Public-Private Partnerships: Considerations for Design Professionals

Mark Kalar

CM-at-risk, Design-Build, IPD, . . . P3? In the sometime quixotic quest to find the perfect project delivery method, Public-Private Partnerships (P3) represent a radical new development. Other delivery methods allocate risk and responsibility among the owner, architect, and contractor. P3, on the other hand, takes the “owner” out of the contractual web altogether, introduces a central developer/operator/financier figure, and makes predesign and post-occupancy phases more than just bookends to the main event.

While P3 supporters promise an influx of innovation and cash to public construction projects, there are cautionary tales, especially for design professionals. As procurement laws get rewritten across the country, architects and engineers, and the attorneys who represent them, need to work hard to make sure changes are made thoughtfully and carefully.

What are Public-Private Partnerships?
Public-Private Partnerships are contractual agreements between state or local public bodies and private sector entities (usually a partnership between an investment firm and a developer). In theory, both sectors share their skills and assets to the benefit of the public, and each shares in a project’s potential risks and rewards. The classic “horizontal” P3 project is a toll road: a private entity provides financing and operates tolls to recoup its costs.

For “vertical” construction (i.e., buildings) the private entity typically provides financing and design, builds the project, and then assumes responsibility for its condition and performance for the life of a long-term lease agreement with the public body, including maintenance and operation of the building. Often, the public body takes full possession at the end of such a lease (a “Build/Operate/Transfer” transaction), although the transfer could take place earlier or not at all.

The public body gets to defer its payments until construction is complete, and then can spread them out over the length of the lease. Politically, this avoids the inevitable bonding showdowns and lets lawmakers push project costs into future operational budgets. It is not hard to see why this delivery method is being embraced by state legislatures.

One of the hallmarks of the P3 process is that design teams have been required to participate in unpaid competitions to be selected by investor-developer clients for P3 projects. Because these tend to be large, complex projects, design teams often must risk hundreds of thousands of dollars in design service fees in hopes of winning the work.

Examples of P3 Projects
A recent Canadian example is the Alberta Schools project. The entire project
constituted forty new schools designed and built over a six-year period. The schools were bundled into three sub-projects, under three contracts, for design, build, finance, and maintenance. Each school is being leased back to the Canadian government under a thirty-year lease. Three different special-purpose investor-developers were involved. In at least one case, the investor-developer, BBPP Alberta Schools Limited, reportedly suffered significant financial losses due to the debt load incurred by the project. Such losses have not had a significant impact on BBPP’s most significant owner, International Public Partnerships Limited, however. Although there has been controversy over transparency and accountability, the government estimates that using P3 saved Alberta’s taxpayers $2.2 billion.

The New Karolinska Solna University Hospital in Sweden is, at roughly $3 billion, the world’s largest P3 hospital. Although it has not been without its own share of accountability controversies, New Karolinska Solna is also being praised for its sustainability features and innovative healthcare design. Another P3 success story is the Long Beach Courthouse in California. This project featured a thirty-five-year leaseback period, after which the building will be owned by the state. In addition to rents, for its roughly $500 million investment, the investor-developer group received a significant first-year fee payment of $54 million. Project costs were estimated to be 15% cheaper than a traditional design-bid-build project would have produced, with a thirty-month schedule savings.

On the other end of the spectrum, the Indiana East-West Toll Road offers a cautionary tale. A Spanish-Australian conglomerate purchased the rights to maintain and operate the stretch of I-90 running along the northern boundary of the state. The deal put $3.8 billion in state coffers in exchange for the rights to collect tolls for 75 years. Unfortunately, the investor-developer was forced to file bankruptcy to restructure its $6 billion of debt when traffic volume fell short of predictions. Evidently, the investors are still convinced of the potential, since the Australian half of the company paid $5.7 billion to reinvest and collect tolls for the remaining sixty-six years of the arrangement.

**Why Design Professionals Should Be Promoting P3**

For design professionals, the positive angle here is obvious: adding private capital as a funding source will almost certainly result in more construction, generally. That the public money can be deferred and paid out of operations budgets makes these public projects less prone to protracted, unpredictable bonding battles.

