, depends on the pre-planning stage, the purpose and importance of the business case is addressed. The business case must identify and address these key success factors: a comprehensive analysis of the objectives; a “reality testing” of the proposed partnership to make sure it makes sense not only from the government’s point of view, but also from the partner’s perspective and as a stand-alone project; and a buy-in from all the key players. If the project does not work or is not supported as defined in the business case, it is unlikely to work in practice. It is better to find out at this preliminary stage before proceeding with a formal P3 process.

The comments in the response to the challenges and business case sections are intended to sketch in a call to action and next steps in the process. Because each project is unique, suggested responses are stated in general terms to allow flexibility in the process.

Finally, the special circumstances of the unsolicited proposal are addressed and an approach proposed for their consideration.

The concluding comments summarize the initiatives identified as essential for successful implementation of the P3 process and suggest some initial steps.



Alternate Procurement Opportunities (P3s)

INTRODUCTION

In 2001, the Minister's Symposium on Schools considered all aspects of the challenge of providing adequate school facilities. Coming out of that Symposium were five subcommittees asked to evaluate particular aspects of the problem. This is part of the report of Subcommittee #1: An Evaluation of Alternative Procurement Opportunities (P3).

While alternative procurement includes a wide variety of strategies, the focus was to evaluate the use of public-private and public-public partnerships in the provision of schools. In various Alberta literature, the accepted definition of a public-private partnership (P3) is a form of procurement that builds on the experience of each partner to meet clearly defined public needs and provide value for money to the public through the appropriate allocation of resources, risks and rewards. A public-public partnership substitutes a public entity such as a library or other not-for-profit agency, such as a YMCA, for the private partner.

There remains much confusion as to what a P3 might mean in the context of educational services. For our purposes we are evaluating the use of P3s in the provision of the physical facilities required. While "needed educational facilities" may go beyond the traditional definition of a school and include the possibility of different ownership, different users and, in some instances, even different operators of the facilities, we have focused on the use of P3s for school construction, either stand-alone or part of a multi-use facility.

The idea of using P3s for schools has recently become increasingly relevant. In December 2002, the Minister of Alberta Infrastructure wrote a letter to all school districts advising that major capital projects were on hold. The public reaction sparked a renewed debate on the value of P3s in school construction. This paper will hopefully facilitate that debate by pointing us to the key policy and procedural issues to be addressed in the current debate and in planning further initiatives.

Much has already been written on the implementation of P3s in Alberta and elsewhere. Internal government documents such as the "Guide for Public-Private Partnerships for Infrastructure Projects in Alberta" and the "Capital Planning Initiative 2001-2002" are valuable resource documents.

However, there is a need to focus the debate on the practical issues that shape the success or failure of P3s in school construction. This paper is not a theoretical exposition of the basis of a P3 or its claimed advantages. The advantages arise only as a consequence of addressing the key policy and process issues.



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LEARNING FROM EXPERIENCE

While experience in Canada is not extensive, there is enough to draw some conclusions or at least point us in the right direction. Although Nova Scotia's experiment with P3s in schools is best known and most extensive (over 30 schools) it comes from an earlier era when P3s were driven by the desire for off-balance-sheet financing. The current focus on value for money and risk transfer allows us to look much closer to home.

For new school development in particular, two elements take on a determining role: the implications of the school reserve land and the question of compatibility of uses. While it is the responsibility of another Symposium Group (Subcommittee #5: Use of School Reserves) to tackle these issues, the ability to access and use land is critical for the future of P3s. The importance of the land question is touched on here to illustrate the inter-relationship of these two issues.

Alberta's experience is best viewed as a very broad, but shallow, spectrum marked by modest success and spectacular failure. At one extreme are the modest successes, which barely make the P3 radar screen. For many years school districts have made excess capacity at schools with declining enrolment available for other uses. Some may qualify as "school authority purposes" (the wording of the Municipal Government Act); others clearly would not. But they are limited uses, generally deemed compatible with a school, and usually in urban schools of declining enrolment so can be justified as making use of existing facilities.

Historically, on non-reserve lands it has been accepted in practice that a range of non-school uses are deemed acceptable (i.e. compatible with a school and a legitimate use of the land). Almost without comment, non-reserve lands have been used for private schools, police and fire training and a range of social services, even if part of the site was used or designated for a school. Most of the leases are with a private or semi-private entity and are commercially driven; that is, the school districts earn money from them and the users may include for-profit institutions.

Slightly further along that end of the spectrum are shared use, new school projects on non-reserve lands. An example is the Lions Learning Centre in Grande Prairie. There the partners included the Grande Prairie Public School District, City of Grande Prairie and Alberta Infrastructure, but also the Grande Prairie Lions Club, the Society for Support to Pregnant and Parenting Teens, the Grande Prairie Council for Lifelong Learning and a few other social service and learning associations. The uses and partners were all public service oriented and, most importantly, the land was donated by the City. The intent was to combine services to create a learning focus and improve facility utilization. Compatible uses, a community service (but



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LEARNING FROM EXPERIENCE (Cont'd)

private) club and non-reserve lands combined with the political will of the community meant the project went ahead with little public policy debate. One is left to speculate whether, even with community desire for the Centre, these social services and a service club would have been permitted if the land was reserve land.

Indeed, it was as projects were being proposed for reserve land that the public policy debate began in earnest. This is illustrated by such projects as the South Fish Creek Recreation, Education and Library Complex in Calgary (otherwise known as the Bishop O'Byrne School Project). The project was on reserve land and while the school and recreation centre were permitted uses, the proposed library was not. The solution: take the library portion of the mixed-use facility out of the land reserve. Even that was relatively easy because the use, a library, was still a "public" facility. The real challenge is when the land is reserve land but the use is by a commercial private sector operator. That is the other end of the spectrum and is best illustrated by the controversy over the Callingwood School project or so-called "shopping cart high" in Edmonton.

