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Public-Private Partnerships:
What Architects Need to Know



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Introduction

Infrastructure needs, including new construction and maintenance of existing infrastructure, far outweigh the ability of government to pay for them. The American Society of Civil Engineers estimates that an investment of \$3.6 trillion is required to reach a state of good repair by 2020.¹ Much of this amount is needed for public schools, correctional facilities, courthouses, and other governmental facilities at the state and local levels. However, faced with treasuries depleted by the Great Recession,² states and local governments continue to delay already overdue infrastructure projects. Consequently, state and local governments and policymakers have been exploring innovative ways to fund, finance, and deliver public infrastructure projects. One such way is the increasingly popular “public-private partnership,” also known as “PPP” and “P3.”

The National Council for Public-Private Partnerships defines a P3 as “a contractual agreement between a public body (federal, state or local) and a private sector entity. Through this agreement, the skills and assets of both sectors (public and private) are shared in delivering a service or facility for the use of the general public. In addition to the sharing of resources, each party shares in the potential risks and rewards in the delivery of the service and/or facility.”³ While P3s can be structured in a variety of ways, P3s for vertical construction are typically long-term agreements between a public entity and a private entity for the designing, building, financing, maintenance, and, when appropriate, operation of a public infrastructure asset, where the private entity assumes responsibility for the condition and performance for the life of the long-term contract.

With government-funded projects a critical source of business,⁴ the introduction of P3s could have a profound effect on the business and practice of architecture. If P3 use facilitates more vertical infrastructure projects, architects could benefit from additional work that may not otherwise exist. On the other hand, P3s have the potential to shift the role of the architect from being the owner’s agent-advocate to a developer’s subcontractor and introduce a number of other challenges that could be detrimental to the profession. The true extent to which vertical P3s will affect the profession of architecture has yet to be determined.

As interest in P3 continues to rise and legislation begins to take shape in the states, architect-advocacy and engagement efforts are at a pivotal point. Architects have the opportunity to shape P3 policy to promote and protect design quality and enhance the built environment at-large, but this opportunity is fleeting.

This report seeks to provide architects with the understanding and knowledge of P3s necessary to meaningfully and effectively engage in the legislative process. In doing so, this report outlines the fundamental features of P3s, key policy challenges for architects, and potential legislative solutions.

Public-Private Partnership Fundamentals

¹ Scott, Doug. "ASCE's New Report Card Bumps the Nation's Infrastructure Grade Up to a D+." ASCE, 1 March 2013. Web. 29 May 2014 <http://www.asce.org/ascenews/featured.aspx?id=23622324272&blogid=25769815007>.

² Gordon, Tracy. "State and Local Budgets and the Great Recession." The Brookings Institute, 1 Dec. 2012. Web. 29 May 2014. <<http://www.brookings.edu/research/articles/2012/12/state-local-budgets-gordon>>.

³ 7 Keys to Success (NCP3). Web. 29 May 2014. <http://www.ncP3.org/P3-basics/7-keys/>

⁴ State and local government projects are particularly important for architects, making up 25% of architectural billings according to the 2012 AIA firm survey. *The Business of Architecture: The American Institute of Architects, 2012 AIA Survey Report on Firm Characteristics* (2012).

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As previously mentioned, P3s “are a long-term performance-based approach to procuring public infrastructure where the private sector assumes a major share of the risks in terms of financing and construction and ensuring effective performance of the infrastructure, from design and planning, to long-term maintenance.”⁵ In more practical terms, this means the public entity:

- Has a single point of responsibility for the design, building, financing, maintenance, and sometimes operations of the asset;
- Does not pay for the asset until it is delivered;
- Pays the cost “over the [contract term] and only if it is properly maintained and performs according to specifications; and”⁶
- Knows the costs for a long-term portion of the asset’s lifespan upfront, “meaning that taxpayers are not on the financial hook for cost overruns, delays or any performance issues over the asset’s life.”⁷

By assuming responsibility for a long-term period of the asset’s life, the private entity becomes fully accountable for the delivered asset and is therefore incentivized, early on, to produce a high-quality product. The payment structure also creates significant financial incentives because the public entity does not begin making performance criteria-based payments until the asset is delivered. Using an output-oriented approach, where the public entity specifies *what* it wants rather than *how* it wants it, maximizes opportunities for innovation and competition and enables the private sector to develop the best solution.

