P-7 P-7

ISSN 1180-4327

Legislative Assembly
of Ontario

First Session, 41st Parliament

Assemblée législative
de l'Ontario

Première session, 41e législature

Official Report of Debates (Hansard)

Wednesday 25 March 2015

Journal des débats (Hansard)

Mercredi 25 mars 2015

Standing Committee on Public Accounts

Comité permanent des comptes publics

2014 Annual Report, Auditor General:

Infrastructure Ontario

Rapport annuel 2014, vérificatrice générale :

Infrastructure Ontario

Chair: Ernie Hardeman
Clerk: William Short

Président : Ernie Hardeman
Greffier : William Short

Hansard on the Internet

Hansard and other documents of the Legislative Assembly can be on your personal computer within hours after each sitting. The address is:

Le Journal des débats sur Internet

L'adresse pour faire paraître sur votre ordinateur personnel le Journal et d'autres documents de l'Assemblée législative en quelques heures seulement après la séance est :

http://www.ontla.on.ca/

Index inquiries

Reference to a cumulative index of previous issues may be obtained by calling the Hansard Reporting Service indexing staff at 416-325-7410 or 325-3708.

Renseignements sur l'index

Adressez vos questions portant sur des numéros précédents du Journal des débats au personnel de l'index, qui vous fourniront des références aux pages dans l'index cumulatif, en composant le 416-325-7410 ou le 325-3708.

Hansard Reporting and Interpretation Services
Room 500, West Wing, Legislative Building
111 Wellesley Street West, Queen's Park
Toronto ON M7A 1A2
Telephone 416-325-7400; fax 416-325-7430
Published by the Legislative Assembly of Ontario

Service du Journal des débats et d'interprétation
Salle 500, aile ouest, Édifice du Parlement
111, rue Wellesley ouest, Queen's Park
Toronto ON M7A 1A2
Téléphone, 416-325-7400; télécopieur, 416-325-7430
Publié par l'Assemblée législative de l'Ontario

LEGISLATIVE ASSEMBLY OF ONTARIO

ASSEMBLÉE LÉGISLATIVE DE L'ONTARIO

STANDING COMMITTEE ON PUBLIC ACCOUNTS

COMITÉ PERMANENT DES COMPTES PUBLICS

Wednesday 25 March 2015

Mercredi 25 mars 2015

The committee met at 1230 in room 151, following a closed session.

2014 ANNUAL REPORT, AUDITOR GENERAL

INFRASTRUCTURE ONTARIO

Consideration of section 3.05, Infrastructure Ontario—alternative financing and procurement.

The Chair (Mr. Ernie Hardeman): We'll call the Standing Committee on Public Accounts to order. We're here this afternoon for the consideration of section 3.03, Financial Services Commission of Ontario—no; wrong one. Hold on a minute.

We'll correct that. We're here for the consideration of section 3.05, Infrastructure Ontario—alternative financing and procurement, from the 2014 annual report of the Auditor General.

We thank you gentlemen at the end of the table for coming in from Infrastructure Ontario. We welcome you, and we would ask you to introduce yourselves for Hansard as any one of you speaks for the first time. At that point, Hansard will keep us in line, to make sure they know who to attribute the comments to.

We thank you very much, first of all, for coming in and helping us with this review. We've allocated 20 minutes to hear the presentation from Infrastructure Ontario. At that point, we will have questions and answers. This time, we start, I think—

The Clerk of the Committee (Mr. William Short): The NDP.

The Chair (Mr. Ernie Hardeman): —with the third party. Thanks for the help, Clerk. We'll have 20-minute rotations to consume the time.

With that, again, thank you for coming, and the floor is yours.

Mr. Giles Gherson: Thank you very much, Chair. I'm Giles Gherson, Deputy Minister of Economic Development, Employment and Infrastructure, province of Ontario. Thank you for the introduction.

I'd like to thank the committee for inviting me here today, and the Auditor General for her thorough review of alternative financing and procurement, or AFP, as it's called.

I'd like to share the time allotted for opening remarks with Infrastructure Ontario's chair, Mr. Tony Ross, who is to my immediate right, and IO's president and CEO, Mr. Bert Clark, to his right.

AFP is being used to successfully deliver much-needed major infrastructure projects right across Ontario, from courts and jails to highways and transit. AFP is a highly disciplined, rigorous procurement approach that fosters innovation, gets infrastructure projects completed on time and saves the province money over the life cycle of the asset.

At the outset of my remarks, I think I should address what has become a major focus of media attention following the Auditor General's review; namely, what was taken to be $8 billion in higher costs attributed to AFP projects, compared to traditional build. I believe this single number, used in isolation, has severely distorted the discourse around alternative financing and procurement and misrepresented what the report said.

The Auditor General's report clearly states that the $8-billion cost was more than offset by the costs of the risks typically associated with the public sector directly contracting the construction and maintenance of major infrastructure. I'd like to drill down on this offset point.

I'm sure the committee appreciates that the building of any major infrastructure projects comes with risks such as delays, flaws, scope changes and substandard long-term maintenance that translate into actual cost increases, so it needs to consider another crucial number: the $14 billion in transferred risks associated with 74 large infrastructure projects built using AFP.

The report, in fact, confirms that through the AFP model, the government spent $8 billion to transfer $14 billion of project construction, repair and maintenance risk to the private sector. It bought an insurance policy, if you like, to protect taxpayers from overruns, delays and flaws that history shows are endemic with publicly built and managed projects, not just here, but around the world—everywhere.

As a result, there has been a net saving of more than $6 billion. That's what the math shows. This $6 billion in savings to taxpayers has allowed the government to further invest in other important infrastructure projects. This is why the government was troubled by the attention given exclusively to the $8 billion in perceived additional costs associated with AFPs, related to risk transfer to the private sector.

Since 2005, some of the largest, most challenging projects have been delivered through AFP, a made-in-

Ontario form of public-private partnership. AFP is not privatization, but since private sector money is involved, and on the hook so to speak, companies have a very large incentive to manage projects effectively. As a result, AFP has established a track record for delivering major projects on time and on budget, with the private sector committed to appropriately maintaining them in the long term. And that's where the government reaps significant savings.

Every AFP project in Ontario has been procured through a highly competitive process. On every project, an average of five to seven bidders participate in the process. These are shortlisted to three finalists, each of whom has the technical expertise and capacity to develop the project. The winning bidder is chosen based on their responses to the RFP, which includes both technical specifications and pricing.

A recent third-party review found that the winning AFP project bids are typically 10% lower than the average bid and 19% lower than the third-place bid. Competition clearly drives bidders to lower pricing.

Regardless of the number of companies taking the lead role in an AFP, there are thousands of smaller local subcontractors across the province that participate in each project.

There is another benefit to this model: AFP project teams drive innovation in the construction of infrastructure. They are given a high-level idea of what the infrastructure needs to accomplish, rather than highly prescriptive technical instructions on what should be built, as is the case with a traditional build. They are told, for example, that a hospital must be able to serve 5,000 patients a day, that it must have parking for 2,000 cars and incorporate natural light and pleasant views. Developers then assemble a team of experts and figure out the best way to accomplish those goals, both in terms of construction and design. This is an inherently innovative process.

Consider St. Joseph's Healthcare Hamilton West 5th Campus: The winning bidder took an innovative approach to the layout of the facility and created significant value. They proposed building the facility to account for the natural contours of the land. This allowed them to build a more compact building. That shortened the construction schedule and lowered construction costs. In fact, the winning bid was fully 27% lower than the average of all bids. It also was evaluated as the best design.

The point here is that innovation in project design and construction is one big benefit to the AFP model. Protecting the taxpayer is another. The government developed the AFP model because the broader public sector has, frankly, a less-than-stellar record, here as elsewhere, in delivering big projects on time and on budget. This is important because the Ontario government is planning to invest over $35 billion in infrastructure over the next three years. Using the AFP approach for large, complex projects, Ontario expects to reduce costs and save money over the life of these projects.

Most of Ontario's public infrastructure continues to be delivered through conventional procurement methods, but experience shows that this method can be subject to significant risk, not least of which are government budgetary pressures these projects can become subject to. Consider the Brampton courthouse, which actually was in the paper today. Designed to serve the needs of a rapidly growing community, for budgetary reasons, the building was scaled back by two floors once construction had begun. The result today is a relatively new building struggling to serve the actual demand for space. Under AFP, and the transfer of risk over a 30-year period, the building plan would have been locked in, protected from the uncertainty of annual budget cycles, costly scope changes and so forth.

Additionally, government budgetary pressures can detrimentally manifest themselves in the form of deferred or delayed maintenance on public buildings. This happens the world over. Unfortunately, there is no shortage of public sector buildings across the province today that would have much greater value and life span had they received consistent maintenance funding in the decades since they were brought into service.

Under the AFP model, the contractor is often responsible for maintaining the infrastructure for 30 years. At the end of this period, the facility must be transferred back to the government in good working order. The point here is that the AFP model has built-in safeguards against poor asset management practices.

While AFP may seem to be more expensive at the outset, when we use AFP, government is not typically on the hook for delays or cost overruns. That burden falls on our construction partner, and that means they work harder to meet the deadlines and keep costs down. A good example of AFP working to protect the taxpayer is the Windsor parkway project. During the construction of the parkway, it was discovered that substandard girders were being used. Ultimately, more than 300 girders were replaced to address concerns of durability. As a result of the strong contract provisions in place, the developer paid the entire cost to remedy the problem. There was no cost to the taxpayer.

The truth is you can't put a shovel in the ground on major infrastructure projects without having some surprises. The question is, who should bear the costs and risks? Alternative financing and procurement is a tool designed to protect taxpayers from the risk of cost overruns and delays. It has done so over the past decade, with $6 billion saved when you subtract the total risks from the actual amount spent.

1240

It is true that we don't precisely know, and won't know for some time, the true cost or benefit of transferring risk on AFP. While AFP has been around for 10 years, the major infrastructure projects constructed under this procurement model have a life of 30 or 40 years or more. If flaws emerge in five, 10, 15 or even 20 years, the cost will fall on the builders, not on the taxpayers.

So Infrastructure Ontario and the Ministry of Economic Development, Employment and Infrastructure are committed to implementing the recommendations from the Auditor General's 2014 annual report. And I want to say, they are helpful and positive. The AFP process, and indeed, public procurement generally, are on a journey of continuous improvement. The AG provided useful advice that we are reviewing closely, and we accept her suggestion that there needs to be better data analysis. We're giving serious thought to ways of refining the criteria for when to use AFP and determining the appropriate threshold level for when AFP makes sense. Mr. Clark will go into more details in his remarks. We want to ensure that Ontario continues to be the leading jurisdiction for modern methods of infrastructure policy, procurement and delivery.

As the auditor says in her report, the track record of IO and AFP is strong. In the past decade, there has been significant improvement in the number of projects coming in on budget and on time. IO and the AFP model bring discipline, rigour and controls to projects that previously were prone to rethinking or redesign late in the game, changes that led to deadlines being missed and cost overruns.

Perhaps a good indication that this model is working is the interest in the international community in emulating it. Several US states, the US government and 40 jurisdictions around the world have all expressed interest in adopting the AFP process and are looking to Ontario's model. The AFP model has helped position Ontario companies to compete for business in other countries and export their expertise around the world.

I look forward to answering the committee's questions with my colleagues. Before I do, I would like to invite Infrastructure Ontario's chair, Mr. Tony Ross, to offer a few opening remarks on behalf of IO's board of directors. And here, I would like to note for the record the very high quality of IO's board and the seriousness and thoroughness with which it engages its work. They are putting their significant private sector expertise in finance, engineering, law and procurement to work in the public service.

Now I'd like to ask Mr. Ross and Mr. Clark to offer further insight into IO's work and how it is addressing the recommendations of the auditor.