There are other benefits to P3. Unlike other delivery methods that end when the owner moves in, the P3 investor-developer is in it for the long haul. Such a long-term building owner has incentives to make decisions based on quality, not just cost, if only to minimize maintenance expenses. This more realistic assessment of total lifetime cost impacts of design decisions will likely lead to results aligned with most design professionals’ sustainability and quality goals.

One of the most touted features of P3 is that it encourages innovation. Because most state P3 statutes allow for unsolicited proposals, investor-developers can be on the lookout for opportunities without having to go through the often onerous bureaucratic process of identifying unmet needs and going through master planning or long-term facilities analyses. Likewise, because most regulations in public construction are tied to funding, relying on private capital opens avenues in approach, design, and construction that may otherwise be closed by well-meaning but possibly overly conservative restrictions.

**Why Design Professionals Should Be Resisting P3**

More construction, spurred on by more capital, is obviously of benefit to design firms. But this benefit carries costs, too. The most significant is that the competition selection process excludes all but the biggest firms from even trying to get the work. Most design professionals cannot afford to front the hundreds of hours’ worth of services necessary to get through an unpaid competition. This means only the few biggest firms will be able to compete—leaving smaller design firms in the cold.

In many instances, even small public projects have been bundled together into larger multi-project packages to entice larger investor-developers, or get more competitive prices from contractors. While perhaps logical goals of themselves, they run contrary to many states’ goal of providing work to a diversity of firm sizes and types. As implemented to date, state procurement goals usually do not find their way into P3 legislation.

One of the ostensible benefits of P3—the deferment of funding battles—can also be a detriment. While the political battle over a single large bonding request is eliminated, funding instead becomes a political issue every session, as operational budgets are vetted and subsequent generations of politicians have the opportunity to consider whether to honor the decisions made by their predecessors as they decide whether to increase those budgets.

In some instances, the entire funding scheme has been based on projections, especially where user fees are the future funding mechanism. Like any projection, there is an element of risk that the projections are based on faulty data or unforeseen conditions will disrupt the plan. Likewise, escalating prices or changes in the market can leave investor-developers without a maintenance budget, or passing along unexpectedly high rents to local governments. Betting on future prices is always a gamble. Before signing on to a long-term commitment, all parties need to make sure they understand the risks and the underlying assumptions.

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Diversity and Inclusion: “One Person at a Time” Starts with Each of Us

William M. Hill

Five simple words: “One person at a time.” That’s how Carla Christofferson, EVP and GC of AECOM, and the Forum’s diversity speaker at the 2016 Midwinter Meeting described her approach to achieving organizational diversity and inclusion. There are mountains of statistics. One is that by about 2043, the U.S. will be a majority minority nation – meaning more than half of our citizens will be non-Caucasian. But those five simple words can move mountains if brought to bear by those of us who care. And each of us in the Forum should care.

Industry groups, consultants and businesses have been learning that they are smarter, faster and more nimble by welcoming employees from diverse backgrounds around the table, onto a project, or into the idea stream. A majority of Fortune 500 executives have agreed that a diverse workforce is crucial to encouraging different perspectives and ideas that foster innovation. Anyone working in a law firm knows that our successful clients are demanding diversity in their legal teams. Within the construction industry, newly formed companies are, as never before, owned and operated by women and minorities. Lots of data leads to a simple paradigm: diversity and inclusion makes an enterprise better. That means us.

There is a lot of work for the Forum to do to get better. One benchmark of this data counts — in Architect/Engineering/Construction firms — women at about 30% and minorities at 15%. The Forum has a way to go to achieve progress on that industry statistic: About 19% of our rank and file members are women and about 90% of all members are Caucasian. While we have a much better story to tell about the diversity of the Forum’s leaders, speakers, authors, and meeting attendees (Diversity Chair Dave Theising has worked hard to assemble that data), the point is that we need to do better making the Forum look more like the world in which we are working, competing and growing.