One of the advantages of P3s is that they provide public entities access to private capital, enabling public entities – at least in theory – to obtain financing for a project. While it may seem like an easy solution, P3s are anything but. Public-private partnerships are incredibly complex and require careful consideration. Adequate jurisprudence, public capacity, and other conditions must be in place before the vertical P3 market will become attractive for private investment. Furthermore, if and when favorable conditions exist and attract private sector investment, P3s are still not appropriate for all infrastructure projects – vertical or otherwise – and should not be used unless they serve the public’s best interests.

Policy Challenges and Implications for Architects

Public-private partnerships have the potential to significantly affect the architectural profession. In this climate, architects interested in shaping this emerging delivery model will need to inject themselves – and their concerns – into the legislative process. Legislative proposals regarding P3s will undoubtedly prescribe how architects’ services are procured and define the role architects play in the process. Based on P3 policy, international experience, and enabling legislation from several states, architects face a number of challenges that need to be addressed promptly.

Fundamental Shift in Architect Procurement and Role

In P3s, the private entity assumes full contractual responsibility for delivering the infrastructure asset – and with this single-point of responsibility comes a single procurement. Because of the significant capital required and risks associated with P3s, this single point of responsibility is commonly a special legal entity comprised of an investment firm and development company. In this model, the public entity is

⁵ Frequently Asked Questions (P3 Canada). Web. 29 May 2014. <http://www.p3canada.ca/about-p3s/frequently-asked-questions/>

⁶ *Id.*

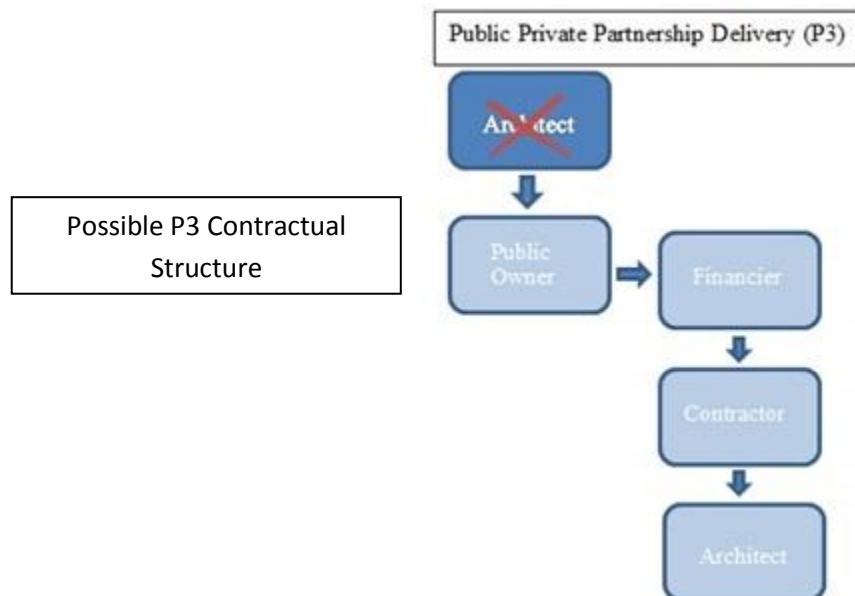
⁷ *Id.*

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not specifically contracting for design services, construction services, etc. Rather, the public entity is procuring the delivery of an infrastructure asset. Accordingly, how the private entity goes about delivering the building and procuring the design and other services is almost entirely within its discretion.

Allowing public infrastructure to be delivered largely through private processes has a significant drawback for architects: qualifications-based selection (QBS) procurement laws are not applicable, nor enforceable. Instead, market forces and profit considerations drive the procurement process of architects for P3s. Depending on a firm's profile (e.g., years of experience, relationships within the industry, size, capacity, specialty area in the public sector, geographic reach, access to capital, and assets and liabilities), P3s could have disparate, industry-wide effects on architectural firms, especially those whose area of practice has been focused on public works.