Mr. Tony Ross: Good afternoon. My name is Tony Ross. I have been chair of Infrastructure Ontario's board of directors since the agency's creation in 2005. I appreciate this opportunity to appear before the committee and to discuss Infrastructure Ontario's work and accomplishments on behalf of the province.

Infrastructure Ontario has a diverse and highly experienced board, whose members consider it a privilege to contribute to the building and maintenance of Ontario's public infrastructure. Our role as board members is to ensure consistency with IO's core mission: to ensure that our projects deliver value for money, that we uphold principles of transparency and accountability and that we protect the public interest in all of our operations. Above all, we work to ensure the government's and the private sector's confidence in our ability to deliver upon what we promise. I can assure you that our board takes our responsibility to the government, to our clients, to our partners and to the people of Ontario very seriously.

The alternative financing and procurement model was created in order to reduce the potential for cost overruns and schedule delays by transferring risk to the private sector. Our board views the AFP model as the most responsible, effective approach to the delivery of large, complex projects that carry such risks.

The board does not approve proceeding with a project, including using AFP, unless the overall benefit of transferring risks outweighs the overall cost, including the cost of private financing. The process is rigorous, and the review by the board of directors is thorough.

The board of directors has reviewed the Auditor General's findings relating to the AFP program. We have assured our minister that we will oversee the prompt implementation of the report's recommendations.

In particular, we agree that our success with the AFP model can be leveraged to further improve risk management on projects where traditional delivery methods are employed.

IO is committed to building on its track record by continuously adapting and improving how it operates. The board of Infrastructure Ontario has confidence in the capabilities of IO's management team and is committed to ensuring continued delivery of strong results in a manner that protects the public interest.

Thank you for this opportunity to address the committee. I know that we are all eager to answer any questions you may have on AFP and how we deliver value for money to the people of Ontario.

Mr. Bert Clark: Good afternoon. My name is Bert Clark. I'm the president and CEO of Infrastructure Ontario. I'd also like to introduce Ehren Cory and John McKendrick, who is seated with his hand up, two of our executive vice-presidents.

Thank you for the invitation to speak with you today. I also want to thank the Auditor General. We believe the 2014 report makes a significant contribution to the healthy ongoing discussion around how the province delivers its infrastructure. We believe the report correctly acknowledges our strong track record and the fact that AFP has a role to play on larger, more complex projects.

The report also helps steer project managers toward the right questions to ask; namely, which projects are appropriate candidates for P3 or AFP and how much private finance is required to transfer risk?

It's probably worth pausing to explain what AFP is. At its core, it's simply a series of very simple changes we made to deliver projects that address the root causes of most cost overruns.

First, we do not break up large projects into smaller projects and tender them separately. Breaking up projects leaves enormous risk with the public sector. The Big Dig in Boston in the best example of what can happen when the public sector is trying to integrate many separate projects. That project increased from a budget of approximately $3 billion to $15 billion.

Second, we do not pay until projects are complete, or at least we try and limit the amount we pay until completion. This gives us tremendous leverage when disputes arise, and they invariably do on large projects. In the past, builders had all the leverage because they had nothing invested in our projects. They could threaten to walk if disputes were not resolved in their favour. We have now leveled the playing field.

Third, we require builders to design the projects to meet our specifications. This eliminates one of the major sources of cost overruns in the past: change orders to deal with deficiencies in designs. Now, when there are design issues, the builder must resolve them at their cost.

Finally, we hold builders accountable for the long-term quality of the asset by paying them a portion of the construction cost over time. If buildings don't last well, we don't pay for the cost of addressing the performance or durability issues.

Since our establishment 10 years ago, our major projects division, run by John McKendrick, has completed 46 projects; the construction value was over $10 billion. A review of the track record conducted as of last March confirmed that 97% of the completed projects were on or below budget; 73% of those projects were delivered within a month of their scheduled completion date. This is a very strong track record.

We're not alone, however, in deploying modern project delivery techniques in order to better align public and private interests and protect the public sector from the risks associated with large projects. Both Australia and the United Kingdom have done so for quite some time, and both of those jurisdictions are already ahead of us in terms of collecting comparative data documenting the relative success of modem project management techniques such as AFP or P3 versus more traditional approaches.

As a result, there is a growing body of evidence that P3s provide the public sector with strong protection from cost overruns. For example, in 2008, the University of Melbourne published a paper which concluded that final costs were, on average, 4.5% more than the original contract price for P3s versus 18% for traditionally delivered projects. The Australian results for P3s are consistent with the results set out in our March 2014 track record, which I referred to previously.

And there are regular reports in Canada of traditionally delivered projects that have significantly exceeded their budgets, often by more than the 18% average. For example, the last large hospitals the provincial government delivered using traditional means were 75% and 150% over budget. Over the coming year, we're going to be working with the ministry to collect this Canadian and global empirical evidence.

Let me conclude by reiterating what I said at the outset. The right questions to ask when it comes to AFP are, which projects, and how much private finance? Our experience and that of countries such as the UK and Australia confirm that modern project delivery techniques like AFP and P3s protect the public sector from cost overruns. As people think about and discuss AFPs, the real question is how to use the technique in a cost-effective manner.

1250

In that regard, we're working with the ministry to review the screening threshold for future AFP projects given the project management experience IO has gained over the last 10 years and the experience of other Canadian jurisdictions. We constantly look for opportunities to reduce the amount of private finance in each of our transactions in order to reduce the cost of risk transfer.

Thank you very much for the opportunity to appear before you today. We would be pleased to respond to your questions.

The Chair (Mr. Ernie Hardeman): Thank you very much. That pretty well concludes the 20 minutes. We'll start now with questions from the third party. Ms. Fife.

Ms. Catherine Fife: Thank you for being here today. I think the Auditor General's report really garnered a lot of attention for many reasons. And I agree: The $8-billion number is really shocking. I think it's incumbent on all of us to peel back the layers and get to the core of that issue.

I want to start off, though, by asking you—the Auditor General met with you. She consulted with Infrastructure Ontario. Obviously, you were very involved in the review because she was going through your documents. You responded in the report to some of her recommendations, expressing some interest and validating some of her findings.

Then, on December 5, though, you wrote a letter to the Minister of Economic Development, and it was a very defensive letter, I have to say, and it was very political. You challenged some of the findings, especially around risk transfer and around the cost of borrowing money.

I guess I'm wondering, why did you not raise these issues with the auditor throughout the entire process so that Infrastructure Ontario—if you have the empirical data, for instance, to justify the cost of risk transfer, why was that not embedded in your response contained within the report?

Anybody can answer.

Mr. Bert Clark: You're referring to the—we actually provided a binder, and in tab 1, the letter from our board.

Ms. Catherine Fife: Yes. It's signed by all the board members.

Mr. Bert Clark: Right. We actually had a very productive relationship with the auditor. As I said at the outset, we think the report will make a valuable contribution to the discussion about how to deliver the province's infrastructure. All of the recommendations, frankly, we have undertaken. We've provided a table today that updates the committee on the status of all of the recommendations and our progress in working through them—all that to say, we actually think the report made a valuable contribution to the discussion around infrastructure.

Ms. Catherine Fife: Just to get back, though, to the question, the letter says, "There is a common misconception that AFP delivery is more expensive." The

Auditor General did highlight the high cost of borrowing for the private sector. I mean, the government can borrow money for these infrastructure projects at a much more competitive rate. Can you comment on the high cost of borrowing money?

Mr. Bert Clark: What the auditor's report said was that Infrastructure Ontario transferred $14 billion of risk at a cost of $8 billion, which left the public sector ahead $6 billion. We agree.

Ms. Catherine Fife: Okay. In the same letter, you say, "As a result of almost 10 years of project management experience, IO is well positioned to implement infrastructure projects using AFP as well as other traditional delivery methods."

The auditor raises the issue of the threshold, the $50-million threshold. Would you like to comment on whether or not Infrastructure Ontario—are you looking at a higher threshold, perhaps the $100-million mark, for traditional?

Mr. Bert Clark: Before Giles talks to something, I think it's worth people knowing that every year we deliver 4,000 projects using traditional means.

Ms. Catherine Fife: Under $50 million.

Mr. Bert Clark: Right, 4,000 projects under $50 million. We use the appropriate technique depending on what the project is. We're not the same organization we were 10 years ago. We think we've developed a significant amount of project management experience—4,000 traditional projects and over $10 billion of AFP projects—so we're always looking at whether and when we use that technique. In terms of a broader policy decision around what that threshold is, I'll let the deputy speak to that.

Mr. Giles Gherson: Well, I would simply reiterate what we said, which is that we certainly are looking at the recommendations of the Auditor General. The threshold is something that we're reviewing as we speak, so we're giving some close attention to that, as to whether that threshold, that $50 million, should shift.

Ms. Catherine Fife: The Auditor General went on in her report to say that Infrastructure Ontario is not checking to ensure risks they assumed were to be borne by the private sector were in fact spelled out in the final AFP contract. What is the response of Infrastructure Ontario? Because the entire premise is that due process was being followed through these contracts.

Mr. Bert Clark: Is the question, does our contract map to the risk matrix? It does. We're always, frankly, updating both of those, so there can be temporary misalignments, but as much as possible, those two things do exactly align.

Maybe I'll let Ehren answer. Ehren's our head of structuring.

Mr. Ehren Cory: Ehren Cory, executive vice-president in charge of transaction structuring.

In the work with the Auditor General's team, we did a very detailed exercise. The Auditor General's team did this mapping exercise, as we call it. As Bert mentioned, there were a few specific instances, on one project in particular, where a risk was mapped as being transferred to the private sector, and that didn't match the documentation. We think that was a great exercise, and it's one, as you see in our response to the auditor's recommendation, that we plan on continuing on a more ongoing basis, to make sure that there's consistency between the risk matrix that we're using and our contract documents.

Ms. Catherine Fife: So you're still in the process of determining your risk matrix?

Mr. Bert Clark: Well, every project is unique—

Ms. Catherine Fife: I know, but there must be some model. I mean, this is exactly the question. The transfer of risk—the model, from our view, is a flawed model. My question to you is, are you reviewing the model with which you assess risk?

Mr. Bert Clark: We have a standard starting-point risk matrix which we use for different asset classes. Every project is unique, and the risk matrix—the risks are updated for every project. We have that for different asset classes, and every time we do a project, we go through the project and we assess the risks. We do that with the help of external professional cost consultants, and the results of that are presented to our board as part of the value-for-money case. We don't proceed with a project unless the view is that there is value for money and protection of the public interest.

Ms. Catherine Fife: Okay. I'm going to go back to the financing. I think all of us here understand that ultimately governments pay for either traditional public sector delivery or AFP. The taxpayers, the citizens of this province, pay for these infrastructure projects. But considering the far higher costs of financing for AFP builds, is it not the government's—and, by extension, then, Infrastructure Ontario's—responsibility to develop the expertise required to increase the number of infrastructure projects built through traditional public procurement methods?

I think that's for you, Bert.

Mr. Giles Gherson: Well, that sounded like a policy question, so I'll answer that, and perhaps Bruce Singbush, my ADM, realty, could supplement what I say.

I think that from our perspective, as Bert has said, IO assesses every project on its merits in terms of whether it's deserving, whether it's worth having, using the AFP approach versus a traditional approach. Where you draw the line—you know, we talked a bit about the $50-million threshold, so that's one clear demarcation. But beyond that, these projects are, as Bert has said, very complex usually and need to be assessed very carefully.

1300

From our perspective, we're comfortable with the projects that have been chosen so far for AFP. I think it's possible, as we move forward—and IO has developed considerable expertise in the past 10 years, as Bert said—that some of the same kinds of savings that we've garnered in AFP projects could be had from strong management of traditional builds. But that's a grey area. I don't think anybody is going to—

Ms. Catherine Fife: I don't know. Why is it a grey area?