To Build the Best Construction Lawyers we need a professional home for women, minority, LGBT and disabled attorneys and associate members. It is also vital if we are to maintain our hard fought reputation as thought leaders in construction law. In working on issues of diversity in private sector and non-profits, I’ve often seen that when you take the foot off the accelerator, you don’t just slow down but can start going backwards. And as successful as the Forum has been in attracting and keeping members (we’ve been among the ABA’s leaders on that), we can’t afford to take our foot off the gas on diversity. We need to press down.

It is within each of us to move the meter on the diversity. I bet you know women, minority, LGBT, and disabled persons who could not only benefit from Forum programming and publications but could provide all of us benefits by their inclusion as authors, speakers or attendees at meeting. Reach out and touch them. Ask. It starts with each one of us: one person at a time.

WILLIAM M. HILL, Mintz Levin, Boston, MA

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The following additional articles appear in Under Construction Online together with the complete version of all articles in this issue.

- **Best Practices for General Counsel Driven Diversity Initiatives** by Shiva S. Hamidinia, Briglia McLaughlin, PLLC
- **Why Power Plant Construction Claims are Different and How to See Them Coming** by Peter G. Hessler, Construction Business Associates, LLC, Division 5, Project Performance
- **Liquidated Damages Awarded Despite the Owner’s Termination for Convenience, Owner’s Contribution to Delays, and Owner’s Lack of Proof of Actual Damages** by Laurann Asklof, Shipman & Goodwin LLP, Hartford, CT, Division 12, Owners & Lenders
- **How Well Do You Know Your Construction Job Site? Recent Developments in the “Common Workplace Doctrine”** by Patrick Sweeney, Rhoades McKee PC
- **The New “Science” of Pre-Arbitration Evaluations** by Daniel E. Toomey, McManus Felsen, LLP and Michael E. Cobo, DecisionQuest
- **Allocation of Insurance Coverage for Long-Tail Losses** by Marc Sanchez and Mike Frantz, Jr., Frantz Ward LLP, Division 7, Insurance, Surety & Liens
The U.S. Court of Appeals for the Third Circuit recently held that an owner of a construction project may not evade a contractual notice-to-cure provision unless the contractor commits an incurable breach of contract. A material breach by the contractor is not enough to excuse non-compliance with the cure provision unless the breach is also incurable. Because the performance bond surety was entitled to the same notice-to-cure protection, the owner’s claim against the bond was voided. Milton Regional Sewer Authority v. Travelers Casualty & Surety Co. of America, 2016 WL 1697091 (3d Cir., 2016).

Read the full article at http://ambar.org/FCLUC.

PATRICK R. KINGSLEY, Stradley Ronon Stevens & Young, LLP, Philadelphia, PA
Stephen Walker — A Construction Lawyer’s Construction Lawyer

Stephen Walker parlayed his degree in civil engineering into a law degree by attending the night school program at Duquesne University while working as a bridge engineer for the Pennsylvania Department of Transportation in the late 1960’s. He was admitted to practice law in Pennsylvania in 1971, but soon moved to New York City after hearing that it was the only place where, at that time, you could specialize in construction law. He joined the ABA shortly after graduating law school in 1971, and joined the Forum on Construction Law as soon as it was available.

Steve has spent his entire career in construction law. He began as an associate at Sacks, Montgomery, Molineaux and Pastore before becoming in-house counsel for Perini Corporation in 1975. Perini moved Steve to the West coast in 1979, promising him that he could return to his beloved East coast after three years. However, by 1982, Steve and his wife had fallen in love with the West coast and instead of returning to Boston with Perini, he took a job at Guy F. Atkinson Company. In 1988, he moved to Bechtel Corporation, and entered semi-retirement in 2014. He now works out of their San Francisco office two days a week, still showing up at 5 am.

While Steve has only attended a handful of meetings throughout his time in the forum, he has maintained a library of every copy of The Construction Lawyer since it was first published in 1980. He has even published a few articles himself: “Statutory Responses to ‘No Damage for Delay’ Clauses” in the April 1986 issue; and “Practical Alternatives When Your Subcontractor Client Cannot Bond” as a co-author in the August 1988 issue. He also was principal editor for Aspen’s 50-State Architect, Engineer and Contractor Licensing Book.