In that situation the school district was sitting on reserve land that had a very significant commercial value as well as a location required for a high school. With the encouragement of the Provincial Government, the school district sought to use a portion of the site for a large food store, which was also desired by the community. The badly needed school was to be partially funded by the Province provided the school district contributed to the cost of construction with proceeds from the food store deal and, secondly, that the food store lands were severed from the reserve lands and re-zoned by the City because of the food store's insistence on ownership of their site. The City of Edmonton, which also had an interest in the reserve lands under the terms of a Joint Users Agreement with the two Edmonton school districts, first demanded compensation and then, following a municipal election, did not have the political will to proceed with what had become a complex undertaking that raised public concerns over whether any commercial activity, particularly a food store, was compatible with a school. In the end, it was too big a leap – dealing with reserve land and commercial and compatibility issues in one project. The school district backed off and is now planning a smaller school approved for complete funding by the Province.



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LESSONS LEARNED

This brief history of P3s in Alberta schools reveals some interesting facts and attitudes that may help us understand the policy issues to be addressed.

1. **Reserve lands**. This is a fundamental determinate and the stumbling block for P3s for a variety of reasons:
 - a) City governments regard a decision to use reserve land to generate income for school purposes as a declaration the lands are surplus to the school's requirements.
 - b) Developers regard the 10% of their land dedicated for reserve as guaranteed for all time to be used only for public amenities (which increase the value of their remaining lands) and not for commercial uses (which might compete with commercial uses on their land).
 - c) Large segments of the public regard the reserve lands as public assets not to be divested or encumbered.
2. **Public-private partnerships distort the system of resource allocation for schools**. This view gets expressed in a number of different ways. Some see P3s as a back door way for the Provincial Government to re-introduce direct school district funding of schools. The Province agrees to fund a school if there is school district contribution through the proceeds of a P3. This is a retreat from the stated Provincial position that the Province will be responsible for all school funding to bring equity between districts. The fear is a P3, which is more likely in urban centres, will once again create the inequities the Province sought to remove.

For others, P3 is an attempt at "queue jumping". The P3 proposal gets the school approved by the Province (because the P3 contribution lowers the cost to the Province), public pressure results in the P3 being abandoned, but the school goes ahead anyway as a fully funded project. That is what has happened at the Callingwood School in Edmonton (albeit as a smaller school) and has been the experience in many jurisdictions.



Alternate Procurement Opportunities (P3s)

LEASONS LEARNED (Cont'd)

3. **Uses compatible with a school.** What constitutes a use that is compatible? What are its inherent characteristics? Is something compatible in one location or grade level and not in another? If uses are compatible on non-reserve lands does that mean they are acceptable on reserve lands? We can guess from recent experience that a library or a social service agency might be acceptable, but a food store is not. Where should the line be drawn and are these lines different in different regions?

4. **There is no appropriate role for the private sector.** There is a strongly held view by some that schools are a public responsibility at the core of our community life and the public sector (Province) has the responsibility, even duty, to adequately fund schools. While some other “public” uses are acceptable, the mere fact that someone is making a profit on public land makes the whole concept unacceptable.

For others in the public, the school and all its personnel are part of a web of safety and development for young children and there is no place for private enterprise in that. The school caretakers are regarded in the same light as the teachers and even if the private sector could provide services for less, they are just not part of the family. There are some activities, such as children’s education, that are so sensitive that some parents want it solely in public hands. They have concerns that this is the first step towards sponsorship advertising in schools and other intrusions into their children’s education. Whatever the truth about these parental concerns, they are real and must be addressed.

5. **The complexity of putting together and then living under a P3 arrangement.** The time, energy and skill to craft a successful P3 is significant and requires school districts to become skilled in areas they have never been involved in before (long-term commercial leases, etc.) The ability to select a good partner and create a strong contract takes time and resources. Many school districts are concerned about becoming involved in commercial matters. Being a landlord of a multi-use facility is not their business, nor is making business decisions such as finding a fair market rent so they are not unfairly competing with the private sector.



Alternate Procurement Opportunities (P3s)

LEASONS LEARNED (Cont'd)

6. **A P3 is often a compromise between complex and diverse needs.** From selecting a location and designing the facility to living together, a P3 is a challenge. What works for a library or a commercial enterprise may not be the best location for a school. There may be design and construction penalties so that different uses can be closed off or monitored. The complexity of operating in a mixed-use facility can be daunting, even with public service partners. The school caters to children and is closed for different hours and for different holidays than almost any other use. The levels of maintenance, the priorities (snow clearing in parking lots is crucial for a library, less so for a school, etc.) and the school's legitimate concern that only its students have supervised access to its facilities, are just some of the issues that combine to create a complex operating plan.
7. **Lack of training in P3 processes.** It is simply unrealistic to hand a P3 arrangement, especially for something as sensitive as a school, to individuals inexperienced with and lacking specific training in P3s. No matter how well intentioned, the skills required to identify the characteristics of a successful partner and negotiate the essential elements of a P3 contract come only with experience, training and mentoring both at the local school level and the provincial level. These front-line individuals often have many years of traditional procurement experience and their approaches, documents and approval processes may be inappropriate for P3s. One cannot move from a structure based on an "owner-contractor" relationship with the lowest qualified bidder to one based on different characteristics and a partnering relationship without spending considerable time training and mentoring the people involved.
8. **The process.** The nature of the P3 procurement process itself needs re-examining. While guidelines are being prepared for Provincial officials, they are preliminary and sketchy in key areas and do not cover the whole procurement process, especially at the local school district level. For example, the Edmonton high school P3 got to the point of detailed commercial negotiations before some fundamental issues were addressed. Negotiations proceeded with a food store without a competitive, public process to select the P3 partner and the City, essential to approve the project, was not fully involved or supportive. Without the necessary buy-in and proper definition of the acceptable partnership conditions, a lot of time and energy can be wasted in advancing a project that is based on a very weak foundation because the process was flawed.