Mr. Giles Gherson: It's a grey area because—in my remarks, I went to some trouble to identify that, while there is a risk, there's a transfer, there's a cost that comes with the AFP model, there is a massive benefit in terms of the forgone costs; in other words, the risks that are transferred to the private sector through the life cycle of a complex large project. And—

Ms. Catherine Fife: But the Auditor General—I'm sorry to interrupt you—found that Infrastructure Ontario was projecting that the risk was five times higher in a traditional method, and yet she could find no empirical data. Infrastructure Ontario could not prove that the risk really was five times higher in a traditionally delivered public infrastructure project. That's what I'm trying to get to. This is your chance to tell us why five times.

Mr. Giles Gherson: Let's not go into the five times, but let's—

Ms. Catherine Fife: Well, that's my question.

Mr. Giles Gherson: Yes, but I think we're trying to find a level of precision that may not be there. But I think it's very obvious, from the examples that we've cited and from experience around the world that there are significant benefits to the transfer of risk to the private sector in large complex projects. Bert cited a number of studies that have been conducted to that effect, and I don't think the Auditor General refutes that. You can—

Ms. Catherine Fife: Listen, this is not about defending the Auditor General. This is about getting to the heart of the matter as to why Infrastructure Ontario attributes five times the risk to a traditional public infrastructure project, and when Infrastructure Ontario could not prove how you came to that five-times-the-risk number. That's something that I think Infrastructure Ontario is going to have to answer for at some point.

Interjection.

Ms. Catherine Fife: Sure, please.

Mr. Bert Clark: In my opening remarks I referred to a study out of Australia where they've been doing this for longer than us so they actually have a good sample of AFP projects, which we, frankly, have now. If you've read our track record, you can see the data on that, the sort of performance we have, where we typically end up about 2.5% different from the contract price by the time we're substantially complete. That is a remarkable result. In Australia, they typically end up about 4.3% on their P3 projects. On their traditional projects, they end up at about 18%. So if you look at the relationship between those two things, 4% and 18%, it's not so much different than the 5-to-1 you're referring to. But we don't actually just take a 5-to-1 ratio; 5-to-1 is an average that was drawn from—

Ms. Catherine Fife: I think in the overview, though, of the 74 projects, when you average them out, that's the number that—

Mr. Bert Clark: But that's not what we do. We don't come at the risk by saying, "Let's just multiply that number by five."

Ms. Catherine Fife: No—

Mr. Bert Clark: What we actually do is have a professional cost consultant who does nothing but estimate costs for public and private owners, and they estimate the costs and risks for us.

Ms. Catherine Fife: I'm glad that you actually went to the consultants that are doing the value-for-money assessments and the risk assessments. I'm glad that you moved to that point, because the Auditor General—this is of huge concern to us as New Democrats—in recommendation 7, she addresses the issue of conflict of interest. So the companies that are doing the value-for-money assessments and who are charged with reviewing the contracts to determine whether or not it should go public, a traditional procurement or an AFP procurement, have a vested, pecuniary interest in doing so. We heard that it's almost between 15% and 20%. So infrastructure Ontario has a serious—I mean, you mentioned that you're concerned about the perception that AFPs are not in the best interest of the public. I'm more concerned about how the value-for-money assessments are being determined, why every single one of those 74 came to the place where it should be delivered by AFP, and why there is such a lack of oversight at Infrastructure Ontario to determine that this conflict of interest is not clearly defined. I would have thought an agency of the government—

Mr. Bert Clark: Sorry, what's the conflict of interest that you're referring to?

Ms. Catherine Fife: On recommendation 7, the Auditor General references that the companies that are conducting the value-for-money assessments actually do have—that "Infrastructure Ontario should ensure that participants involved in evaluating the submissions sign the required conflict-of-interest declaration," and that was not happening. You can understand why that would be a huge concern.

Mr. Bert Clark: Right. I think what was being referred to was that the bids are evaluated by evaluation teams. None of the cost consultants that I was referring to—this is an entirely different subject—those people sign conflict-of-interest declarations. In certain instances, people forgot to do it or we couldn't find the records. We've now tightened up that process and made sure that that doesn't happen, that things don't get missed or misplaced. It's not the cost consultants.

Ms. Catherine Fife: So you consider this just to be an administrative issue, that you—

Mr. Bert Clark: It's a very important issue, but it's not the cost consultant issue that we were talking about previously.

Ms. Catherine Fife: Would you like to weigh in?

Mr. Taras Natyshak: Some fairly simple questions—thank you, Chair. How many minutes? Three, four?

Of the 4,000 projects that IO oversees—the question is, of the projects that fit over the $50-million threshold, how many are specifically P3s and how many have you chosen to use the traditional funding method?

Mr. Bert Clark: Of projects over the last 10 years, how many over $50 million weren't P3s? Is that the question?

Mr. Taras Natyshak: Yes.

Mr. Bert Clark: I'm not sure I can answer that question, but I'll tell you that over $50 million the risks increase dramatically. Those are the projects we tend to use some variety of AFP.

By the way, there's a wide range of varieties of AFP. For some of those projects we had the private sector build it and finance it for the construction period, then we paid them out. For some of them, we had them design it, build it, finance it, then we paid out all the construction costs. For some of them, we designed, built, financed and maintained it for the 30 years.

Mr. Taras Natyshak: Yes, I understand the model. Of the 4,000 that are under your oversight, as an amalgam, is there a cost overrun there? Of those 4,000 that are under the traditional model, can you say that they far surpass any value for money? Do they fall way outside of the parameters? Are they more expensive in general, or do you study them? Because the Deloitte report notes that there is no systemic performance data tracking for traditionally delivered projects in Canada. So how do you measure those?

You've said unequivocally that P3s provide better value for money. They come on budget and on time. I would hope they do, as we would hope any infrastructure project does in the province. But there is also a buffer that's built in to mitigate any of those costs and we pay a premium for that. That should be expected. However, are you saying that the 4,000 that we currently do under traditional models are always more expensive, they come over budget and over time every time, at every point?

Mr. Bert Clark: What I would say is, AFP is a tool that you would use for larger, more complex projects where there's more risk. A smaller project—the projects under $50 million range from thousands of dollars to $50 million—

Mr. Taras Natyshak: But do they come in on budget, by and large? Are you measuring whether they do? If it's a $50,000 project, then I would assume that if it goes over budget $5,000, that's a large percentage of an overrun on that project. Are we measuring those, and can you quantify whether those projects are being delivered on budget and on time as well?

1310

Mr. Bert Clark: I think we actually have a very good track record, whether it comes to AFP or traditional, and we're much more comfortable using traditional methods for under $50 million.

As someone who does project management for a living, who has 100 people who do nothing but project management for a living, they would not recommend using that same tool, AFP, for the small projects. They would, similarly, not recommend using the same project delivery technique that you use for a $10,000 painting job on a multi-billion dollar LRT.

The Chair (Mr. Ernie Hardeman): Okay. Thank you. That concludes the first set of questions. Mr. Potts.

Mr. Arthur Potts: Thank you, gentlemen, for coming here today. I appreciate this opportunity.

I want to maybe step back into the first principles of why IO was established in the first place. I wasn't here as part of government at the time, but as a taxpayer, I was quite aware of this perception, reality or not, that the public running the large projects was out of control, that projects were going way over cost.

I'm just looking at your December 9, 2014, press release here. It seems awfully compelling that the projects that were AFP were typically almost all under budget, and the ones that were not were over budget, so that assuming a risk and having other people take on that risk seemed to be a prudent thing to do.

What seems to be troubling us in the audit is, I guess, the characterization in the auditor's report of $18.6 billion, whether that's a realistic risk figure. So that's something that we've been struggling over, because not appreciating that is what takes us down to this $8-billion overrun concept.

Could you maybe extrapolate on whether those risk factors here are—and explain more fulsomely why it is those are appropriate risk factors, particularly on the maintenance over a 20- or 30-year period? You addressed part of it in your remarks, but I'd like to hear a little bit more on that.

Mr. Giles Gherson: I'll just start off in a more general way. I think, to take the point that Bert was just making earlier about the way the risk profile of a project rises with the scale of the project, it's a bit akin to—I think it's been mentioned—it's like an insurance policy.

If you lived in a rural area and there was no traffic on the roads, you might actually wonder why you pay the kind of insurance premiums that you do. Am I really getting value for money there? But if you drive in the middle of Toronto every day going to work during the kind of congestion that we have, you would probably value paying the insurance premiums. Now, you don't know you're going to have an accident, but you know what the statistics are, and you know that the likelihood is quite strong that you're going to have one, possibly, over the time of your driving experience. So that's why you pay your insurance premiums.

The value for money is transferring the risk to the private sector, having their dollars at stake, if you will, on the hook, for the completion of the project, on time and on budget, for the quality of the work, for the maintenance of the project over time to ensure that there aren't flaws that crop up, and if there are flaws that crop up over time, they're dealt with by the contractor themselves, rather than the government. They've got legions of examples of buildings in this space where there hasn't been necessarily the ability to fund the maintenance and repairs the way one might like to do just because it's expensive and government has competing priorities. So you transfer that to the private sector, with a requirement that at the end of the 30 years, or the life cycle of the building, that when it's transferred back to the government, it's in good working order.

All of that risk is transferred to the private sector. So it's hard to imagine, given the experience that we've had, what we know about the experience with traditionally procured projects, that, in fact, it isn't a benefit to do the way of the AFP model.

This government came into power, I think, not necessarily sure that it was going to be interested in doing P3 projects, but it looked at the kinds of infrastructure requirements that it faced and then looked at some of the history around at that time of public sector projects that were grossly over budget and off time and it decided to adopt the AFP model. So it wasn't an ideological thing; it was a practical approach based on what they saw in other jurisdictions.

Mr. Arthur Potts: Right. So the risk factor—

Interjection.

Mr. Arthur Potts: Go ahead. Sorry.

Mr. Bert Clark: Maybe I'll rewind: About 10 years ago, the average age of a hospital in Ontario was 42 years, and medicine had changed a lot in 42 years. You literally could not do in these facilities what people needed to do today. It was the average age, so almost every community had a hospital that was old.

At that time, the last two projects to have been delivered by the government were 75% and 150% over budget. They had asked Tom Closson, the former head of UHN, to investigate what happened. Those were not freakish events. That was what happened when the province delivered big projects. They started to look around the world and say, "Who has addressed their infrastructure deficits in an effective way, on time and on budget? What did they do to that?"

They started to make the changes that we now routinely do when we deliver projects, which is that we try and align the private sector's interest to ours so that they've got an incentive not to drive costs up, but they get projects built as soon as possible, on time and on budget. In order to do that, you need them to have some money at risk, too, not just have our money at risk, which was the way it used to be in the past. You need to have them design the building to meet our specifications so that when there are errors in designs—anyone who's been involved in major projects knows there are invariably design issues—those aren't opportunities for change orders to drive up costs; those are issues they need to address on their dime. So we made a bunch of those changes.

In that period of the last 10 years, Ontario has been one of the most active infrastructure markets in the world as a result, delivering 46 projects valued at over $10 billion. Our projects come in on time and on budget because we made a very simple set of changes for the right reasons, for project management reasons, to get public infrastructure built.

Mr. Arthur Potts: Would it be fair to say that in that $18.6-billion aspect for retained risk, maintenance long-term and the building is a significant piece of that?

Mr. Bert Clark: It is. At Infrastructure Ontario, we have a few business lines. One is, we build the major projects for the province and other crown agencies. We also happen to manage the existing portfolio of traditionally built projects—Macdonald Block, courts, special schools and prisons around the province. That portfolio is now being refreshed, but a lot of it actually is projects that were traditionally delivered many, many years ago. So we know that when builders are not required to build things to last, they don't build them to last. They build them to win the contract and make as much money building it as they can, and we're left maintaining it for 30 years.

