

Feature



BY CHRIS MATTHEWS

Use of P3s for Small Infrastructure Projects : A PERSONAL PERSPECTIVE

IN RECENT YEARS, many governmental authorities find that they have fewer budgetary dollars to address needed infrastructure repairs and upgrades. Moreover, national engineering organizations, such as the American Society of Civil Engineers (ASCE), have assigned poor or failing marks to the state of America's infrastructure. For example, recent ASCE Report Cards for the nation's water and wastewater infrastructure average a grade of D; and the capital investment needs for such systems are estimated to cost in the hundreds of billions of dollars. Few would argue that addressing water and wastewater infrastructure

needs, especially those for small municipalities, is, at best, a daunting challenge. Privatization through use of public-private partnerships (P3s) offers local municipalities and others avenues to achieve upgraded infrastructure.

P3s can provide smaller municipalities opportunities to expand infrastructure in a meaningful and efficient way.

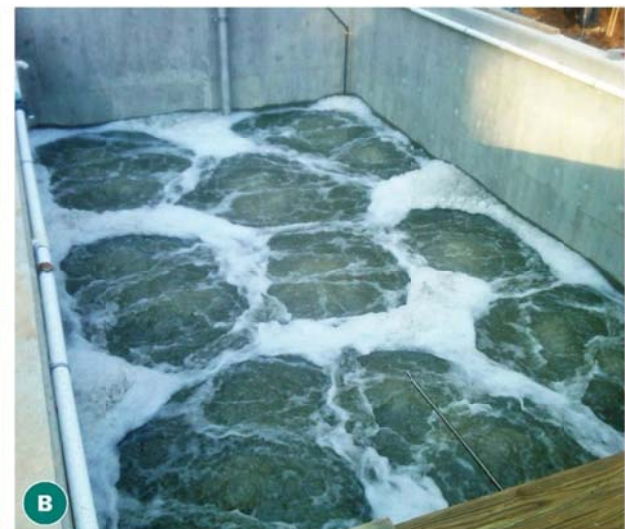
The use of P3 contracts for the small municipality is desirable for multiple purposes: to save time, to save costs, and to use the least expensive financing model for the project. By combining these facets in the P3

contract, the lowest available cost for the consumer can be achieved. In larger P3 projects, the design and construction, as well as the operational involvement, is of a magnitude that requires large firms for each of these disciplines.

For smaller projects, specialized firms may be able to provide more of these services. Global and national investments into major infrastructure upgrades and projects are indeed necessary to support our burgeoning population; however, savvy small municipalities can address certain projects, such as wastewater projects, effectively through P3 vehicles. In fact, use of P3s in this context is



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A. From left, Bob Chambers, Esq. of the law firm of Smith, Currie & Hancock (SCH), Chris Matthews, and Mark McCallum, NASBP CEO, at the fall 2014 educational conference on P3s that was co-sponsored by NASBP and SCH. **B.** The plant, shown here during initial diffuser testing, meets Enhanced Nutrient Reduction standards and treats average daily flows of 70,000 gallons per day.

not new. For example, municipalities in my home state, Alabama, have done so for decades. I cannot say if my experiences are typical in all jurisdictions around the country, but I offer my personal experiences in this article to demonstrate in cursory fashion that P3s have been and can be successful means to accomplish smaller scale infrastructure projects.

Project parameters to consider for good P3 candidates

First, let's explore the "bread and butter" project parameters for what I consider to be a good candidate for a P3 in the smaller market:

- Initial construction volume is under \$5 million;
- The project can be an upgrade to an older, out-of-date system or a brand new system for an area that has no current central system; and
- There is either an established customer base or a reasonable expectation of growth.

Now let's explore the typical P3 contract scenario and what is required to give an incentive or expectation for the above parameters:

- P3 terms vary, but in most cases they exceed 20 years;
- System operating revenues
 - Should exceed initial operation costs; and
 - Should include return on investment
- Capital Return or Impact Fees
 - Should repay system capital costs, including interest; and
 - Should cover cost of plant and collection system
- The public body should be willing to cede detail control of the system and its development to those who have expertise in P3 contracts.

If the above project parameters can be satisfied, then proceeding with the P3 can be considered. A significant hindrance in the past for smaller systems has been the cost and knowledge available for legal considerations necessary to procure and put a P3 into place. To a great extent, the Engineers Joint Contract Documents Committee (EJCDC) has helped to streamline this process.