Alternate Procurement Opportunities (P3s)

LEASONS LEARNED (Cont'd)

9. **Resolution of Key Policy Issues.** How can a successful P3 be created if there is no common understanding of what constitutes a successful project? For example, if it is reserve land there are municipal trusts or joint user agreements or other such arrangements that suggest the “public” in P3 is made up of a number of organizations and governments. Assuming they have different objectives, how are the public benefits identified, articulated, prioritized and communicated to the stakeholders, the public and especially to the private partner? Even more fundamental is a consideration of why the P3 is being considered at all. What are the objectives? What criteria will we use to see whether this is a good idea and it works? Because P3 can be done, does it mean it should be? Some benefits may be self-evident (enhanced utilization of facilities, for example), but what are the costs incurred in achieving these benefits? We have already noted some policy issues relating to project approval (compatibility of uses, for example) but more basic questions arise. Is it current government policy to re-introduce local school district funding of schools, except this time instead of school taxes the contribution is to come from the proceeds of P3 arrangements? Because school districts cannot take on the debt of a long-term concession contract what is the respective role and responsibility of school district and the Province in P3? Once a P3 is advanced how does the Province juggle priorities? Are there two streams, one for P3 schools and another for traditionally funded schools? These and many other basic policy issues need to be addressed and government policy clarified so that everyone working in the process understands, not only the rules, but also the policy driving the process.
10. **Political leadership.** If the policy and procedure issues are all addressed, yet there is not the political will to advance the P3 process, it will fail. In fact, many groups are counting on this to happen. Rather than participating in a rational evaluation of P3 projects to see if they really do contribute value for money and serve the public interest, these groups tend to elevate the debate to the “political” level through extravagant claims and, worse yet, creating public fear and apprehension. In doing so, they are betting that no matter the benefits demonstrated, the P3 will not go ahead because public pressure will force the government to back down. This has, in fact, been the case more often than not. Especially in the sensitive areas of health and education, P3s in a number of jurisdictions have been started and then converted to a publicly funded project because it became a hot political issue. The private sector partner or government may not want to get into a public fight and school districts may feel the P3 effort gets them up the priority ladder and are just as happy to avoid all the



Alternate Procurement Opportunities (P3s)

LEASONS LEARNED (Cont'd)

controversy and complications of a P3 if the government offers to fund the school, so the debate is one-sided. With everyone ducking, politicians often feel isolated and the political will starts to fade. The project cannot succeed without strong political leadership that goes well beyond a stated intention to use P3.



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RESPONDING TO THE CHALLENGES

If the Government of Alberta is serious about utilizing public-private partnerships for school construction it must build on the work undertaken to date, including the Minister's Symposium, and systematically tackle the various policy, process and political issues standing in its way. There do not appear to be any insurmountable legislative obstacles, though there seems to be some confusion as to whether a long-term capital lease or concession contract is a "debt" under the Financial Administration Act. Any uncertainty should be resolved, as it affects the provincial approval process and who can enter into P3 contracts.

It is acknowledged that not all situations are appropriate for P3s and each project will have a distinct structure and character. However, there are a number of initiatives that could be taken to address the obstacles to a successful P3 program.

R1. Reserve Lands. Land is a valuable asset and the ability to leverage that asset for the public good is crucial for the future of P3s. First of all, because of the limited revenue-generating potential for school construction, the P3 often becomes essentially a land play – the private partner can use part of the site to raise the revenue that is returned to the public through a contribution to school construction. Typically the private partner makes its money through a combination of highest and best use of the site, efficiencies in construction, operational savings, enhanced utilization and project refinancing, so the importance of land-related policy is obvious.

The irony is that many school districts have more than enough land assets to meet their needs. They own under utilized schools and dedicated land in inappropriate locations. Politically they find it nearly impossible to close schools, and they hold Reserve Land that is not needed for a school but cannot be liberated to make it a working asset. Even if they could access the land base they cannot incur debt so could not enter into long-term concession agreements without the participation of the Province. As a result, some school districts sit on land worth millions of dollars that they will unlikely ever use for a school while real and immediate school needs are going unfulfilled. A classic land rich but cash poor straight jacket.



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RESPONDING TO THE CHALLENGES (Cont'd)

Tackling the reserve land issues will take some “outside the box” thinking followed by comprehensive public and stakeholder consultation and some bold, new policy initiatives. While P3 initiatives are still possible under the existing Reserve Land Structure, if P3s are to play a major role in funding, some change is essential.

A good starting point is to understand the underlying principles and public policy objectives of the reserve land system. If the reserve lands are a public trust, who is accountable for managing the trust and who are the beneficiaries? If Reserve Land is an asset, whose asset is it? There are reserve funds and user agreements involving both the municipality and school districts, but these entities have different mandates and objectives (municipal open urban spaces vs. school construction). Is the mechanism to resolve different priorities adequate? If “the local community” is the beneficiary, how does it express its will and have its priorities met? Is a land dedication system for multiple, often conflicting uses appropriate? Should school districts be permitted to incur debt (essentially mortgage their land assets) to meet current needs?

The Minister’s Symposium recognized the crucial role of the reserve land issue when it created a specific group to focus on different aspects of this question (Subcommittee # 5). The resolution of the reserve land issue will have a profound impact on the success of P3s in Alberta. From a P3 perspective, there are responses that should be considered along with the Subcommittee #5 recommendations, including the following:

- a) Make it clear that a proposal to use a portion of reserve land for other than recognized “school authority purposes” (permitted uses) does not mean that land is considered surplus to school requirements. It does not put the issue into a land disposition mode with all the complexities that entails. Is using Reserve Land to raise money for school purposes (all or partially fund school construction or operations) a legitimate use of Reserve Lands? Is it consistent with government policy to foster P3s in school funding to mortgage, lease or otherwise encumber the Reserve Lands?