I can tell you that for our AFP projects, we now have 100% certainty about what these projects are going to cost the public sector for their life, and we know what they're going to look like at the end of those 30 years.

Mr. Arthur Potts: Excellent. There is a perception that they come in on time and on budget, and I'm hearing sometimes under budget, because the price is artificially inflated to start with. It's easy to come in on budget if your price starts out way too high. Can you maybe address that as a perception, particularly within the procurement process: how aggressive we are about getting numerous bidders to the table, how that process works to ensure that it's competitive, that pencils are as sharp as possible, and where the innovation that may come along with building is seen in the project development?

Mr. Bert Clark: Sure. You obviously can't build a buffer into a project if you're competing vigorously with another builder to build something. We have very, very vigorous competition for our projects. As I said, we have one of the most active infrastructure markets in the world. Domestic players and international players are competing vigorously to build our projects.

Typically, on the largest projects where there's a maintenance component, we will start with five bidding teams—a builder, an operator and a design firm; five teams like that—who will attempt to qualify to bid our projects. We'll short-list that to three; from an efficiency perspective, it doesn't make sense to have five teams bidding for the project. We short-list that to three. They bid very, very aggressively to win the projects. They're then held to account for whatever number they give us. That's all we're giving them for 30 years.

1320

I should say, one of the things that we've been most surprised at over the years is the kind of innovation you get in design when, rather than prescribing what the building is to look like, whether it's going to be made of brick or glass or concrete or steel, you tell them the output you want. It's not at all unusual for us to have the winning bidder significantly inside the two losing bids and then, again, significantly inside our budget.

Mr. Arthur Potts: I guess you were referring to St. Joseph's Healthcare, for instance, as an example of that innovation, and you're probably referring to Sudbury and Thunder Bay as projects that, beforehand, were way over cost. We see it continually, still—the extension of the TTC line up through York University and such, where, in a traditional model, the contractor walks off, it's years behind and it's getting more expensive.

Are there other larger, significant examples of these kinds of public cost overruns that aren't under IO's purview that you would point out?

Mr. Bert Clark: I'm not sure I want to point to anybody else's projects, but if you google "cost overrun" in

Canada, you get a long list. If you open the paper weekly, you get examples that are close at hand.

Big projects have very big risks and if you're left with those risks and the private sector has an incentive to drive up costs, you will almost invariably end up with cost overruns. What our model does is push that back, push those risks on to them and have them drive towards being on time and on budget.

The Chair (Mr. Ernie Hardeman): Mr. Fraser?

Mr. John Fraser: Thank you, Mr. Chair. Just to follow on that question, the cost of borrowing in the private sector is really the third-party lever or hammer, if you want to call it that, to help drive your risk down; right?

Mr. Bert Clark: Yes.

Mr. John Fraser: You use that.

Mr. Bert Clark: Correct.

Mr. John Fraser: In other words, it's not a direct contractual relationship. There's a third party that's involved there that's putting pressure on the builder by virtue of their commitment to get that done on time.

Mr. Bert Clark: Right.

Mr. John Fraser: And to live up to your contract, which is the pressure on the other side. Is that an accurate description?

Mr. Bert Clark: Precisely. Interestingly, financing for us is actually a by-product of a very powerful tool that we use, which is not paying people until we get what we want. We don't go out to privately finance projects. In fact, as was said earlier, ultimately this is going to be paid for by us, but we're not going to pay for it until we get what was committed to, and then, once it gets into operation, we're certainly not going to pay if they didn't deliver what they said.

Because we don't pay them, they need to go out and borrow their own money and they now need to account to that person for late delivery. If they're not getting paid, now they've got to explain to their lender that they're not getting paid because they haven't got it built on time. And if we get into operations and the building doesn't perform, we don't pay them. Again, they need to answer to someone else. As I said, we're not actually privately financing these things; we're just not paying people until we get what we contracted for.

Mr. John Fraser: Okay. Thank you very much, that's really helpful.

I want to ask a question about capacity. You touched on that a bit earlier: 46, 47 projects over the last 10 years.

Mr. Bert Clark: Yes.

Mr. John Fraser: I know, and my friend from Nepean–Carleton would know, at every hospital in Ottawa there was a crane at one point, for about five years. I want to talk about that in terms of risk. When you have a growth in capital builds that's beyond what anybody else is doing and beyond what you've done before, there are risks involved if you don't have the capacity at the public level to be able to build those projects, if you decide to build them as quickly as you are. Would that be a fair thing to say?

Mr. Bert Clark: If we tried to do this all traditionally and not leverage private sector expertise, we'd have a very, very big organization and we'd have a lot of risk in that organization. Yes, correct.

Mr. John Fraser: So with the inception of IO, you've built that capacity inside, and working within the AFP model, you've evolved—would that be a fair thing to say?—evolved over time, evolved your methods?

Mr. Bert Clark: Yes. I think two things have happened over the last 10 years. Infrastructure Ontario is not the organization it was 10 years ago. We've built 46 projects valued at $10 billion. We've also been doing small projects that entire time. So we've built up an incredible amount of large project management expertise. It's why we're helping the city, the region of Waterloo, with their LRT. It's why we've been asked by the city of Ottawa to help them with their LRT. It's why 40 jurisdictions have come and visited us to say, "What are you doing?" It's why the National Governors Association in the US has asked us to be a part of their organization to help educate US states on how they can use modern project techniques.

I think the other very interesting thing that's gone on is that there's been a transformation in our domestic Canadian construction companies. EllisDon is not the same organization they were 10 years ago. PCL is not the same organization they were 10 years ago. They're now seeing opportunities internationally that they would never have seen had we not been at the cutting edge of project management and infrastructure investment. PCL now is involved in a billion-dollar hospital project in Australia being delivered as a P3—inconceivable five or six years ago. But given the experience they've had here, they're now over competing globally. A lot of our domestic players are now looking at the US market, which happens to be behind us, and saying, "How do we take what we've learned here and go and enter those markets?"

Mr. John Fraser: Just one more question about capacity, and then I'm going to pass it over to my colleague. In terms of the capacity within your organization—as you're assisting Waterloo, and Ottawa has asked as well—but more specifically with regard to all capital projects, not AFPs but also traditional builds, have we grown our capacity or our ability or understanding of how we can—as I know, you're looking at changing the threshold—

Mr. Bert Clark: Yes.

Mr. John Fraser: —but our capacity to look at the risk involved in public sector-driven projects or traditional projects?

Mr. Bert Clark: As I said, we're not the same organization we were 10 years ago. We have significantly more project management experience. Frankly, things we've learned by delivering large, complex projects using AFP we think we may be able to use for certain smaller projects. It's a discussion that is, frankly, ongoing between us and the ministry.

But I caution to say, there will always be a size and complexity of projects at which we say, "That's not a risk that the public sector ought to assume. We should make sure that the private sector assumes that risk." And figuring out where that cut-off is—

Mr. John Fraser: Where that threshold is.

Mr. Bert Clark: —is the discussion we're having with the ministry.

Mr. John Fraser: Yes, because I can see that, in justice, almost everything's in—there's not a big capacity inside that ministry, necessarily, to do that. So the projects that are ongoing there are mostly design, build, finance and maintain.

Anyway, I'll leave a bit of time for my colleague here.

The Chair (Mr. Ernie Hardeman): Two minutes.

Mr. Han Dong: Two minutes? I'll be very quick.

First of all, thank you very much for coming in and answering some of these questions. My colleague mentioned cost overruns, and you suggested maybe googling and finding out. I can use a perfect example, and that's the Spadina subway line. We all heard in the recent media—and I know the mayor's quite excited about that. I think the number is around $150 million or something like that. In your mind, had this project been under AFP, what would the outlook be? What kind of difference would we see had this been under AFP?

1330

Mr. Bert Clark: That project, actually, has all of the features of traditional projects that we found challenging, frankly, in the past and have tried to eliminate.

The first, which I referred to earlier, is that that's a big project that's been broken up into small projects, so you've got tunnels meeting stations meeting tunnels meeting stations. Every time those things meet, there's integration risk, and that integration risk has been retained by the public sector. That risk has come to pass.

The Chair (Mr. Ernie Hardeman): Okay, that concludes that one.

The official opposition: Ms. MacLeod.

Ms. Lisa MacLeod: I'd like to say thank you to all of you for coming in, as well as to the auditor for the value-for-money audit.

I have long been on the record as supportive of P3s and AFPs and, in particular, ensuring that the Royal Ottawa Hospital was built, about a decade ago. I think it's one of the finest institutions that we have in the city of Ottawa.

That said, I must say that I was quite shocked when the auditor came forward and said that she questioned the $8 billion cumulative that would have made these projects higher than if they had been contracted out and managed by the public sector.

I'm listening to you, and I'm looking at the higher financing costs. I had a great discussion this morning with Michael Harris, who is our infrastructure and transportation critic, who spent some time, actually, managing P3s. He indicated that all is not what you see, that there are maintenance costs that are included, and these are all built in, and that is effectively there. I think it was the auditor who said that about $6.5 billion of that went to the higher private sector financing costs.

I'm not going to belabour the point, but I wouldn't mind if you just wanted to touch on that one more time, from your perspective. Again, I think, if we're to proceed in the province of Ontario, we're going to actually need to use more models like this, not less of them.

Mr. Bert Clark: Sure. As the deputy said at the outset, there was certain coverage of the Auditor General's report that focused on the $8 billion. That was not the central point of her report. Her report said that $14 billion of risk was transferred, at a cost of $8 billion, which put the province $6 billion ahead.

I think the implication that the report was getting at was that you need to be always mindful of the cost you pay in order to transfer risk, which is something we do, frankly, and that the board is intensely focused on, which is why I said at the outset that the really important questions, when it comes to AFPs or P3s, are which projects do you use it for, and how much finance is in the projects?

It clearly works. Our track record, and the experience in other countries, is that these projects come in on budget. There is cost certainty for the public sector. That's a good thing.

It's like insurance. No one is debating whether insurance makes sense. Insurance makes sense. The only question is, when do you get insurance, and how much insurance do you buy? That's what we spend our time thinking about.

The point of the $14 billion, $8 billion, $6 billion was, I think, to drive people towards thinking about when you do this and how much finance you use.

Ms. Lisa MacLeod: I just want to go back to this $6 billion. I just want to be very clear, for those who are watching at home or might be reading this in Hansard at some point in time: Effectively, there was $14 billion of risk; $8 billion was the cost for that; and you're arguing that there was $6 billion left over.

In a briefing that we had earlier today with the auditor, she cited, on pages 204 and 205 of the auditor's report, some of the differentials. You would say, for example, that you have retained risks of $18.6 billion for public sector comparators, while the AFP would have been about $4 billion. The auditor, on pages 204 and 205, effectively tells us that you would remove about $5.9 billion from that $18.6 billion, leaving it at about $12.7 billion, and from the AFP, effectively, instead of $4 billion, it would be $3 billion; meaning instead of having a $6-billion differential, it's actually $1.7 billion—still coming out ahead, but there are some issues with the methodology that you would be using in terms of the risk assessment. I wonder if you have a comment on that.

She indicated on page 204, "Two significant risks on the public sector comparator side should not have been included." To remove from that $18.6 billion, the total overall—one was for AFP projects with a maintenance component, nearly $3 billion. That was included twice in the $18.6 billion, so that's a $3-billion error.

Then she suggests on page 205 that there was another $2.9 billion in costs associated with planning, process and allocation practices which was also included in the $18.6 billion of retained risk on the public sector comparator.

I want to talk to you about that because the next question I have—I think you have about 93 different criteria for risk assessment. I want to talk a little bit about that, and then I want to talk about screening projects as well. Can you make a comment at this point in time on the differential between what the auditor says will be your differential and what you suggest it is? You're suggesting $6.6 billion. Her changed numbers—correct me if I'm wrong, Auditor—are $1.7 billion.