THE P3 CONTRACT MAY PROVIDE FOR VARYING TYPES OF FEES TO BE RECEIVED BY THE CONCESSIONER DURING THE TERM OF THE CONTRACT.

EJCDC recently released a first-of-its-kind P3 standard form agreement, P3-508 (www.ejcdc.org). The *Surety Bond Quarterly* reported on this document in the Winter 2014 issue.

My experience in privatized municipal wastewater P3 contracts includes acting as a private entity owner and manager, as well as a design-builder and operator of these systems. These experiences fostered my belief that the greatest potential for savings lies with the use of a private entity that will employ a true fast-track, design-build construction process, combined with a related operations group that has input to the design. Ideally, a single purpose firm would be best; but presently there are not many such smaller firms that have the requisite capabilities.

Thoughtful delineation of rights and responsibilities of public entities and private entities is critical

During the initial solicitation phase the public entity will need to be sure to develop a set of minimum standards to be used in both new plant and new collection system construction. The intent of these standards, which can be as simple as a few pages of general specifications, is to provide the proposers with the guidelines that will become part of the contract. By setting these standards, once under contract, the private entity can proceed with fast-track design-build phases as long as the standards are met.

As I had the opportunity to serve on the EJCDC task force that drafted EJCDC P3-508, which includes provisions incorporating concepts from my P3 experiences with small wastewater projects, I believe that document provides a reasoned delineation of public entity responsibilities and of the rights granted to and the responsibilities assumed by the private entity. Under this standard

agreement, the governmental entity grants a concession to the private entity to:

- Acquire the site
- Purchase or lease existing facilities
- Design and construct the new facilities
- Operate, maintain and manage the project facilities
- Generate and receive revenue from project facilities during the concession term
- Receive availability fees, or fees based on estimated usage and periodic fees (fees may flow from the user or the public entity)
- Finance and bear responsibility for the costs of such design, construction, operation, maintenance and management, pursuant to the terms of the contract
- Transfer the project facilities to the public entity at the close of the concession term

The most important part of a P3 contract to remember is that the responsibility is shifted to the private entity for all design, construction, financing, operation and maintenance of the facility or system. Another important item to remember is that all permitting lies with the private entity, even though existing permits may be transferred from the public entity.

Performance and payment security is important

Performance and payment security for the construction portion of the P3 project is important. The P3 contract should anticipate that the construction contract will include a requirement for performance and payment bonds, that the public entity will be furnished a copy of these bonds and that any sub-tier contractor providing services to the project will be furnished a copy of the payment bond.

Another critical matter to be addressed in the P3 contract is the treatment of revenues and financing. The P3 contract may provide for

varying types of fees to be received by the concessioner during the term of the contract. These may include new customer fees (sometimes called impact fees) recurring periodic fees, special fees and also fees that will flow to the public entity. In most cases, the final rate approval resides with the public entity as determined by applicable statutes and regulation. Provisions typically are included for escalation clauses

over the term of the contract as well as special rate adjustments due to changes in the law.

Other responsibilities of the private entity may include the following (although some of these functions may remain the responsibility of the public entity):

- Staffing
- Training and safety
- System and equipment operation
- Periodic inspection and monitoring

- Preventive and corrective maintenance
- Cleaning and waste removal
- Customer billing
- Meter reading
- Marketing and public relations

The P3 contract should provide a method for changing the concession term or the construction term as well as making changes to the scope of the construction or management items of work. The P3 contract also should address the circumstances in which the public entity may take over the concession, such as if the private entity becomes insolvent, files for bankruptcy protection, or fails to carry out its material obligations.

Never forget that P3s are partnerships

I have only the space to provide a cursory treatment of the myriad issues to be addressed in a P3 contract for a small municipal water project. A more complete picture can be achieved by reading EJCDC P3-508 Public-Private Partnership Agreement. Regardless of whatever is considered in the contract, however, always remember that small P3 water projects truly are partnerships. In my view, the public entity is not the customer. Rather, the customer is the public user being served by the concession. The public entity and the private entity must form a communicative working relationship, and the P3 structure should reflect this philosophy. In this way, the public and private entities will work together to deliver the concession to the customers at the lowest possible cost.

I can personally attest to successful use of P3s to address small waste-water infrastructure projects badly needed by localities. P3s for small infrastructure projects are not coming; they are already here. ●

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