In addition to a shift in procurement, the P3 contractual structure shifts the architect's role from being the owner's agent-advocate to a private entity's subcontractor. This fundamental shift has the potential to diminish the role of the architect and introduce other issues that may have detrimental consequences for both architects and public entities. The direct contractual relationship between the architect and public entity helps ensure that the architect and his or her design is responsive to the public's owner's needs. Architects traditionally hold a direct contract with the owner that obligates the architect to represent the interests of the end user; however, in P3s, the architect's role and duties become muddled (see graphic, below). This situation becomes even less clear when the architect and public entity-owner do not have direct communications – and even if they do, the public owner's needs or desires may be "filtered" through the lens of a developer, financier, and/or a contractor. Best practices and trust should govern, but without a baseline safety net in the procurement laws, there is potential for communication problems.



In addition to obligating the architect to respond to the public entity-owner's needs, a direct contractual relationship between public entity and architect helps to protect the public owner's interests throughout the project. Without this direct contractual relationship, the owner is left to manage, without unbiased professional guidance, important programming, construction-phase, and delivery

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issues. When a public entity represents itself, as many will do, it is analogous to a *pro se* defendant, accused of a crime, who negotiates directly with the prosecutor. It can be done, but the *pro se* defendant is at a disadvantage because he or she is negotiating from a weaker position, without professional guidance. Without an attorney who has criminal defense and trial experience, the defendant cannot effectively represent himself or herself. The same principle applies to public owners using P3 as a delivery method without an architect-advisor. Public-private partnership projects are extremely complex from all perspectives. Even the most sophisticated public owners need professional guidance to help navigate the process from beginning to end.

Unsustainable Pursuit Costs and Uncompensated Design Work

For architects, perhaps the most immediately damaging issue of P3s is the heavy cost, generally, of pursuing a project. P3 procurement, like the projects for which the delivery model is used, is complex and expensive, often costing private entities several million dollars because procurement is done through a one-step process via design competition. For architects competing in this process, this often means spending hundreds of thousands if not millions of dollars to develop the substantive pre-design and design work required, with no guarantee of compensation. Architects must consider and study existing topography, climate, subsurface conditions, and existing site utilities, as well as compensate administrative and support staff employed during this time. Because of the high burden of pursuit costs for P3 projects, small, medium, and even the largest architecture firms are unlikely to have the financial resources necessary to submit an unsuccessful bid.

Projects are not Performance-Based

As previously described, a typical vertical P3 arrangement provides that the private entity will not only design and construct the infrastructure asset, but will also be responsible for its financing, maintenance, and operation over a long-term period. This contractual structure incentivizes the private entity to deliver a high-quality and high-functioning building that meets performance-requirements efficiently, effectively, and economically throughout its life. However, if the contract is not performance-based, then the private entity will not be responsible for cost overruns, delays, poor design, and performance issues. Without assuming that risk and having “skin in the game”, the private entity has little financial incentive to deliver a well-designed, optimally-performing building at the outset, let alone one that maintains those standards over the building’s lifespan. Unfortunately, a majority of current vertical P3 jurisprudence, codified and proposed, does not enable or even mention performance-based approach. Failing to authorize and use performance-based P3s is detrimental to public entities and the taxpayer.

Potential Policy Solutions

The following policy proposals could be made to eliminate or mitigate the aforementioned challenges, as well as address other issues inhibiting P3 success:

Require Professional Advisers throughout P3 Process

Because of their complexity, scale, and contractual structure, which shifts the responsibility of designing, constructing, financing, maintaining, and oftentimes operating the infrastructure asset to the private entity, it is critical that public entities have unbiased, professional, technical advice throughout the P3 process to protect their interests. One prudent option for protecting taxpayer investment in vertical infrastructure is to require public entities to have professional advisers, including an architect, from procurement to delivery, at a minimum. The architect-adviser, whose sole contractual obligation is to independently represent the interests of the public entity, would be responsible at the outset for assisting the public entity and determining whether P3 is appropriate, identifying and developing building performance requirements, providing guidance throughout the procurement selection process

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and contract negotiations, monitoring contract performance, and other aspects of the P3 process. The architect-adviser, however, would be precluded from bidding on that P3 project due to a conflict of interest. Having an architect-adviser assisting and advocating for the public entity would ensure the public's design interests are protected and enable more positive design outcomes.