It might be easier for you to refer to our—

Ms. Bonnie Lysyk: What we're referring to is on page 203, where we've got the figure 5 chart, and it comes down to the retained risks figure. It goes 18.6, 4.0 and 14.6. Those two risk factors that factor into the math here: One of them is $3 billion and another is $2.9 billion which, when you take it across, it's not quite the math of $5.9 million; it's a little bit less. But if you factor that in, it changes the overall total on the VFM to lower than $6.6 billion.

The point we're making is that when we looked at the model that was being used to assess the projects, those two assumptions, one being the maintenance component being—the asset residual risk having been included in two parts of the framework, and then the $2.9 billion with the planning process and allocation practices having the same impact on both traditional procurement versus the private sector model—when you factor those in, the numbers are a little bit different.

I guess our message on the whole thing is that when we looked at the $8 billion, that was the measureable cost. The key component, as Bert had pointed out and we totally agree with, is the financing of that, the $6.5 billion. Our point in showing the difference in the retained risks is to say the discussion really is, like you pointed out, the financing side. There's subjectivity and judgment in the model, and that's where we were looking for the empirical evidence.

So we're not disputing the fact that P3s are good or P3s are not good; all we're saying is, the math, when you use the retained risks model, offset to cost, kind of skews one in favour of AFP when in fact the discussion needs to go back to the financing.

I've gone on and on, but really, I think the point of this whole chart is to focus on that decision as to how much should be private sector-financed, how much should be public sector-financed, and which projects should be handled by AFP and which ones shouldn't. That's the simplicity of the chart.

I think we can get involved in all the numbers and everything, but really, it comes down to those two things.

Mr. Bert Clark: If you want, Ehren can speak to those two points, but I completely agree that at the end of the day, the discussion that ought to be had is which projects—we're having that discussion—what's the threshold, and how do you make sure that if you're using this tool, if you're buying insurance, you're buying the right kind of insurance. That's what our board does every time we bring a project to them.

Mr. Ehren Cory: Just to talk to the two risks you asked about—and they are two significant ones. First, I'll come back to the two, the asset residual and planning, in just a second. But I'll just start from where we get the assumptions from in the model. It came up earlier, but I think it's the important place to start, the way we do this.

1340

This is a planning tool. This is the tool we use at the outset as a part of the decision-making of which way to go: to use the risk model—you talked about the 93 or 94 risks—which is developed by our expert third parties, to take that standard risk matrix and then say, "For this project, what's different about this project that means that risk is either bigger than usual or doesn't exist on this one?" They customize it. That risk matrix, then, is what we use to calculate that risk that we're avoiding, that risk avoidance number. That's where we get those numbers from.

In the Auditor General's work—and we had a lot of discussion with their team around these two big risks—the recommendation that came out was that we should make sure that the costs are not double-counted, basically; not accounted for in two places I think was the wording. We agree with that recommendation. Let me talk about each of them in turn.

Asset residual is one of the risks that the Auditor General and the team called out. It is one of the big risks in our model. That's the risk we talked about earlier, that at the end of the 30 years of the life, the quality has deteriorated. Asset residual is the idea that at your 30th year, is the asset still in good shape or not? That's a risk that in the assessment of the third parties is much higher on the traditional side, because there's the risk that over the 30 years, the building isn't maintained to the same standard, that you defer, defer, defer on maintenance. Anyone who has deferred maintenance for long knows that when you finally do it, the work is much bigger and the bill is much bigger. You can get away with not changing your oil for a while, but then your engines seizes on your car, and you pay a lot more. So that's what asset residual is about.

What the team pointed out is that when we build our model, and I'll try not to be technical about this, we assume the same what we call base cost for both the traditional and the AFP. We assume the same costs, and then at the end we have this bigger risk on asset residual. What the Auditor General's team pointed out is, "There's a potential contradiction in doing that, because you're saying that you spent the same money on maintenance in both worlds, but the asset is in way worse shape under one." That was the point.

We take that point. There are many technical arguments, and we had those with the third parties, because, again, those assumptions come not from us but from cost experts and engineers. But we actually think the Auditor General's team has highlighted something. So what we're doing as we work on updating our VFM methodology, which we're in the midst of and we plan on publishing later this spring, is eliminating that double-counting. By that I mean, we will not assume that you spend the same money on maintenance for the 30 years, because that's not actually the experience that we see in large traditional projects. What we see is that maintenance costs get deferred and deferred, pushed out, reduced.

What's a little bit different than the comment on page 204: That won't take it to zero. We're going to try and eliminate the double-counting, because we agree there is some, but in the change which we'll be making, I don't think that it will be totally eliminated—

Ms. Lisa MacLeod: Because the two numbers won't be equal at the—

Mr. Ehren Cory: Correct.

Ms. Lisa MacLeod: Okay. I think that's a good explanation, so that's important.

You had something else to add.

Mr. Ehren Cory: Just on planning, a similar comment—that's the other big one that's mentioned. Again, there the issue is that we have a couple of risks in our matrix that refer to planning. One of the things that the Auditor General's team—and they got this also in interviews with ministries that we work with, because when we do that risk matrix that I described, part of that is sitting down with a ministry and saying, "For your particular project, could this risk manifest itself?" We have three different risks about planning. They were quite nuanced and different. There was at least the high potential that someone might double-count by saying, "Yes, that risk could happen, and so could that risk, and so could that risk." In our new version, which we're going to release, we're going to collapse those into one, make it much clearer what the risk is. Again, I think we're going to eliminate the double-counting, but it won't go away completely—same story.

Ms. Lisa MacLeod: Okay, that's good.

We've talked about risk assessment. We've talked about the numbers. I'm just trying to think here. I guess, Bert, it was you—you were talking about reviewing screening thresholds for future AFP projects, given the project management experience IO has gained over the past decade. I'm wondering if you could give us a sense of what type of screening mechanism you're looking at right now and what may have provoked some of those changes. Was it because IO was taking on projects that maybe they shouldn't have been or should be taking on projects that they aren't right now? How do you make those assessments? Is that done with your board?

Mr. Bert Clark: It gets done in two places. Our board would have to be comfortable moving the threshold up. They'd have to be comfortable that we can in fact deliver larger, more complex projects without the risk transfer of AFP and without exposing the province to undue risk. It's also a discussion that we would have with the ministry, our shareholder, about what their view is of the appropriate threshold.

Why might one raise it? As I said, 10 years ago, we were a lot smaller organization, we delivered a lot less projects and we had a lot less expertise, so we were less capable of managing risk than we are today. As I say, as you move up in project size, projects get more risky. Our risk tolerance 10 years ago is different than it is today, so we might think of increasing it with our shareholder.

Ms. Lisa MacLeod: Right. Your deputy minister is here. Is this a conversation that you would have with a variety of ministers on the risk threshold that they're willing to take? Has this discussion already started with cabinet?

Mr. Bert Clark: I have discussions with my board, and the shareholder has their own discussions.

Mr. Giles Gherson: We have those kinds of discussions for exactly the reasons that Bert mentioned. Our interest is the same in terms of ensuring the lowest-cost delivery and highest-quality delivery of public projects, but we also share the responsibility of oversight with the treasury board, so that's the kind of discussion that we would be having with them.

Ms. Lisa MacLeod: Okay. I don't know how much more time I have. I just have—

The Chair (Mr. Ernie Hardeman): Four minutes.

Ms. Lisa MacLeod: Four minutes? Okay. I have two quick questions, then. At one point in the—I cannot find it, I apologize; I'm not sure who said it—you were talking about innovation assessment. I know we talked about that as well with the auditor—if you don't mind forgiving me for one moment—an innovation adjustment.

I guess the question I have is, if you're starting to talk about innovation—was it you, Bert, who mentioned that, who brought it up?

Mr. Bert Clark: I did, yes.

Ms. Lisa MacLeod: Okay. So if Infrastructure Ontario is planning on adding an innovation adjustment for future value-for-money projects, how do you plan on appropriately estimating that, and what does that mean? It's a great buzzword, "innovation."

One of our former chairs of this committee, when I was first elected here almost nine years ago—Julia Munro was actually on the committee with me—was Norm Sterling. Norm took me aside, and he said, "The one thing you have to worry about in government is information technology projects because they will always have a cost overrun." Boy, was he right when I looked at eHealth.

When I hear the word "innovation," I start to think of things like MaRS and other things, and I want to know how you define that, because that has been a buzzword around here. I'm not comparing it to eHealth or Ornge or anything, but I am saying that that's a word that we hear quite a bit. I'd like a little bit more explanation on it, if you don't mind.

Mr. Giles Gherson: Can I just start off by reciting what I said in my opening remarks? I did give an example of it, and I think it was just one of many. It was with regard to St. Joseph's Healthcare Hamilton's West 5th Campus, where I pointed out that, the way that AFP project worked, of the three bids, one really tried to reconsider the design of the project in a way that took advantage of the landscape, if you will. It was able to do that in a way that produced a smaller, more compact design, which reduced the cost of the build and then led to a winning bid that was 27% lower.

Ms. Lisa MacLeod: So can I ask you a quick question? My husband used to do a lot of procurement. He worked for the federal government, and he would always talk about lowest-cost compliance. When you're doing your grid when people are bidding, typically your lowest-cost compliant is who you choose, but are you now suggesting that in some projects you are, or will be in the future, adding this innovation component? No?

Mr. Bert Clark: No. Under the traditional model, we would go and we would hire an architect to design St. Joseph's hospital.

1350

Mr. Giles Gherson: It's prescriptive.

Ms. Lisa MacLeod: Okay.

Mr. Bert Clark: They would go out and they would design a hospital. It would have four floors and it would be made of brick, and there would be a mechanical/electrical system that looked like such. Then we would get three guys to bid it, and the lowest-priced guy would win.

Under our model, we say, "Let's prescribe the outcome." We're not going to tell them that it should be four floors or three floors. What we're going to tell them is that we need this many emergency rooms, this many ICU rooms.

Ms. Lisa MacLeod: I see.

Mr. Bert Clark: We need the temperature in the place to always be this temperature. Let them figure out what the cheapest way is to achieve that, on a whole-life, 30-year basis. Rather than us having—

Ms. Lisa MacLeod: So getting the parking spots and the patients, the 2,000 and 5,000—

The Chair (Mr. Ernie Hardeman): The answer for that will be in the next round.

Ms. Lisa MacLeod: Can you believe this? He's cutting me off. He's my seatmate in the Legislature.

The Chair (Mr. Ernie Hardeman): We'll now start the second round with the third party. This time it will be 18 minutes per caucus.

Ms. Catherine Fife: I'm sorry, Mr. Chair. How long?

The Chair (Mr. Ernie Hardeman): Eighteen.

Ms. Catherine Fife: Eighteen. Okay, thanks.

This has been interesting, some of the questions and answers, just to follow along. I do think it's important for us to remember that this is the second Auditor General whose report has raised the high cost of AFPs to the taxpayer. The previous auditor, Jim McCarter, also raised this issue.

The insurance analogy is also pretty interesting. I think it comes down to this fundamental question: Is the $8-billion risk premium worth it for the people of this province? I think you clearly see that we don't feel it is.

I want to get back to how the risk premium is calculated, because I think that's the pivot. I don't think anybody really challenges the $6.5 billion in financing costs that the Auditor General identified. That's a big number, it's a real number, and maybe we'll get to some of the interest rates that affected that number a little bit later on.

What I want to do is I really want to understand the public sector cost comparator in calculating the risk premium. It is a number that suggests what a typical cost overrun is that is incurred in the traditional public approach to building infrastructure. Is that correct?

Mr. Bert Clark: For every—

Ms. Catherine Fife: For the public sector cost comparator.

Mr. Bert Clark: We do this for every project. Every project has a unique risk profile. That risk is assessed by a professional who does nothing but cost consulting and risk assessment for public and private owners. They do that for us, like they do for others. They would assess a whole series of risks, both during the construction and the operating phase, and they would provide us with a probability of all of those risks coming to pass.