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RESPONDING TO THE CHALLENGES (Cont'd)

- b) Expand the definition of permitted uses on reserve land. With the new thinking about life-long learning and the variety of elements that make up a learning environment, the definition of school and recreation purposes can be expanded. It may mean a privately run child care centre for staff and students, or social services geared to the student age group, libraries and so on. If facilitation of learning is more broadly defined to go beyond what a school district traditionally provides, reserve lands should be available for these other support services. Wherever the line is drawn for “school authority purposes”, it is important the public be consulted so that everyone involved in the process knows what is, and what is not, permitted before they start the P3 process.
- c) Make it easier for land to be extracted from the reserve. This may be easier for existing underutilized schools than for recently dedicated land. If a use is desirable but not permitted (as libraries are now), the process for extracting the land necessary for that use should be clearly known. It may sometimes be desirable to keep the land in the reserve but allow a building or part of a facility to be outside. Land swaps for more suitable locations should be facilitated.
- d) Separate the concept of use and ownership. All agreements should provide that ownership remains public or, after the term of the concession/lease, the land and facility returns to the reserve. Land is often extracted to allow for private financing, but even then, after a long-term concession, the private sector partner and their funding agency have recovered their investment (in fact both are looking to the government guarantee of a long-term cash flow, not the land, as their security) so there should be no impediment in having the land become public again. Use of such mechanisms as special purpose companies, with combined public and private ownership, can also be used.
- e) Ensure not only the school district but also the municipal reserve fund or other entity shares in the benefits as the reserve lands are dedicated for a variety of uses. If a community is to lose a park to gain a school, these trade-offs should be explicitly made. Joint user agreements or other such arrangements should be renegotiated to accommodate P3s. Mechanisms must be put in place to resolve the different mandates of the public agencies put in charge of managing the reserve lands.



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RESPONDING TO THE CHALLENGES (Cont'd)

- f) The rules for land dedicated by private developers should be re-evaluated. Currently, 10% of newly subdivided residential land is set aside for reserve lands in perpetuity. If this is to change, the legitimate interests of that development community must be considered. However, there may also be an overriding public interest and changes could be introduced to benefit both the public and private sectors. For example, the land dedicated could be used for defined public purpose for a stated term only, or maybe 8% is public and 2% can be used for related uses, land swaps or whatever. Even more fundamental, perhaps it is inappropriate to lump school and other (recreational, green space) uses together in one reserve. Just as environmentally sensitive lands may be separately dedicated or purchased for preservation, perhaps the 10% dedication should be split into two reserves or a reserve for green space and cash in lieu to allow the school district to purchase the land it needs.

There are ways to be fair while still not “freezing” land that could serve important community needs. Either there is a publicly accountable way of resolving conflicts over priorities for reserve land or the reserves should be separated from inception. These are not easy issues, but the resolution of the use of reserve land is crucial for the future of P3.

- R2. Distorting the system of resource allocation for schools.** The impact of a P3 on the allocation of government resources is worthy of a special comment as there is clearly much confusion about how P3s are to be approached. Under existing procurement policy the Provincial government receives the capital plans of school districts, evaluates them and ranks them in some form of priority and, based on the funds made available, develops a capital program and advises the school districts. That method of proceeding will continue, as P3s are not appropriate for a majority of situations. The government must now decide how it is to receive and allocate resources under P3 arrangements. Presumably, P3 schools will arise because the school is not at the top of the government’s priority list, yet it is an acknowledged local need. If it is not high on the government priority does it go ahead of top priority schools simply because it is partially funded outside government?



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RESPONDING TO THE CHALLENGES (Cont'd)

When the purpose of school P3s was to secure off-balance-sheet financing the rationale was clear. If off-balance-sheet financing is the precondition, that should be clearly stated, as it will severely limit the P3 opportunities because almost all rely on a long-term concession contract. P3s, therefore, may be limited to those circumstances where use of a provincial asset, such as reserve land, is granted to a private entity that, in exchange for a commercial opportunity will provide funds for a school. Those special circumstances raise questions of allocation of resources through the disposition of public assets, and are really not a partnership (though this is how it was originally structured in Nova Scotia and other jurisdictions).

If, on the other hand, the transaction relies on a long-term concession contract, the province must be clear whether it is running two parallel resource allocation systems and how they can be integrated. If the province cannot answer the question why it is embarking on a P3 and how P3s will affect its priorities and resource allocation, it should not be launching the P3 process. P3s for schools are possible. It is possible to protect the provincial priorities (require all proposals to meet provincial priorities, bundling schools into packages so less commercially attractive but high priority schools are also included, etc.). The question is not can we do it but should we do it and if we do it how does it fit into the balance of the Province's procurement strategy for schools. These fundamental questions must be addressed and answered before proceeding.

- R3. Uses compatible with a school.** This question, combined with the use of reserve lands (response to R1 above), are two of the key issues to be resolved in tandem. A public debate, followed by clear published guidelines, should clarify first what are "school authority purposes" that, therefore, can take place on reserve lands and, second, are there other uses that are deemed ancillary or complementary to a school or, at least, are compatible with a school so that they can take place on adjacent lands. What are the implications for uses of reserve land as Alberta moves toward the life-long learning model? School districts and potential P3 partners need to know if their proposed activity is compatible with a school; if it is, then a P3 is possible and negotiations can take place; if not, the private sector partner will need to look elsewhere. So far, we know in Alberta that a library is compatible, but a food store is not. A guideline that merely states the use must be compatible is not enough. A more definitive definition is required after a comprehensive consultation process. The Province should determine who makes the determination, what public process is



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RESPONDING TO THE CHALLENGES (Cont'd)

involved and whether compatibility will be determined on a site-by-site basis, based on the urban context or Province-wide guidelines. In either case, participants need to know what is compatible early on in the process.

- R4. There is no appropriate role for the private sector.** This can be addressed by being careful, first, to separate school construction and school operations. The private sector is already building the schools. The idea that they also fund them generally is not an issue; the fear starts from a concern about transfer of ownership and the private sector operating a facility. Any P3 must be clear what is and what is not within the scope of the P3, and how the public sector will continue to exercise its responsibility, whether to provide consistent specifications and standards, monitor the facility or control permitted operations. A comprehensive, well-articulated P3 strategy is required.

While sourcing private sector funding for schools is acceptable to some, for others there is a lingering problem of the mere fact a private enterprise is earning a profit out of the partnership arrangement. This is true even though it can be demonstrated that the public sector is better off under the arrangement. This is a bit of a red herring since the private sector is already making a profit out of school design and construction. The only difference under a P3 is if there is also a risk transfer that is paid for and, in some cases an operating and maintenance responsibility. However the school district is just buying a service, presumably at less cost than doing it themselves. This is often true because P3 facilities tend to operate longer hours and most school contracts are with unionized employees who would have to work overtime. The practice of preparing a public sector comparator in each instance and making it public should be adopted.