Require Value for Money

Public-private partnerships are not appropriate for all public building projects. Though a project may have certain characteristics indicating it *may* be suitable for P3, a Value for Money Analysis is essential for determining whether a P3 *is* proper for a given project. A Value for Money Analysis is a comparison of the total lifecycle costs of delivering, financing, maintaining, and operating a project over a long-term period through P3 versus other available delivery methods. Public-private partnerships are best suited for projects representing a major capital investment with long-term requirements, a complex risk profile with opportunities for risk transfer, life-cycle costing, measurable outputs, opportunities for innovation, and a competitive process because P3 projects involve significant scale, cost, risk, and obligations. While the benefits of a P3 may exceed costs for some projects, the costs may dramatically outweigh the benefits for others. A standardized, objective process that evaluates whether P3 provides the best value and, therefore, protects public investment is a prerequisite for P3 use. Without a Value for Money Analysis, the public sector may use a P3 inappropriately, resulting in a project costing tens if not hundreds of millions of dollars more than it should. This inefficient, uneconomical approach hurts taxpayers and the profession of architecture because it prevents those already scarce public funds from being used on future infrastructure projects.

Establish Centralized P3 Center of Expertise

The establishment of a centralized P3 center of expertise, or "P3 unit," is internationally recognized as a best practice and key to P3 success. Public-private partnerships require large-scale investment, long-term obligations, careful consideration, and significant expertise. A P3 unit is a dedicated body of experts that identify and analyze P3 opportunities for public entities. A P3 unit can serve many functions, but often entails formulating and coordinating P3 policy, standardizing procedures and requirements, providing technical capacity, navigating legal, financial, and technical complexities, evaluating potential partnership projects, monitoring and enforcing contracts, and gauging and promoting private market interest. This type of dedicated resource naturally has fiscal implications, but given the experience of other countries and even states that have created transportation-focused units, their value well-exceeds their cost. Its creation is received by the private sector as a signal that the jurisdiction is ready for and serious about P3 opportunities. As such, a centralized P3 unit is truly the catalyst for creating a smart, successful, and sustainable P3 environment - a solution architects, private investors, and the public at-large get behind.

Use 2-Step Procurement Process to Award P3 Contract

Though the structure of a typical P3 arrangement does not trigger QBS (because the public entity is procuring the delivery of an asset, rather than professional services), procurement should still include an evaluation of qualifications. Vetting private entities' – and their key personnel's – qualifications before seeking proposals promotes competition and quality outcomes. Narrowing the field of participants in the proposal process to three, for example, provides predictability and increased likelihood of being awarded the contract, making the investment more attractive to private participants. Using qualifications and experience to narrow that competitive field enables the public entity to determine whether a private entity is capable of satisfying their infrastructure needs and delivering the asset at the standards they expect. Because the private entities participating in the procurement process will

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typically subcontract much of their work, it is critical that qualification considerations include key personnel, such as architects.

Authorize Stipends for Unsuccessful Bids

Awarding stipends to unsuccessful bidders will lessen the financial burden for firms submitting extensive design and other required work. Providing reasonable compensation for the work produced for P3 procurement may increase competition and proposal quality by making the endeavor slightly more economically feasible, expanding the pool of firms willing and able to participate.

Conclusion

This paper is intended to inform AIA Components about emerging P3 policy. AIA National State & Local Government Relations staff will continue to research and develop materials including model legislation and a matrix of P3-related laws in every state that can be found at <http://www.aia.org/advocacy/state/index.htm> under the “Project Delivery” Tab. We also offer our time through conference calls or component visits to help educate members and contract lobbyists on ways to approach this issue.

P3 is a policy on the rise and on the move. There are opportunities here that can transform this increasingly popular project delivery method into a win-win for all. The solutions proposed herein will benefit both public entities seeking new ways to deliver infrastructure and the architects who will design these future projects.