Steve is a strong believer in the ADR process, and has been an arbitrator with the AAA since the mid 1970’s. His advice to outside counsel? There are a lot of excellent firms out there, so it is hard to sell yourself on your expertise. Responsiveness, on the other hand, varies greatly. What in-house counsel needs is a responsive firm that delivers only the information they need, when they need it.

In his off-time, Steve likes to bike. He used to do a lot of triathalons. Much like practicing as in-house counsel, he enjoyed the variety of exercise and challenge that such a varied competition brings. Now that he is semi-retired, he settles for century rides, or short, 65-mile training rides.

WESLEY BONNHEIM, Papich Construction Co., Inc., Division 11, Corporate Counsel

The Publications Committee requests that anyone with experience teaching a construction law course complete a survey regarding the Forum’s Casebook, Construction Law (William R. Allensworth, Ross J. Altman, Allen L. Overcash, Carol J. Patterson, ed., 2009).

Survey: https://www.surveymonkey.com/r/CHFMMV9
Stay “Current” by Reading and Writing for Under Construction

Jayne Czik

When reviewing the table of contents for this issue of Under Construction, it struck me just how much we construction law attorneys need to stay abreast of to remain useful to our clients. One of the best ways to stay current is to read Under Construction. This summer’s edition includes a wide array of issues ranging from the New Science of Pre-arbitration Evaluations to Best Practices for General Counsel Driven Diversity to Recent Developments in the “Common Workplace Doctrine.” You never know what a client may ask you for assistance with and you want to ensure you’re familiar with the issue. Besides reading an article, what better way to stay current than by researching and writing an article? Even if it’s writing a human interest story like this issue’s Member Feature on Stephen Walker, you’re bound to learn something new.

I’d also like to urge you to let Tom and I know how Under Construction can be more useful to you and help you stay current in your practice.

JAYNE CZIK, Citnalta Construction, Bohemia, NY, Division 13, Government Construction

Society recognizes that individuals with specialized training and experience have unique expertise beyond that possessed by the public at large. The alignment of parties under P3 takes that professional expertise away from the end users. In many ways, this puts public governments in circumstances similar to that of a pro se litigant. Although such entities are “owners” of their projects in the sense that they are the ultimate occupants and users of their buildings, they are part of a process with which they are probably unfamiliar, negotiating with other parties who are both more experienced and have the expertise of design professionals at their disposal.

Depending on the lease agreement, the long-term commitment of the investor-developer may be less meaningful than as described above. If maintenance and utility costs are passed along to the public entity lessor, there is little incentive to invest in quality or sustainability. This tendency is exacerbated by the lack of oversight and policy implementation that comes without a legislative vetting process. In short, there will be little to counteract the short-term incentive to favor short-term cost-saving measures at the expense of long-term performance.

Finally, P3 raises liability concerns for design professionals. The Beacon case has brought to our attention again that architects owe a duty to future owners, regardless of who signs the processional services agreement. While the condominium market obviously has many other risk factors leading to excessive litigation, P3 sets up a similar set of relationships. Design professionals will be contracting with investor-developers with interests at odds with the interests of the public entities who will be using the spaces. Although we are typically dealing with leaseholds in P3, it is still easy to imagine a court finding an obligation connecting the public entity and the architect—especially since that is whom the architect is naturally predisposed to perform its work.

By working for the investor-developer, design professionals become subcontractors. This raises issues related to standard of care, insurance, and professional responsibility. While this problem is hardly unique to P3, the solutions that have been carefully crafted over decades of design-build, for example, will not necessarily transfer directly.

Whereas design-build still contemplates an owner in the traditional sense, P3 projects are built in anticipation of a tenant, renting the building from the investor-developer. What is the standard of care for such a project, especially as it relates to ongoing post-occupancy maintenance? Will investor-developers agree to limit design professionals’ liability within its traditional boundaries? And perhaps more importantly, what will professional liability insurance cover?