They would do that for us delivering the project under the traditional means—design-bid-build—where we do the design, someone else builds it, and then we take back the operating risk, and they would do that for design-build-finance-maintain, where we pass to the private sector the risk of that cost certainty.

Mr. Ehren Cory: If I may, one of the common shortcuts that we see is, people say, "You have a project that has an estimated cost of $500 million, and then you've got retained risk estimated, when we look at your VFM report"—which is posted—"of $400 million. Are you saying you expect the risk that the overrun is an 80% overrun?"

I just want to be clear that that retained risk accounts for risks of overrun during construction, risk of cost overruns during the 30 years of life, and risk of schedule delay also, which has a cost. So it's not apples-to-apples math, to divide the two and say, "That's the cost overrun being assumed."

Ms. Catherine Fife: Okay, I understand that. But which companies, if you will put that on the record, are calculating the cost overruns? The auditor has rightly pointed out that the evidence is not there to measure the risk. Which companies are telling Infrastructure Ontario that these cost overruns are real?

Mr. Bert Clark: We actually do publish on our website, I believe, the base risk matrix that we use. Those are developed with—

Ms. Catherine Fife: But those are done by consulting companies, and who are those?

Mr. Bert Clark: Right, and I'm about to tell you who those companies are.

Ms. Catherine Fife: Okay, that's good.

Mr. Bert Clark: Altus Helyar and Marshall Macklin Monaghan are the two that I think are published on our website. We actually provided a letter, in the binder you've got, from Altus Helyar.

Ms. Catherine Fife: I'm sorry to be jumping around a little bit, but the issue, though, of managing risk and the justification of transferring risk is really the question that we have here today. I think that the Auditor General's report points to some gaps in the process to evaluate those risks and I think you've already acknowledged that you're going to be reviewing some of those processes. But Infrastructure Ontario must have some responsibility, if you will—and I also appreciate the fact that you've mentioned that Infrastructure Ontario is not the organization that it was 10 years ago. That's why these reports are so important; going forward, they should inform some changes.

But in the government's Building Together: Jobs and Prosperity for Ontarians from 2011, a guide to investments and infrastructure in Ontario, the objective at that point was that Infrastructure Ontario would have a greater role in procuring infrastructure, including engaging in traditional public sector forms of procurement. So you can see why there's a disconnect between what the government originally, I think, set in motion and what's actually happening with Infrastructure Ontario doing the bulk of your projects through AFP.

Have you met with the economic development minister to discuss moving forward and following through on this original mandate?

Mr. Giles Gherson: I'm deputy minister of economic development, and—

Ms. Catherine Fife: I know who you are. Have you met with the minister?

Mr. Giles Gherson: We talk to the minister quite frequently.

On the question of which projects should be assigned to AFP and which ones shouldn't be, there is the threshold that we talked about. The reason the government has asked IO to look at both AFP and traditional, to assess the merits of which one you should use in this specific project, is because as you get into different types of projects, you want to be clear that the risk matrix is appropriate. So it's really a diligence issue that the government wants to be assured of, that the right type of approach is taken for the specific project. I don't think there's anything incompatible with what the government said and with what in fact IO has been doing.

As Bert mentioned, something like 4,000 projects have not been AFP but the traditional approach, but as projects have become—particularly now, when you move into the transit and transportation area—very complex projects, those really do, as discussed earlier, lend themselves to the AFP model.

When you move to very complex hospitals, again, there was a reason why AFP was chosen. But that doesn't mean that it's an ideology that AFP must be used in all cases or anything like that. It's really a careful assessment of what makes the most sense, given what we know about the project and the historical record of similar projects, where they've gone and how they've performed.

I think to try to turn this into a scientific exercise is a little bit difficult because each project is so different. What you're doing is, you're trying to look at where have things gone wrong in the past and can we correct those wrongs, those flaws, those cost overruns or delays in the management of the traditional way, or is the project going to be so complicated that in fact it would be easier to transfer the risk to the private sector, where, as Bert said, they would have real skin in the game and a real requirement, actually, from their lender and from their own interest, looking forward, to make sure that they're doing it in the cheapest way and, in fact, to use innovation where they can because it's in their best interest. They're going to save money if they do that.

Ms. Catherine Fife: Infrastructure Ontario now has 10 years of experience. Right?

Mr. Giles Gherson: Yes.

Ms. Catherine Fife: Certainly over the course of that time, you now have the capacity to potentially directly manage. The Auditor General even mentions that Infrastructure Ontario may now be positioned to directly manage the construction for certain large projects and thereby reduce the cost of private sector financing. That should be the ultimate goal. The goal shouldn't be just to maintain the status quo of always contracting out. We should be building our capacity—Infrastructure Ontario should be building your capacity to ensure that people are getting value for dollar. She recommends this. In fact, I think that the government, originally, from that 2011 strategic framework—I think that was the original intent, and so I see Infrastructure Ontario going in a completely different direction. I think that this Auditor General's report confirms that.

1400

I think at the end of the day, especially with the infrastructure gap in this province, we will never close that gap if we continue to favour the AFP. Right now, you have a risk assessment tool that directly favours going AFP.

Mr. Giles Gherson: I think it does so on large, complex projects. It doesn't favour AFP across the board in any way at all. I'll just ask Bruce Singbush to elaborate, but I think it's important that we recall the $8 billion against the $14 billion. You're paying $8 billion to transfer $14 billion of risk. It's true that you can parse all of those numbers. You can parse the $8-billion number—

Ms. Catherine Fife: Well, I would—

Mr. Giles Gherson: You would.

Ms. Catherine Fife: And I could.

Mr. Giles Gherson: You could.

Ms. Catherine Fife: And I will at one point. But I'd rather get—

Mr. Giles Gherson: Let me just say this: You can parse that number, you can parse the $14-billion number, and over time those numbers will change. If you look back at the record in 10 years' time, you'll probably find that, through improvements in process, the $8-billion number, if that was analogous, would come down over time. In fact, you're seeing financing costs come down in the market that we're in.

If you look at the $14-billion number, it's probably true that over time, as techniques improve, the risk transfer might be lower, but that then would require you to assess each project, as time goes on, with the knowledge you have and the experience you have—that IO has—to make a very careful assessment of which it should be using and which method gives it the best opportunity to maximize the benefits of lowering the cost of construction and maintenance and reducing the probability of cost overruns.

Ms. Catherine Fife: I think that's the point. I think the model for assessment is flawed right now.

Mr. Giles Gherson: But it doesn't throw the baby out with the bathwater. I don't think it actually—and I don't think the auditor would say this—obviates the benefits of using AFP. She is saying you want to be very, very careful and have the data to support, in every case, the best way you can, the $8 billion and the $14 billion. We completely agree with that.

Ms. Catherine Fife: She has also said that there is no empirical evidence thus far to prove that that risk transfer is worth it.

Can we just go back to the building capacity of Infrastructure Ontario, please?

Mr. Giles Gherson: Sure.

Mr. Bruce Singbush: It's a good question, so—

The Chair (Mr. Ernie Hardeman): If we could have you introduce yourself first.

Mr. Bruce Singbush: I'm Bruce Singbush. I'm the assistant deputy minister at the Ministry of Economic Development, Employment and Infrastructure.

The Chair (Mr. Ernie Hardeman): Thank you.

Mr. Bruce Singbush: Part of your question is the centre of excellence that is Infrastructure Ontario. Bert mentioned the evolution over the past decade. I think it's important to unbundle that a little bit, because that will help in this conversation. It brings together a few points.

Infrastructure Ontario was created, in part, specifically to look at alternative finance procurement and the procurement of infrastructure using that one type of tool. That was what it was originally created for, and that's what it had built a very strong reputation on.

You referenced 2011 with Building Together. That's an important point in time, because in 2012, Infrastructure Ontario was actually merged from a policy perspective with what was called the Ontario Realty Corp., as well as another organization called Stadium Corp. That brought together the infrastructure procurement expertise that the government requires across the board. That's both on the construction side and on the management side—

Ms. Catherine Fife: Bruce, I'm sorry. I don't want the history of Infrastructure Ontario. You've already provided it and I've already read it. I just want to know this: Is Infrastructure Ontario looking at moving towards direct management of these projects? Because that was originally in the mandate. Just yes or no.

Mr. Bruce Singbush: The answer is, they do that today. Bert mentioned that. They do that on over 5,000 buildings today and over 4,000 projects a year.

Ms. Catherine Fife: My colleague has a question.

Mr. Taras Natyshak: Just a couple of brief questions.

Under a traditional method, what are some of the safeguards that you would have in place to be able to ensure the value for money throughout the lifespan of a project? Do you have a holdback provision on funding for contractors? You are going to hold back funds if the project isn't completed?

Mr. Bert Clark: There is, obviously, statutory holdback for one of the—

Mr. Taras Natyshak: Penalty clauses as well in terms of deficiencies, I would imagine.

Mr. Bert Clark: You have statutory holdback for liens.

Mr. Taras Natyshak: Yes.

Mr. Bert Clark: We have bonding. Those would be the traditional security items you would have, which I can tell you is nothing near like the security you get when you haven't paid until they perform—nothing near.

Mr. Taras Natyshak: But you would still—I mean, if the performance isn't there on the project, then you would be able to hold back a substantial amount of funds in terms of incentivizing them to continue the project.

Mr. Bert Clark: Remember, under a traditional project you're paying progressively, so your money is in the project, not theirs.

Mr. Taras Natyshak: But at some point—I mean, upon substantial completion—

Mr. Bert Clark: At some point you could theoretically not pay them for a project that they haven't completed. Your money is in, they're out, and you're suing them and maybe suing their bonding company, and you are unlikely to recover anything like what you'd have if you got the money yourself.

Mr. Taras Natyshak: The concept around P3s is obviously to bring infrastructure projects online quicker, faster, kicking the financing down the road or kicking the bill down the road for some time to come.

Mr. Bert Clark: Could I just answer that? There's no accounting benefit. There's no effort made in doing P3s to change the accounting or fiscal treatment of these projects—

Mr. Taras Natyshak: Not on the IO side. It's still accounted for on the budgetary side.

Mr. Bert Clark: No one inside government is spending time structuring transactions to move financing around. When the province moved, 10 years ago, to consolidate the MUSH sector: municipalities, hospitals, colleges, schools—we moved to consolidate all of that expenditure. There's zero accounting benefit to going P3 or traditional. In both cases, the debt and the costs are all amortized over the life of the asset. The reason you do it is for project management reasons.

Mr. Taras Natyshak: In Windsor right now there is a situation that's developing that I think relates right back to the quality and the benefit that P3s supposedly deliver. We saw that one of the subcontractors had deficient girders that have now led to some substantial time delays. I'm understanding that none of the provisions or the ability for IO to hold the Windsor Essex Mobility Group to those protection mechanisms are being used—holdbacks or penalties. Is that what's happening?

Mr. Bert Clark: I'll tell you, we have the ultimate holdback in that case. There is no way I would have wanted to be leading IO when we ran into the difficulty we did on that project, and it's been one of our more challenging projects. There is no way I would have wanted to have been delivering that project using traditional means.

When they ran into trouble—and projects do run into trouble—

Mr. Taras Natyshak: Did the deficiencies of the girders—were they detected—

Mr. Bert Clark: May I finish?

Mr. Taras Natyshak: Were they detected by ministry officials? I just need to know that, first of all.

Mr. Bert Clark: Let me answer your first question.

Mr. Taras Natyshak: I've got 30 seconds left.

The Chair (Mr. Ernie Hardeman): It's all gone.

Mr. Taras Natyshak: If you could now answer both my questions, that would be good.

Mr. Bert Clark: When we ran into that trouble on that project, it was their money that was in the project, not ours.

Mr. Taras Natyshak: It's ultimately all of our money.