The other area of potential concern is the additional “development profit” for taking on risk and perhaps some additional management. This is a new issue for many school districts who have to decide whether they wish to transfer risk to others and pay this risk premium or keep the risk and manage it. These issues usually come clear in a competitive process when the risk tolerance and the risk premium come out.



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RESPONDING TO THE CHALLENGES (Cont'd)

A risk management plan and a risk transfer plan will address these concerns. Sometimes the real concern is windfall profit, which would embarrass the school district or the politicians. This can be addressed by ensuring the partnership provides for an open-book process of selection and a formula to share profits above a certain level. It is also possible to create a special purpose company where the profits go to both the public and private sector.

Underlying all of this is, of course, a need for a comprehensive and effective communications program. There is significant mis-information in the public realm that can only be met by an open process, full disclosure and a clear articulation of what the initiatives are intended to achieve.

- R5. The complexity of a P3 arrangement.** Crafting a successful P3 arrangement takes time and skill (see training section below). If the Province is serious about pursuing P3s it must determine whether these negotiations should be centred in the school district or at the Provincial level and hire or retain the skills necessary to evaluate and implement the initiative. It is unrealistic to expect all school districts to deal with the complex private sector financing, capital cost allowance and other tax treatments, and the myriad of other “business” considerations that have not historically been part of a school district’s responsibility. The P3 will essentially place people who have been involved in delivering capital projects funded by government into the position of structuring business arrangements and managing private sector partners. A core of well-trained professionals within government and a set of rules on what technical resources are required to advance a P3 proposal, would give the public confidence that these complexities are understood and that the public school authorities, who may only do one school in a lifetime, have demonstrated it was in the public interest and passes audit requirements.
- R6. A P3 is often a compromise.** With respect to selecting an appropriate site, there is often little that can be done. It is an issue that is more difficult to resolve in lower grades where parents want schools in residential areas close to the children whereas high schools are more suited to location in commercial areas. From a school perspective, the issue can be addressed by determining the appropriate site for a school and then identifying compatible uses that find the location acceptable. Only if that does not work, should other sites be evaluated that might be less suitable for the school, but acceptable to the various other proposed uses.



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RESPONDING TO THE CHALLENGES (Cont'd)

Operating differences can be addressed through an operating plan that acknowledges the differences and allocates responsibility and cost accordingly. Better still, the partners can create a separate operating company for the complex so no one partner determines the level of care. An agreement should specify the responsibility of each of the partners and create a funding mechanism that reflects the effort expanded on each partner's behalf. This approach will also tend to eliminate cross-subsidization and pick up life cycle cost penalties due to extra heavy utilization.

With respect to the facilities themselves, if the mixed-use nature of the project is understood from the start, interesting design concepts can evolve that will meet the needs of the various participants without undue financial penalties. It is important to follow the FED process. This means looking at and settling on Function first, evaluating the Economics and only then turning to Design. It probably also requires new and different skills to be brought into the design process. For example, developing a comprehensive safety and security plan for the area will identify how different uses will impact each other and what backup systems are required. The key is being flexible and open to new ways of operating, implementing these changes with sensitivity, respecting labour and personnel concerns and documenting these changes in an operating plan.

- R7. Lack of training.** It is unrealistic to expect successful P3 projects to be created without a considerable effort at identifying individuals interested in and capable of crafting such partnerships and giving them the exposure and training required to incorporate best practices. A core of people who have the knowledge and skill to promote and evaluate P3s for school construction should be identified within the Provincial government. Typically, these individuals would come out of Treasury Board or have similar skills at evaluating public initiatives, but these skills must be complemented by broader experience in the actual implementation of schools. A P3 is not solely a financial arrangement and this must be reflected in the individuals chosen to spearhead their evaluation. A number of jurisdictions have created special units within the provincial government (Partnerships British Columbia; Super Build in Ontario, etc.) to centralize expertise and export it to entities such as school districts to help them in their consideration of P3s. These individuals have an attitude of "partnership" and are supported by the creation of standard forms, mentoring and training programs and upgrading to continually develop best practices and advance the P3 process.



Alternate Procurement Opportunities (P3s)

RESPONDING TO THE CHALLENGES (Cont'd)

R8. The process. The Province must establish a comprehensive, transparent and fair process for the consideration of P3s. Much is written about the P3 process and what constitutes best practices. The Province must adapt these to its own requirements and issue very comprehensive guidelines that apply to school districts as well as Provincial officials involved in P3s. The “Guide for Public-Private Partnerships for Infrastructure Projects in Alberta” is a good first step. These guidelines must deal with, at least, the following:

- Evaluation of alternate procurement options.
- Set out clear objectives and scope of the partnership.
- How to select a good partner since you are looking for different characteristics. This will include the handling of unsolicited proposals.
- Feasibility analysis covering financial, operational and implementation issues.
- Risk assessment, allocation and management.
- A business case showing value for money.
- Set out a series of detailed rules for selection that is transparent, fair, open to competition and publicly defensible.
- The criteria for selection should be clear and the rules should not change in the course of consideration.
- Create a competent team with authority to negotiate.

It is beyond the scope of this paper to set out the guidelines in detail but there is sufficient information available and experience in both Alberta and other jurisdictions to create a comprehensive set of rules for both Provincial and school district officials. The ad hoc approach taken to date should not be allowed to continue.



Alternate Procurement Opportunities (P3s)

RESPONDING TO THE CHALLENGES (Cont'd)

R9. Resolution of key policy issues. Through a consultative process supplemented by advisors experienced in public-private partnership, the Province should identify the key policy issues raised by advancing P3s for school construction, adopt a coherent policy and thereafter articulate this as formal government policy. This will act as a guideline for potential participants, government and approval authorities alike. Until these “rules of engagement” are articulated and fundamental policy issues addressed, the private sector in particular will not have the confidence to participate.