Conclusions/Recommendations

Given the problems associated with P3, it will be important for design professionals and their attorneys to make their voices heard as public procurement laws get re-examined and rewritten. Following are some approaches that can be used to take advantage of P3’s benefits while minimizing the potentially deleterious effects on the public.

One is to provide an independent “architect as advisor” model to represent public interests. In such a
scenario, the public entities in P3 projects would be required to hire an architect to assist them in a limited role throughout the process. This would benefit the investor-developer as well, since having an informed tenant with the advantage of professional advice is likely to minimize risks of lawsuits alleging misrepresentation or breach of duty to the tenant.

A strategy used in Canada is to require a value-for-money analysis to demonstrate viability of any proposed P3 project. Establishing a specific level of due diligence will not reduce all the risk of uncertain future funding streams, but it would at least temper overly optimistic investor-developers’ and public representatives’ enthusiasm for risky projects.

P3 legislation should also require qualification-based selection processes for contractors and designers. Quality-based selection has been embraced by the federal and most state governments as means of balancing experience and cost. Quality-based selection has been shown to reduce construction costs, shorten construction schedules, and encourage participation by small design firms. Any changes to procurement laws should protect the use of this proven system.

While it is probably inevitable that local governments will embrace P3, such a delivery method should supplement, not replace, traditional funding. For significant projects, the oversight and direct control afforded by a traditional design-bid-build method are irreplaceable. Legislators should strive to find a balance between providing oversight and allowing the market to find architectural solutions.

By reining in the most laissez-faire excesses of P3, public agencies can reap the benefits of P3 without abdicating their responsibilities to the public. Design professionals and their attorneys should do their part to shape that conversation. When confronted with P3 projects, design professionals should also be wary of taking on excess liability and should take care to understand who their client is, and to whom they owe their loyalty.

MARK KALAR, Cuningham Group Architecture, Inc., Minneapolis, MN, Young Lawyers Division

Endnotes
7. International Public Partnerships LD Fund Factsheet, Interactive Investor (April 4, 2013), http://www.iili.co.uk/research/LSE/INP/News/item/677535/ additional-investment-alberta-schools (noting that IPP’s re-investment following BBP’s losses “has been performing well and the additional investment is expected to be accretive to the overall portfolio.”).
9. P3 Projects in Alberta, supra note 5.
17. For a general discussion of risk allocation in P3, see Harry Z. “Zack” Rippeon, Risk Allocation in P3s, Common Sense Contracting, supra note 16.
I Should Have Known Better Construction & Design Defects & Project Delays

Please save the date, and make your reservations early! It’s on to Chicago for the Forum’s Fall Meeting which will take place at the Swissotel on October 6 and 7, 2016. Chicago is particularly spectacular in the fall, and the meeting, “I Should Have Known Better – Construction Design Defects & Delays”, will include eight action packed Plenaries. The first day will feature a Life of the Project Video that will be used in the first two plenaries, a plenary on insurance issues (what’s hot and what’s not) and a plenary on contract clauses you need to know about. The day rounds out with a presentation on cutting edge technology (the drones are coming!). The second day then will include a delay claim presentation, a stellar panel of state and federal judges and an interactive ethics presentation!

We truly are honored to have Robert Grey, Jr. Past President of the ABA and President of the Legal Council on Legal Diversity speak at our Diversity Breakfast. As always, networking opportunities will abound! There will be a construction law practicum on arbitration, a first time attendee’s welcome and kickoff, an exhibitor reception, division lunches, a women’s networking reception and a welcome reception.

We have tons of fun planned as well – Second City Comedy Theater is ours for a night, and we have reserved the Chicago Architecture Foundation River Cruise. There even will be burgers and beer at the World Famous Billy Goat Tavern to top off the deep dish pizza you won’t be able to avoid. Please accept our invitation to join us for The Forum’s fall meeting in Chicago on October 6 and 7, 2016! See you there!

Register: http://ambar.org/FCLCHI2016; #FCLChicago

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