Mr. Bert Clark: In terms of the ultimate holdback, we had paid them nothing. At that point, they had hundreds of millions of dollars in that project; we had zero. They're now going to correct that issue at their cost, 100% at their cost. Had we not had the sorts of levers we do in a P3 contract, we would have had a much different result.

The Chair (Mr. Ernie Hardeman): Save that for the next answer.

To the government: Mr. Rinaldi.

Mr. Lou Rinaldi: Thank you, Chair. For the benefit of the member opposite, if you have more to add on the Windsor issue, please do so. I'll give up my time for that.

Mr. Taras Natyshak: You can concede it to me and I'll ask the questions.

Mr. Lou Rinaldi: No, no. It's my time, thank you.

Interjections.

The Chair (Mr. Ernie Hardeman): Order.

Mr. Lou Rinaldi: If you need to expand, please, before I go to my question.

Mr. Bert Clark: Proceed with your question.

Mr. Lou Rinaldi: Okay, so you're done with the Windsor issue.

Mr. Bert Clark: I'm done.

Mr. Lou Rinaldi: I just want to shift gears a little bit and look a little bit more globally. Ontario is not the only jurisdiction with AFPs. There are other jurisdictions, which I think you mentioned in your opening remarks, that have been there before us, and some are coming along. In general, do you see, from your expertise, that's a growing trend or a diminishing trend? We heard some things this morning when we had a briefing that there might be some jurisdictions that are maybe not as strong or not as strong as they were. Can you elaborate where it's at a little bit more globally?

Mr. Bert Clark: I'm not sure I want to provide commentary on the global infrastructure landscape. I will tell you that we have been one of the most active infrastructure markets in the world. The market I'm most familiar with other than ours is the United States. They're sadly significantly behind us in terms of their infrastructure investment, but there are some spots where they're starting to invest and they actually are borrowing heavily from the Ontario model. For instance, Long Beach, California, built a court in the last five years modelled on the Durham court. We have been asked by the National Governors Association to participate in a group to help educate governors on how to use modern project-delivery techniques.

1410

There are a number of states that are starting to get on with the important work of investing in infrastructure and, like many places, have had bad experiences in the past delivering projects. They have come in over budget. They have come in late. They have had quality issues going forward. So they have come up to look at what we do and learn from us.

Frankly, as you look across Canada, the most recent province to make significant inroads in modernizing the way they deliver infrastructure is Saskatchewan, but whether it's BC or Alberta or Manitoba and Winnipeg, they've used it. Saskatchewan has used AFPs, and Ontario, obviously. Quebec has used it—less so in the Maritimes. But really, across Canada and at the federal level, people have changed the way they deliver infrastructure.

Mr. Lou Rinaldi: Maybe if you could comment on this other issue: Just recently, the leader of the official opposition in Ottawa made a statement that it wasn't dogmatic and, "The point is to get things built," when he was referring to alternative financing. Can you maybe explain the pragmatic piece to infrastructure, the process we have? I know this is a comment that was made by somebody else, but if you'd like to comment, I'd appreciate it.

Mr. Bert Clark: I think that comes back to something I said early on, which is that we did not set out to privately finance infrastructure. What we set out to do was to address the major sources of cost overruns in the past.

One of the big tools we use is that, during the construction period, we don't pay until they perform. That necessitates private finance on their part, and their lenders have their risk, as opposed to us. Similarly, during the operating period, we withhold some amount of the construction to ensure that what they have built performs and lasts.

Again, none of that is ideological. None of that is affected by anyone's view on private finance one way or the other. It's entirely a project management technique. That's how we look at these projects.

Mr. Lou Rinaldi: Chair, I just want to say, for the committee's interest, that in the town where I live, the local school board just invested $1 million to rebuild a track facility with a football field. Things went south. It had been two years of waiting by the time they sued, by the time they sued whoever fought—I'm trying to think of the word—the bond folks. For two years, the school was without a field. I mean, it looked like a mess, frankly. Anyway, that was just a comment that I wanted to make, but my colleagues, I'm sure, have other questions.

Ms. Harinder Malhi: I guess I'll go next. The Auditor General briefly talked about the Fraser report and cited it about the study on P3s. Would you be able to better explain that to the committee?

Mr. Ehren Cory: Talk about the Fraser report?

Ms. Harinder Malhi: Yes.

Mr. Ehren Cory: The Fraser report, which was published two years ago or so now, was really looking at transportation infrastructure across Canada and ways to spur investment in transportation and the role that P3s could play.

They looked across the country, and they looked at experience both traditionally and under P3s. The conclusion they came to, which they stated pretty clearly, was that P3s are an important tool in the tool kit. It goes back to what we talked about earlier. It's about picking the right model for the right project. But the Fraser report pretty clearly says—especially when you get into the transit projects, which are, in general, very big projects with a lot of complexity and a lot of risk to them, as we see in transit projects that are under way all over the world. The Fraser report really focused on, for that big transit and transportation build that Canada has to do, how P3s and the AFP model have to be part of the approach.

Ms. Harinder Malhi: Thank you.

The Acting Chair (Mrs. Julia Munro): Any other questions?

Mr. John Fraser: Just one quick question. Going back to figure 5 in the report, a very simple question: Are you satisfied with your retained risks of $18.6 billion?

Mr. Bert Clark: The simple answer is yes.

Mr. John Fraser: Yes. I just wanted to confirm that.

Then, go back to the double-counting: In terms of the way that it's represented, from an accounting purpose, is that it should be on another line as opposed to on that line—is that fair to say?

Mr. Bert Clark: We're looking at the issue of whether or not there is double-counting. We've agreed to look at all of the recommendations. We're looking at that one. We firmly believe that the end product for traditional delivery has significantly more risk that often manifests itself as a large deferred maintenance issue.

Mr. John Fraser: Okay. It was just a question on the risk that's involved with maintenance on a traditional build project is different than—

Mr. Bert Clark: Very, very big.

Mr. John Fraser: That's what I was trying to establish.

Mr. Bert Clark: Yes, correct.

Mr. John Fraser: Okay. So where that's represented and how that's represented is really what you're going to look at?

Mr. Bert Clark: Right.

Mr. John Fraser: Okay, thank you.

Interjection.

Mr. Arthur Potts: No, we have a few more minutes. Chair, if I could?

The Chair (Mr. Ernie Hardeman): Go ahead, Mr. Potts.

Mr. Arthur Potts: If I could talk maybe a bit about the quality price matrix and how we choose the winning bidders. I know the auditor in her report talked about—I think in about two thirds of the projects, the lowest bidder was chosen. They were also the best projects, from a quality standpoint. She makes the comment that in one third of the cases, we went for the lowest price and we didn't get the best quality.

Is there a thought around IO about changing the metric in order to ensure that innovation is fully recognized—the better design—and it's not always just a bottom-line price?

Mr. Bert Clark: I'll ask Ehren to speak to that.

Mr. Ehren Cory: Sure. The price and quality matrix that we use, and that we have used, really is meant to capture two things. First, Bert talked earlier about the whole concept of output specifications, so we don't specifically prescribe what to build, but we set really clear criteria around what's required of the asset in terms of performance. When we evaluate bids, we have quite a high threshold: a 70% score they need to get on our specific criteria. We have engineers, experts, the owner of the asset—the ministry that will be the long-term owner of the asset—and our team evaluating those designs.

Anything that doesn't meet the output specification and anything that doesn't achieve a high score from a design and technical perspective can't win. Above the threshold, though, what we're saying is that all of those designs meet the output specification: They meet what we want the asset to do and they meet it at a quality and a technical capability that we're comfortable with. Once that's true, that gets weighted against price—and price does get quite as high a weighting amongst those highly qualified, technically—and we design satisfactory bids.

We've looked at that quite a bit. We've looked at the sensitivity—what if you tweaked and had a little bit less to price and a little bit more to design? We've gone through all the products we've done historically. Would it have changed the winners? The answer is no, over quite a wide range. So we don't have plans at this time to change the relative weighting.

Mr. Arthur Potts: Okay, fair enough.

If I could go local, Bridgepoint is close to where I live—not in the area I represent but it's close to where I live—and is a fantastic building. I have friends whose fathers and mothers have been in there recently, and it's an extraordinary facility built under the AFP model, and I believe on time. It's a spectacular facility, so I just want to congratulate you on that level.

But then, moving forward—maybe it's too early to tell—do we anticipate the expansion of Toronto East General Hospital to be under the same kind of model?

Mr. Bert Clark: I don't think that that has actually been assigned to us at this point.

Mr. Arthur Potts: No? Okay, so it's too early.

The Fraser study—

Interjection.

Mr. Arthur Potts: Go ahead. Why don't you do it?

Mr. Lou Rinaldi: Bear with me for a second here. How much time do we have?

Mr. Arthur Potts: We've got about six minutes.

Mr. Lou Rinaldi: Going back to the model of what you use, and you just mentioned—my colleague here, Mr. Potts, highlighted that you're satisfied in general with price and quality and all that stuff. I just want to revisit that a little bit more, in the sense that, besides the price and the modelling, are there other areas that you might want to re-look at? The way I look at it—and this is my perspective, because sometimes we say, "Hindsight is 20/20. If we had only done that." Is that something that you review on a regular basis, or are there things that you've tracked along the last 10 years that you've been in place? I guess what I'm thinking—I'm hoping it's not fixed.

1420

Can you maybe highlight some of the things where you went from A to B, that you've changed to make the process better?

Mr. Bert Clark: Again, maybe John could talk a bit about—it is price and quality, or price and qualitative factors. There are quite a few things within the qualitative factors other than generic quality. We actually try to not change the model massively from project to project and the way bidders approach them, and we only do that where necessary to increase the efficiency of the process and bidding and building these projects. So unless there are good reasons for changing the mix, we don't.

Mr. Lou Rinaldi: I wasn't referring just to the model from project to project. That's not what I'm looking at. I guess it's the overall picture, the bigger picture. You must have learned, over the course of 10 years, that things are different, whether it's the technology—and I guess more of the bigger picture.

Mr. Bert Clark: Let me give you an example of something we've introduced at the RFQ stage over the last two years: the local knowledge requirement. Our experience on a couple of projects was tough, and tougher than it needed to be, in our view, because we found that some of the teams that showed up to bid projects didn't have the local knowledge or the expertise that was required to successfully build the project. Even though our contracts have lots of protection in them for us, it's still, frankly, painful dealing with a project that's not going well, even if the pain is mostly being suffered by them and the financial pain is theirs.

So one of the things we introduced about two years ago was a requirement that teams be able to demonstrate that somewhere within the team, there's the local knowledge and expertise to deliver the project successfully. So that's an example of the evolution of the way we evaluate our projects. But as I say, it's not something where—if we feel it works quite well, we don't revisit it unless there's a good reason to do so.

Mr. Lou Rinaldi: Just to change gears a little bit again, when I look at the chart, most of your projects that are either ongoing or finished are health care-related. I know, for example, just east of me, part of Quinte Healthcare—there was a new wing added about seven or eight years ago through Infrastructure Ontario. I know they were quite pleased with the outcome and how it came about, finished and done. There are a number of other examples. The Runnymede Healthcare Centre was done ahead of schedule and under budget.

Can you maybe touch—because that's certainly one of the things you've had a lot of experience and expertise on, through the numbers. Can you give us some sense of how especially the procurement process—and I guess I'm focusing on health care—has improved the way that you look at future projects, for the betterment of folks who need that infrastructure?

Mr. Bert Clark: John, do you want to—

Mr. John McKendrick: Yes, sure. My name is John McKendrick. I'm the executive vice-president of major projects at Infrastructure Ontario.

I would say that certainly we started off with a lot of smaller hospital projects. You learn from things that go wrong as you go through. If you discover contamination, then you learn how to strengthen your specifications to transfer the contamination risk, or other soils risks. You learn how to manage the integration of diagnostic imaging equipment into the contract, because that could be a major source of change orders if you're not careful with that.