What will the Government have to do to mobilize the private sector? Will Government have to freeze funding for schools to force school district assets to be mobilized? Will they have to cut across school districts to assemble a bundle of schools to create a large enough package to attract the right private sector proponents and amortize the transaction costs? Is operations and maintenance within the scope of the opportunity? Resolution of these questions will define the scope for private participation and identify the likely proponents.

The Province must also establish some benchmarks based on what it is attempting to achieve through the P3 process. Only then will the participants know what they must achieve in order to demonstrate value for money and only then will it be clear to all stakeholders why a P3 is proposed in the circumstances. It starts with an understanding of why the P3 is being considered at all. The impression gained is that there has been too little consultation with the parties and indeed with the general public to develop a stated government policy on P3s. This type of consultation is needed, followed by a clear statement of the objectives being sought and the tests to be applied to evaluate proposals. A number of jurisdictions have developed policies and criteria for determining value for money, appropriate risk transfer and other elements for evaluating a successful P3. Adapting those documents to the Alberta situation would increase the level of comfort and public acceptance of P3s.

R10. Political leadership. P3 is a high profile political issue, so to succeed it needs political champions at all levels. Until that happens, any initiative will be subject to uncertainties of follow through, to the detriment of the P3 process. To date, there is little evidence there is a serious commitment by all partners to make P3s work. For example, at Callingwood School in Edmonton there was no buy-in by City officials or Councillors to the concept, much less a recognition that they were all partners in achieving a community goal. In each instance



Alternate Procurement Opportunities (P3s)

RESPONDING TO THE CHALLENGES (Cont'd)

where a P3 is being proposed, the political leadership must be identified and committed. Political support must be explicit and sustained. Successful P3s can only be created when there is confidence that there is a political will to follow the process through to a successful conclusion.



Alternate Procurement Opportunities (P3s)

THE BUSINESS CASE

The Business Case: The Missing Step In Effective P3s

While it is helpful to identify the impediments to a successful P3 and the responses available within the public sector to deal with those obstacles, to be successful the P3 process must bring these issues together in a comprehensive and integrated manner. While there has been some consideration of the process of evaluation and there is extensive literature on best practices in implementing public-private partnerships, much less attention has been directed at the preliminary work required before these implementation steps are taken. That is until recently. It is now widely accepted and, in some cases, required that any initiative leading to any form of public-private partnership must be preceded by a business case. How that might be applied to a school facility is worthy of some further consideration.

In October 2002, Alberta Infrastructure issued a “Business Case Analysis Guideline”, setting out a new policy of the government of Alberta, and it is a useful starting point. The business plan section of the Capital Planning Initiative is helpful but limited. It requires redefinition and further consideration, as it looks at a business plan from purely a government perspective.

Much attention has recently been lavished on determining what constitutes an effective business case. While there is no universal model, the following elements should be a part of any good business case:

- a) Project objective and alignment with government policy and strategic plan.
- b) Scope of the project defined in terms of outputs.
- c) Risk analysis and risk allocation identifying material risks, who assumes them and why.
- d) Preliminary cost estimates and evaluation against the public sector comparator.
- e) Description of the public sector commitment and obligations.
- f) Cost benefit analysis to demonstrate value for money in comparison to other options, including doing nothing.
- g) Analysis of the private sector’s capability to deliver the project, its interest to do so and the level of competition.



Alternate Procurement Opportunities (P3s)

THE BUSINESS CASE (Cont'd)

- h) Description of the proposed performance measurement and how that relates to payments from government.
- i) Identification of key stakeholders, within and outside government and the consultation plan.
- j) Demonstration of how the project serves the public interest.
- k) Indication of how significant site issues, legal concerns, labour relations, environmental and planning or school curriculum issues are to be addressed.
- l) Project timetable and evidence the government has the personnel and other resources to proceed with a successful P3.

Nor should one underestimate the difficulty in providing a reliable business case. For example, a typical cost benefit analysis often does not consider or quantify the value of risk transfer. As more and more school projects go ahead as part of multi-use projects, this risk analysis and risk transfer will become increasingly important. While construction risks are well understood, the risk of a viable multi-use facility with a number of stakeholders and operating imperatives is much less understood.

The business case must acknowledge that it is bringing in new criteria for evaluation. For example, concerns are often expressed that multi-use facilities are “overbuilt” and that may be true, as they are required to serve multiple uses and are more extensively used. Similarly, a goal to increase facility utilization necessarily puts limitations on spontaneous extra-curricular activity. The business case must acknowledge and recognize the different standards and criteria and evaluate them on a life cycle basis.

The business case must also recognize that a P3 proposal creates a whole new layer of complexity. Staff transfers, union relationships, multi-users with different requirements, long-term working arrangements, private sector requirements and so on will all significantly change the working environment.

The business case should also very clearly deal with the issue of the private sector partner making a profit in the arrangement and deal with such concerns as the added cost of borrowing for the private sector. The issue of the private sector profit is often more concerned about private sector windfall gains causing embarrassment to the public sector. These sorts of concerns must be forthrightly addressed in the business case.



Alternate Procurement Opportunities (P3s)

THE BUSINESS CASE (Cont'd)

Typically a developer participating in a P3 for a school expects to cover 85 to 89% of the capitalized cost of the project through the concession agreement with the school district and seek the balance from multi-use of the facility, such as renting it to educational or civic organizations after hours. Increasingly, many proponents are seeking to satisfy their return by offering maintenance contracts and other operating services at less cost. School districts must be prepared to deal with the question of operating and maintenance contracts as part of any P3 evaluation. While this raises concerns with unions and sometimes parents who may feel their children's safety is being compromised, such contracts are going to become increasingly important. School districts should evaluate which operations they are prepared to leave to others while retaining their core educational services.

Many of the subtle issues that shape the success of a P3 are difficult to quantify. A good business case should address such personnel issues as whether or not the public servants understand and are prepared to accept and operate in a new mode of procurement where they are sharing authority and also have to accommodate and respect private sector requirements.

