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The nuts and bolts of a design-build partnership

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By Ken Peterson

Association: Design-Build Institute of America - Upper Midwest Region

A public-private partnership (P3) is a contractual agreement between a public agency (federal, state or local) and a private-sector entity. Through this agreement, the skills and assets of each sector (public and private) are shared in delivering a service or facility for the use of the general public. Each party shares in the risks and rewards potential in the delivery of the service or facility.

With the design-build-finance-operate (DBFO) approach, the responsibilities for designing, building, financing and operating are bundled and transferred to private partners. DBFO projects are partly or wholly financed by debt leveraging revenue streams dedicated to the project. Future revenue is leveraged to issue bonds or other debt that provide funds for capital and project development costs. They are also often supplemented by public-sector grants. Private partners may be required to make equity investments as well.

As the name implies, there are three components of a P3:

The owner or the public partner. Procurement regulations must allow the public owner to use alternative delivery systems. In many instances it may be desirable for a special- purpose public entity to be created to act as the public partner. Sports authorities, utility districts and local government organizations are often able to function as a public partner.

The private partner. The private partner may be a single company, but most often it is a team of organizations that have come together to execute the partnership.

The partnership agreement. The agreement between the parties is often complex and involves numerous documents, particularly if there is a private financing dimension to the project. It involves much more than a design and a construction agreement.

Several conditions are necessary for a P3 to be structured and considered an option:

A clear and sustained need for the project. The project must have a strong public need for the foreseeable future to justify funding.

A solid project scope definition. There must be no question as to the project scope - at least in terms of performance. Agreement on project performance requirements by the partners must be absolute.

The project must produce a product or a service that can be measured. Financing is almost always derived from the product or service produced by the project. Whether financing is provided by the public partner or the private partner, it is essential that the revenue stream from the project be quantifiable so that an appropriate financing mechanism can be set up.

The partners must be able to agree on how to share the project risk. The roles and responsibilities of the partners must be clear and complete for both sides and must be in writing. DBFO procurements can be expected to shift a great deal of the responsibility for developing and operating infrastructure projects to private-sector partners. Given the ability of public agencies to issue low-interest, tax-free debt, it is often more cost-effective for public project sponsors to issue debt than their private-sector partners. Because of this, public project sponsors using the DBFO approach often issue project debt themselves, but rely on their private partners to study the options for doing so and to recommend a final financing package. In such cases, the revenue risk may be passed on to the private partner or retained by the public project sponsor.

The project must have a strong political champion willing to confront the interest groups who may be opposed. There will be opposition from various interest groups who see the P3 as an infringement on their normal rights and responsibilities, and there must be a strong political champion willing to work with these groups to mitigate their concerns.

Even in the best of times, government agencies are challenged to keep pace with the demands of their constituencies. During periods of slow growth, government revenue frequently is not sufficient to meet spending demands, necessitating painful cuts or tax increases. Partnerships can provide a continued or improved level of service at reduced costs and provide the capital needed for the construction of major facilities.

If you are interested in finding out more about design-build, the DBIA-Upper Midwest Region invites you to our upcoming annual awards program at 7:30 a.m. March 16 at Midland Hills Country Club. More information about the program and registration information can be found at www.dbia-um.org or by contacting the DBIA-UMR office at 952-928-7471 or info@dbia-um.org .

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