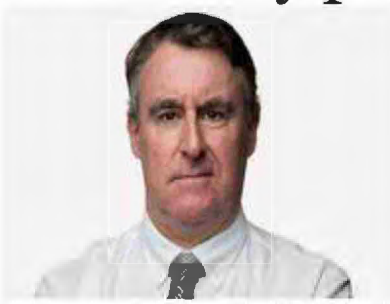
Canadian governments have become seduced by private-public projects



BARRIE MCKENNAECONOMICS REPORTER
PUBLISHED DECEMBER 14, 2014UPDATED MAY 12, 2018
0 COMMENTS

Revelations that cash-strapped Ontario may have squandered as much as $8-billion on dozens of infrastructure projects is shocking enough.

But the real stunner for tax payers is that the province, and governments across the country, risk repeating the same costly mistakes on hundreds of future projects.

Governments in Canada have become seduced by the wonders of private-public partnerships – so-called P3s – and blind to their potentially costly flaws. In a typical P3 project, the government pays a private sector group to build, finance and operate everything from transit lines to hospitals, sometimes over decades.

These projects almost always cost significantly more than if governments just put up the money themselves and hired contractors to build the same infrastructure, under conventional contracts. Ontario Auditor-General Bonnie Lysyk found that the province may have overpaid to the tune of $8-billion for 74 major infrastructure projects, dating back nine years.

A key factor is financing. Private-sector companies can't borrow as cheaply as governments can, adding significantly to the cost, especially on contracts that may run for decades.

Other transaction costs, including lawyers and consultants, are also typically higher with P3s. But the biggest variable is the substantial price tag put on the risk shifted from governments to the private sector. Ontario is convinced the risks of cost overruns, delays, design flaws and the like are substantially lower with public-private partnerships, and it's willing to pay a premium for that peace of mind.

Unfortunately, the government has struggled to accurately price that risk, relying on the murky and potentially inflated calculations of outside consultants. As Ontario Economic Development Minister Brad Duguid sheepishly admitted: "It is a bit of an art, identifying risk, as much as a science."

Ontario's Auditor-General is blunter, suggesting the government's so-called "value assessments" are little more than junk science. "The probabilities and cost impacts are not based on any empirical data that supports the valuation of risk," she said in her report.

And yet quantifying risk may be considerably more straightforward than Mr. Duguid suggests. Change orders routinely add about 5 per cent to the cost of conventional infrastructure projects, according to a consultant involved in numerous government infrastructure projects in Ontario. He said that's a fraction of the steep risk premiums Ontario and other governments routinely put on their P3 projects.

And that miraculously flips around the cost comparison, making P3s the clear value winners. A 2013 study by InterVistasConsulting Inc. for the Canadian Council for Public-Private Partnerships, estimated that governments across Canada saved a total of $9.9-billion on 121 public-private projects between 2003 and 2012, compared to conventional contracting.

"Risk premiums are really tipping the scale in favour of P3s," said University of Toronto associate professor Matti Siemiatycki, who authored a 2012 study on public-private partnerships. He found that P3s cost an average of 16 per cent more than conventionally tendered contracts, based on data from 28 P3 projects in Ontario.

Governments are buying the equivalent of a very expensive insurance policy against something going wrong, without a valid actuarial calculation of the real risks involved, Prof. Siemiatycki argued. He said governments will never get value for money unless they do a much better job of quantifying risk.

But Mark Romoff, president and chief executive of the Canadian Council for Public-Private Partnerships, disputed the notion that governments are exaggerating the risks of traditional procurement.

"If you were to collect that information it in fact would demonstrate categorically that projects procured in the conventional way are consistently over-budget and late," Mr. Romoff said. "We all know that intuitively."

And yet the stakes are simply too high to rely on shaky or absent data. There are roughly 220 P3 projects worth more than $70-billion operating or planned in Canada. The next big one is the federally funded replacement of Montreal's Champlain Bridge, a project that could cost as much as $5-billion.

Ottawa and many provinces remain deeply committed to the public-private model.

The allure may have a lot more to do with politics, than sound financial management. These projects give governments the ability to push spending down the road, with ribbon cuttings today and most of the bills due later.

They also allow governments to duck the inconvenient responsibility when things go terribly wrong. No politician, or bureaucrat, wants to have to explain why a high-profile project is late or over budget.

Taxpayers may have a very different perspective on the responsibilities of public officials, and a few good suggestions on what to do with an extra $8-billion.