Of course, it is not only the personnel in school districts who will have to change. The role of Alberta Infrastructure and other Provincial agencies will similarly evolve. For example, the School Capital Manual provides for a detailed review that still concentrates on standard unit rate analysis that could make innovation difficult. One should expect that an agency like Alberta Infrastructure with its broad role in publicly funded schools would play a different role in P3s. This may require not only clear instructions and procedures but also identifying personnel to deal exclusively with P3 projects.

Many jurisdictions have defined in some detail what elements must be addressed in the business case, have set out multi-agency reviews and require formal acceptance of the business case before initiating a P3 process. Given that whole new considerations are brought to bear and the project must work from the perspective of a variety of interests, the concept of a business case is a well-established prerequisite for consideration of public-private partnerships. It should be taken seriously, for the exercise itself will uncover issues that, once addressed, will make the P3 process stronger.



Alternate Procurement Opportunities (P3s)

PUBLIC-PUBLIC PARTNERSHIPS

A few comments on the unique requirements of a public-public partnership might be in order. Clearly there are differences. For one thing there is generally a broader acceptance in the public for multi-use facilities involving other public institutions. Alberta legislation allows for schools and recreational facilities together on reserve land. Experience has shown that combining schools with libraries has also been accepted on reserve land and other uses have been found compatible, including such not-for-profit operations as the YMCA. There are, however, significant challenges that require the same attention to detail as when structuring a public-private partnership.

Most public institutions have a statutory mandate that must be respected. They may also have an elaborate approval and decision-making process that may slow down the project. Most have the same problems schools do, a lack of funds, so there is limited revenue generating potential. They are also limited by the need for annual appropriation of funds, capital funding formulas that do not reflect the added cost of extended use, possibly the need for capital fundraising and the inability to incur debt or enter into long-term contracts. While P3s have been used in the provision of recreational facilities (especially arenas) for years the funding arrangements have been quite different than what would be acceptable for a school. Finally, most public institutions are as risk averse as schools and, with the increased scope and cost of a multi-use facility, the allocation of risk is no easy task.

The operational complexities are no less challenging. The extended use and multi-use of facilities is appealing, but the allocation of the incremental costs can be problematic. Design compromises, union or jurisdictional disputes around extended hours of operation, incremental cost of material upgrades and the allocation of operating costs have to be accommodated. A school and a library may serve a common purpose of advancing education, but operationally they are very different (library attracts all ages, opens different hours, operates all year, etc.) and their different operational priorities and maintenance standards have to be recognized.

One vehicle for overcoming these difficulties is to create a special-purpose entity owned by each of the public institutions. This entity will be responsible for building the multi-use facility and then operating the facility under an agreed-to operating plan. This allows the different public institutions to contract with a third party service provider that they partially own and control. The approved operating plan can provide for different standards in different areas and allocate the costs to each public institution on a cost-recovery basis. Operating an integrated facility separately is neither



Alternate Procurement Opportunities (P3s)

PUBLIC-PUBLIC PARTNERSHIPS (Cont'd)

practical nor cost-effective, as it limits shared systems and economies of scale. It is often easier for public institutions to delegate their authority over operations to a third party rather than to a different public institution.

While on the face of it public-public partnerships are easier and more compatible, the challenges are sufficiently great that the same rules of procurement and due diligence that apply to private partners should be applied to public partnerships.



Alternate Procurement Opportunities (P3s)

UNSOLICITED PROPOSALS

Of particular interest in school construction is the handling of unsolicited proposals. Typically these arise when a developer launching a residential subdivision offers to facilitate school construction on reserve lands to assist in marketing to young homebuyers. However, unsolicited proposals can also arise in regard to underutilized or abandoned facilities or where significant commercial opportunities arise coincident with the need for a school. These initiatives can come from both the public and private sectors, as for example when the local YMCA is looking for new facilities. While school districts are usually the initial recipients of unsolicited proposals, the procedural and policy issues apply equally to Provincial officials.

In truth, no jurisdiction has really solved the policy dilemma and created a true unsolicited proposal process that doesn't lead, ultimately, to some form of public process. The policy dilemma is clear. Governments want to encourage innovation and the introduction of creative (often proprietary) solutions. On the other hand, typical public sector procurement policy and arrangements such as the Internal Agreement on Trade, demand a fair and open competition.

The usual justification for unsolicited proposals, that they present a unique concept or technology or address a need not recognized by government, is problematic when applied to school construction. Looking at school construction it is not really evident what novel technology could not survive a competitive process and it would be rare where school districts did not recognize a need.

The fundamental rule in dealing with unsolicited proposals must, in fact, be a clear indication that it is meeting a need and that the project is a government priority. Building unneeded schools because they are "free" while needed schools await funding is a public policy nightmare.

Assuming it meets the test of a required facility, there may be circumstances where accepting an unsolicited proposal is appropriate. The government should establish a clear policy for the guidance of officials so they understand when they can accept a proposal, how it is to be dealt with and create an evaluation system that will withstand the inevitable criticism of others. Even the Internal Agreement on Trade acknowledges there may be particular circumstances that justify direct procurement. While it is beyond the scope of this paper to develop a comprehensive procedure, some guidelines are evident from a review of the practice in other jurisdictions. In



Alternate Procurement Opportunities (P3s)

UNSOLICITED PROPOSALS **(Cont'd)**

deciding whether to accept an unsolicited proposal, the school district should be sure:

- a) The unsolicited proposal does not relate to a project for which a selection procedure has been initiated or announced.
- b) The school district has determined, based on an assessment of the appropriateness of the arrangement (a considered judgment) that it is in the public interest. This judgment is based on an evaluation of such factors as the proponent's qualifications, feasibility of the project, value for money and that the project meets a real need and has real merit.
- c) The unsolicited proposal can be evaluated without violating the proponent's intellectual property rights either by disclosure under freedom of information legislation or use of the information.
- d) That it is truly an unsolicited proposal providing a facility or service that is innovative or unique and addresses a real need, and is not merely a marketing initiative.

If the proposal passes that initial test, the government should clearly set out the rules for receipt and consideration, covering both the school districts and the provincial government itself.