It certainly allowed us to move up to bigger and bigger projects. We now have the new Oakville Hospital under way; that's in the range of a billion dollars. We also have the Humber River Regional Hospital project, which is in the range of a billion dollars, too. Those projects are going very well. They're going to be completed this summer, on time and on budget.

It's really just a matter of, the more you do something—and also the industry has completely stepped up. They've learned, as well, and they're very efficient. They know how to manage the risks, as well; it's not just us. We've been able to improve the documentation that we give out, and when we do transfer the risks, the industry knows how to manage the risks.

They have definitely become more innovative in their designs, and thinking about more ways—the St. Joe's project in Hamilton was a very good example. They are willing to take more risks in terms of changing the design around in a way that will save money for taxpayers, but still knowing that they will be able to give the users the design that they want, so they're more sophisticated about interacting with the hospital management. So the more you do something, it—okay. Sorry. I'll stop.

The Chair (Mr. Ernie Hardeman): The more we do, the more time it takes.

It goes to the official opposition. Ms. Munro.

Mrs. Julia Munro: Thank you very much. I just have a couple of questions that I hope I can squeeze in here.

My first one is putting on my MPP hat for the kind of question that I think my constituents want to have answered, and that has to do with the way in which this process influences employment.

You mentioned—I'm sorry; I'm not sure which one of you—the fact that it has been a stimulant to the kind of growth in expertise and in management by the construction companies, which I take as a very definite positive outcome, but I'm now speaking in terms of people who would be further down that chain. The kind of potential problem that I would be concerned about is, does the local community have the expertise? Can they get the contracts? Are you bringing people from any distance? What do you see as trends in the area of the actual construction and workforce impact that what you do has?

Mr. Bert Clark: I'll ask John to—

Mrs. Julia Munro: Yes.

Mr. John McKendrick: Yes, typically what we've always learned from the projects is that it's always best to have local companies working on the projects. Certainly, if you don't do that, it typically costs more. You have to pay accommodation costs and transportation costs when you bring people from outside of the area, and making sure that price is an important driver ensures that you'll get the local people and skills—subtrades and contractors—working on the project.

Also, you will find, generally speaking, that the local contractors know the local situations better. They'll understand the nature of the soils. They'll understand if there are contamination issues. They'll understand how to source labour and materials in that particular area. They will understand the authorities having jurisdiction, so they will know the building inspector and the planning department better. All those factors add up. If you don't understand those, you can really get tied up very quickly before you even get into a project. So it's really only if you require a very specialized skill set or a very specialized subcontractor that you would think about bringing them in from outside of the area, but I think that is not very common.

There was one other issue. I think, really, the local knowledge in the RFQ is kind of just an extension of that. I think that's the way to go for these types of projects, for sure.

1430

Mrs. Julia Munro: I appreciate the answer because it is something that people have some apprehension about, particularly when they see somebody who is a major contractor and what kind of loyalties there are in the community. I think that's a really important message to be able to take.

The other question that I have is more of a personal one, in the sense that I'm curious. When maintenance was added to the list of obligations, I recognize that came partly as a result of the fact that you could bid on something and put, perhaps, cheaper items in there that, because you walked away when it was done, weren't your obligation any more. I always appreciated the fact that maintenance, then, was added. But my question is, what kind of risk management do you have to do in order to feel comfortable when you're looking at a 25-year or 30-year contract? It's more a question of curiosity than anything else.

Mr. Bert Clark: Let me start by saying you're absolutely right that getting the person who builds it to have the responsibility for maintaining it for 30 years radically changes the way the builder thinks about what they're building.

Mrs. Julia Munro: Exactly.

Mr. Bert Clark: Not only do they build things to last but they start making what people refer to as whole-life decisions. A simple example of that is, in the past someone might have installed a linoleum floor because that was the cheapest thing to put in, whereas tile would be much more expensive but the linoleum is something you're going to have to replace every seven years. When you add up all the times you're going to replace that linoleum, it's actually more expensive than the tile. When you get the builder with responsibility for operations, not only do they build something that lasts better, they build something that is cheaper on a whole-life perspective. That's a huge benefit for the public sector.

I guess ultimately we prescribe those outcomes, we prescribe the quality we want to see for 30 years, and the ultimate risk strategy we deploy is that we don't pay if the performance isn't there. Once we get to substantial completion of the asset, we pay them a percentage of the construction costs but we withhold a certain amount for 30 years to give them a very strong incentive to make sure that what they build actually performs that way, because if it doesn't, we have a penalty regime in our contract where we simply deduct dollars for poor performance. So they have an incentive to address it.

Mrs. Julia Munro: Thank you. That's it.

The Chair (Mr. Ernie Hardeman): Anything further? Further questions from the official opposition?

Ms. Lisa MacLeod: No. I think we're pretty good. I think I've asked all my questions. We had been spending some time straightening up.

I would leave it with one final thing: In terms of your work across the country and throughout the rest of the world—obviously you're one of the first, I would say, agencies of a government in this country to be charged with this type of responsibility, this type of budget and this level of activity—what are your experiences with other jurisdictions, whether it's in this country or elsewhere around the world, in terms of how they assess risk, how they screen projects and what their threshold is?

Mr. Bert Clark: The $50-million threshold, is that the question?

Ms. Lisa MacLeod: Yes.

Mr. Bert Clark: It varies. At the federal level in Canada, I think it's still $50 million. In British Columbia, it's recently moved to $100 million. Beyond that, I'm not sure I can tell you what it is—

Ms. Lisa MacLeod: Why would British Columbia go up to $100 million?

Mr. Bert Clark: Frankly, likely for the same reasons as us, which is that they've been delivering major projects now—Partnerships BC, which is the rough equivalent of IO, with a much narrower mandate but does a lot of the same things we do, actually started before us. They've had many, many years now of delivering large projects and are starting to think, "Maybe we could move that number up." Also, there is inflation, so $50 million 15 years ago is not $50 million today.

Mr. Ehren Cory: On the other part of your question, on the screening more generally, some version of doing a business case or doing a value-for-money analysis is what almost everyone does. There's a survey; it's in some of the third-party material. If you look at 20 OECD countries that use some kind of P3, 19 of them use something like what we do, which is to compare the cost of the financing against the risks.

One example where we know they used to do that and they've actually stopped now and screen on more, I'll say, qualitative factors in making decisions is in the UK, where they've actually started evolving beyond doing VFM. But in general, the answer to your question is that every jurisdiction uses some form of the screening tool we do, where you're trying to weigh that tangible financing cost against the risks that your transferring to the private sector.

Ms. Lisa MacLeod: Are any members of your board members of a similar entity in any other jurisdiction?

Mr. Bert Clark: No.

Ms. Lisa MacLeod: I only ask this because I used to be a member of government agencies. We actually had Infrastructure Ontario in a number of years ago.

Interjection.

Ms. Lisa MacLeod: You were on the committee then, too? I guess you can't get rid of me. I travel around with you.

The reason I was asking is because we did, in some cases, have have some people involved with lottery and gaming in other provinces and things like that.

What kind of conversations would you have, for example, with British Columbia in terms of best practices? Would that be quite frequent?

Mr. Bert Clark: There's something called the pan-Canadian working group that meets or talks at least twice a year. That involves more than us and BC. It involves now all of the jurisdictions that are involved, which is Alberta, Saskatchewan, the federal government, Quebec and—

Mr. Ehren Cory: New Brunswick

Mr. Bert Clark: —and New Brunswick. So they meet and talk regularly.

Ms. Lisa MacLeod: To your knowledge, are they also subject to value-for-money audits by the auditor? Have any of them been, do you know?

Mr. Bert Clark: I don't know what the mandate of the Auditor General is in each. I'm assuming it's about the same.

Ms. Lisa MacLeod: Would you know?

Ms. Bonnie Lysyk: There have been reports written by other Auditors General; I believe in Nova Scotia, and I believe there was a report written in British Columbia as well. I think the federal government did some work in the area assessing their—I think it's called PPP—

Interjection.

Ms. Bonnie Lysyk: Yes, so there has been other work done.

Ms. Lisa MacLeod: Okay, very good. I have just one final question, and it's really not on topic, so just let it go, Chair.

With respect to the Ottawa LRT, you're working as an advisor there. You're also doing the same thing in Waterloo. What is the shape of the advisory role that you take with municipalities that choose to go it alone but then may need some support?

Mr. John McKendrick: Really, it's up to the municipality to decide how much or how little they want us. They will take our documents, and we will advise them sometimes to follow our advice; sometimes they don't follow our advice. Sometimes we will amend our documents—

Ms. Lisa MacLeod: Sort of like here at Queen's Park.

Mr. John McKendrick: It's their money, and it's up to them as to how they want to do it.

Mr. Bert Clark: In both of those cases, we were much more actively involved with the municipality, the region, during the procurement phase. Once the contract was awarded, they had actually built up internal teams within their governments.

Ms. Lisa MacLeod: So you helped them with risk assessment and how to do the scoring—

Mr. Bert Clark: Risk assessment, the documents, the process, the procurement. We helped them select a partner. Then, when they get into construction, they tend to take over more of the responsibility, I'd say. We're still present, and we're always happy to help. In both of those cases, we've certainly got calls after the fact, "Could you help me with this? Could you help me with that? Could you have a guy come out and see us?"

Mr. John McKendrick: And as an example, if an issue arises with the project company or a claim arises, they'll come to us and seek our advice. We will talk about our experience on similar issues on similar projects. That's one of the advantages: If you've done enough of it, or for a lot of it, then you tend to have seen more things than they might have seen on their own, if it's the first time they've ever done it. You can share that experience with them and help them deal with it, and make suggestions and recommendations about how to approach the issue with the project company, and they find that helpful.

Ms. Lisa MacLeod: So a lot of the companies that they would deal with, you would deal with quite frequently too, right?

Mr. John McKendrick: It would be the same companies, yes.

Ms. Lisa MacLeod: So that means that it's going to be on time and under budget. Is it?

Mr. John McKendrick: We hope so, yes.

Ms. Lisa MacLeod: Okay. Thanks very much. I do appreciate the round of questioning and you coming in. Thanks again to the auditor and her staff.

The Chair (Mr. Ernie Hardeman): Thank you very much. That concludes the questioning. Thank you very much for coming in this afternoon. We appreciate all the information you've given us, and we can use it in our deliberations as to preparing a report.

With that, the committee does have to go in camera to discuss some of the report-writing, so if we could just clear the room as quickly as possible so we can get that done.

The committee continued in closed session at 1441.

CONTENTS

Wednesday 25 March 2015

STANDING COMMITTEE ON PUBLIC ACCOUNTS

Chair / Président
Mr. Ernie Hardeman (Oxford PC)

Vice-Chair / Vice-Présidente
Ms. Lisa MacLeod (Nepean–Carleton PC)

Mr. Han Dong (Trinity–Spadina L)
Mr. John Fraser (Ottawa South L)
Mr. Ernie Hardeman (Oxford PC)
Mr. Percy Hatfield (Windsor–Tecumseh ND)
Ms. Lisa MacLeod (Nepean–Carleton PC)
Ms. Harinder Malhi (Brampton–Springdale L)
Mrs. Julia Munro (York–Simcoe PC)
Mr. Arthur Potts (Beaches–East York L)
Mr. Lou Rinaldi (Northumberland–Quinte West L)

Substitutions / Membres remplaçants
Ms. Catherine Fife (Kitchener–Waterloo ND)
Mr. Michael Harris (Kitchener–Conestoga PC)

Also taking part / Autres participants et participantes
Ms. Bonnie Lysyk, Auditor General
Mr. Taras Natyshak (Essex ND)

Clerk / Greffier
Mr. William Short

Staff / Personnel
Mr. Ian Morris, research officer,
Research Services