These rules usually start by outlining the information that the proposal must contain, which typically include the following:

- Full information on the proponent and their previous experience.
- Clearly identify the school district need being addressed.
- What activity is proposed and what results are anticipated.
- What the proponent requires from the school district/Provincial government.
- Implementation details and supporting information such as schedule, budget, risk allocation, etc.
- Clearly identify proprietary information and its permitted use by the school district and Province.



Alternate Procurement Opportunities (P3s)

UNSOLICITED PROPOSALS (Cont'd)

The school district would then do a preliminary review to be satisfied that all the necessary information is provided, that the project is in the public interest and (and this is largely ignored) that the school district has sufficient funds and personnel to follow through with the comprehensive review and the project itself.

If on this preliminary review the school district does not wish to proceed, all information should be returned to the proponent. On the other hand, if it is to consider the proposal, it must move to a comprehensive review. This review must be broad-based to ensure there is no bias or favouritism, and must involve a number of agencies and perhaps independent evaluators. This comprehensive review would examine all elements of the preliminary review in more detail, plus such further considerations as demonstrated value for money, fiscal and budgetary implications, public policy and acceptability issues, and legislative and regulatory implications. This comprehensive review is often supported by having the Auditor General or another independent source without a stake in the project state that it is good value for money and do an internal quality audit to demonstrate the process of evaluation was rigorous, fair and justifies the decision to proceed. It is only after this comprehensive review and the value for money and process audit that approval of an unsolicited proposal should proceed.

In the limited experience in Alberta, it is difficult to see where an unsolicited proposal would be appropriate. The Edmonton project put forward by a food store is an example where a project would not even pass the preliminary test and, hence, should not have been advanced without an open competition. This would not only have avoided the potential litigation by excluded competitors, but would have allowed the public policy debate to take place earlier in the selection process. Similarly, new residential developments will only generate future students, but even there the school district must be satisfied the location meets their priorities and criteria for selection. Public-private partnerships create political challenges that are heightened when the opportunity is offered on a non-competitive basis. While the opportunity should exist, the rules must be carefully followed. Even then, most school proposals, as stand-alone projects, often end up initiating a competitive procurement process.



Alternate Procurement Opportunities (P3s)

CONCLUSIONS

The original intent of this paper was to sketch out a process for applying alternate procurement strategies, including public-private partnerships, to school construction, utilizing current best practices. A description of public sector comparators, value for money assessments and the constituent elements of a risk transfer plan would provide the tools for the implementation of a successful P3 strategy. However, what we found in talking to the people in the field and reviewing the Alberta experience was a process that had been launched with significant policy, process and personnel issues unresolved. Public-private partnerships cannot deliver what the Provincial government wants and the school districts need without a resolution of these issues, so the focus shifted.

The paper has identified ten issues that have arisen as impediments to the successful implementation of P3s. Some relate to public and stakeholder attitudes that can be addressed by articulation of a coherent policy and a meaningful public consultation process. Many operating within the school system believe you could use P3s, but don't know whether you should use them. This ambivalence leads directly to the fundamental question of whether there is the political will, at all levels, to see P3s succeed. There must be more evidence of commitment than mere declarations of policy.

But even declarations of policy need to address the core issues and policy objectives. Are school districts now being asked to bring money to the table to fund schools, only this time through P3 arrangements? If P3 is a government policy, what changes in other policies and established procedures are required to accommodate that policy? This leads us to the most crucial issue – the use of reserve lands.

The issue of reserve lands is being addressed by Subcommittee #5 and their work is critical for the success of P3s. We have recommended here not only that there be clarity in such things as the definition of permitted uses, separating use from ownership, keeping ownership public and refinements of process, but that the operation of the reserve land system itself be re-examined. Either there must be a better system of resolving the inevitable conflicts over the use of reserve lands or the land base for schools should be separately provided for, either by a grant in lieu (often the preferred option for non-urban school districts) or a segregated reserve.

Key procedural issues must also be addressed. The most basic response is to require a comprehensive business case before launching a selection process. If a compelling business case that works from both the public and the private partner's perspectives cannot be publicly explained and defended, the project should not proceed.



Alternate Procurement Opportunities (P3s)

CONCLUSIONS (Cont'd)

In proceeding, the “rules of engagement” need to be clearly set out and followed. While there are some guidelines as referenced in this paper, they are not well known or understood and a much more rigorous procedure must be developed and adopted by all the approval authorities.

Finally, as in most things, real change depends on the people. The respective responsibilities of provincial, municipal and school district personnel must be clarified, as they all have a role to play in a successful P3. It would be unfortunate if there were no experienced and trained individuals within the Provincial government advocating and advancing P3 or if municipal officials looked for compensation rather than solutions.

Addressing all these issues will not be an easy task, but some “next steps” come to mind. Building on the guidelines, symposiums and experience available, the Provincial government should create a core of experienced people dedicated to making P3s work. They will become mentors to school district officials, develop procedures and standard documentation and be the source of knowledge and advocacy both within government and in creating partnerships. They would also address the public policy and public attitude issues by clearing up some of the confusion and myths about what a P3 is and what it can do. This public aspect of their mandate is especially important in the context of schools where confusion over ownership vs. use, construction of facilities vs. operations and P3 vs. sponsorship are just some of the concerns to be openly addressed.

Then just do it. Find a project where the need is greatest, the business case strongest and the public and political support most solid and successfully undertake a pilot project. Make it as simple as possible, adopt the right attitude, be flexible and be prepared to learn as you go. There is enough information, what is needed is knowledge gained through application of this information to meet the increasingly critical need for schools. While there is a danger that a single project will not attract the real “players” because it is too small, if the cost of participation is kept low experience suggests that qualified proponents will participate as a marketing effort if nothing else to demonstrate to the Alberta government the viability of the process.

Public-private partnerships are not a solution for every situation, but they can play a valuable and constructive role in meeting the educational needs of communities. Addressing the policy issues openly and honestly, being clear on what is and what is not an acceptable arrangement, adopting an open and competitive procurement process and creating the public sector capability to deliver under this new strategy will create the conditions for the successful use of public-private partnerships in Alberta schools.