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Rebuilding Strong Communities

P3 Recreation Facilities: Who benefits?

Physical activity is essential to human health and development. As communities grow, municipalities across Canada are seeing an increase in demand for recreation services such as community ice time at local hockey arenas.

Municipal governments have an opportunity to invest in publicly owned and operated facilities that build community assets and expand access to services. But competing costs and limited capital budgets are leading local governments to seek alternatives to public investment for capital projects like arenas and recreation facilities.

Private for-profit companies are eager to offer a convenient package that includes both financing and operation of new facilities through public private partnerships (P3s) or alternative service delivery (ASD), but at what cost? The profit-making incentive can influence the nature of a project so much that it may no longer address community needs, despite the higher cost of pursuing the project to the municipality and its taxpayers.

THE TROUBLE WITH PUBLIC PRIVATE PARTNERSHIPS

HIGHER COSTS

P3s are promoted as a way to keep debt off the public books but, while P3s may hide debt, they never reduce it – just the opposite.

- Higher borrowing costs and the need to generate profit, make private financing more expensive.
- Lawyers, accountants and other consultants, detailed proposal processes,

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- drafting, negotiating and renegotiating complex agreements, are all expenses incurred by the public partner that add up before the shovel hits the ground.

- Once a P3 is up and running, legal and forensic advice, audits, termination payments, monitoring and negotiation, are additional costs rarely factored in to the costing of a P3 deal.

- Add in lost revenue from ticket sales, concessions and space rental that the city would receive in full were the facility publicly owned and operated, and the cost of the deal increases again.

ECONOMISTS AGREE:

- Auditors General of Ontario, Nova Scotia and New Brunswick, and the National Audit Office in the U.K. have expressed concern about claims that P3s are cheaper than public ownership. They question P3 accounting practices and the extent to which they obscure and hide real public liabilities.[i]

- The International Monetary Fund also recently issued a report warning against "off-book borrowing" for P3s. The IMF's managing director stated that P3 debts should be counted as public borrowing, and that "governments had 'no business' hiding private finance projects away from their balance sheets."[ii]

REDUCED ACCESS

Equal access to sports and recreation facilities is essential for an equitable society where everyone has a fair chance regardless of their social class, race, gender, or ability.[iii] And governments' role is to ensure that all children have the opportunity to realize their full potential and fully participate in community life.

- Studies show that active children achieve higher grades, are healthier, and are less likely to smoke and to abuse drugs and alcohol. Access to community recreation programs has also been linked to reduced crime rates.[iv]

- To promote access, municipalities typically subsidize the cost of ice time in public recreation facilities, whereas the private profit motive drives operators to charge the highest price the market will bear.

While the motivation to pursue a P3 may be increased recreation capacity, the private sector profit-focus may actually reduce access.

Increased Risk, Reduced Accountability

P3s compromise democratic accountability and transparency, while the public partner shoulders the risk of bad deals that go on behind closed doors.

- The terms of P3 contracts and negotiations are typically kept secret in line with standards for private sector commercial confidentiality. Public policies and procedures that require public consultation and transparency are seen as obstacles to P3s.

- The public and elected representatives have little, if any, opportunity to influence how services are delivered and how tax dollars are spent and invested.

- Lines of accountability on the private side are unclear, since the bidder is usually a group of companies that acts as an individual entity without clearly defined roles and responsibilities.

- When P3 business ventures fail the taxpayer absorbs any additional costs because the public partner is ultimately responsible for providing a public service. Municipalities are left carrying the cost of debt incurred at private sector borrowing rates. Just ask people in the municipalities of Guelph, Victoria, Cranbrook, Port Alberni, and elsewhere.

Who pays? Who Benefits?

Privatization widens the gap between rich and poor and reduces average incomes and spending power in communities are reduced with privatization. Corporate profits are made at the expense of community interests. Private, for profit projects almost always transfer profits out of the community.

Companies, like Maple Leaf Sports and Entertainment (MLSE) and US Global Entertainment Corporation, are eager to get on the public recreation bandwagon and advance private for-profit ventures. But what they deliver is a whole different ball game from what municipal governments set out to achieve.

- Instead of additional ice time at affordable rates, towns and cities often get plans for multi-million dollar entertainment complexes in response to requests for proposals. Community recreation facilities are a secondary consideration, yet costs paid by the municipality are high. Local governments are left with little flexibility around scheduling and setting of fees to ensure public access.

- Auditors and auditors general consistently raise concerns about potential mismanagement of public funds with P3s. In recent reports, organizations such as the World Bank and, more locally, the CD Howe Institute, that support privatization, cannot point to any outright successes in terms of public benefit.

- This was confirmed by a report issued by the City of Newmarket, Ontario's Director of Parks, Recreation and Culture in 2003. The study recommended that the city not pursue public private partnerships for their community, because "…*the costs and risks outweigh the benefits which can be generated from a public/private sector model*." [v]

THE EVIDENCE: TRUE STORIES OF MUNICIPAL P3 RECREATION FACILITIES

In 1996, **City of Victoria** struck a deal with Victoria Sports/Entertainment Associates to build and operate a multiplex facility. The company broke its promise not to increase costs and in 1999 the deal was cancelled. The City put out another call for expressions of interest. Four firms responded and only one qualified: RG Properties. The second attempt at a P3 deal cost the City almost double original estimates after accounting for interest payments over the life of the deal.

The project was originally scheduled to open in August 2004. One year later, the timeline has been pushed back yet again, and the completion date is still anyone's guess. [vi]

Construction companies who say they are owed millions for unpaid services have filed lawsuits against the City. Residents of Victoria will be absorbing some of the increased costs through ice rental fees at least 25% higher than rental fees at the municipality's publicly owned and operated arenas.

The **City of Guelph**, Ontario invested $10.5 million of public money and then guaranteed a $9 million loan to a private company (Nustadia Developments) to build a P3 arena mall complex called The Guelph Sports and Entertainment Centre. [vii] Still early in the 35-year deal, the company realized they were in trouble when revenue turned out to be lower than expected. After having already subsidized the project with almost $20 million in capital funding, the City was now forced to the cover private partner's portion of the debt as well.[viii] In the summer of 2001, the City began to pay Nustadia's $750,000 mortgage payments and all federal and corporate taxes associated with the project.

The **City of Cranbrook**, BC tried a P3 to keep the debt incurred from building a 4250-seat arena off-book. The private partner had trouble securing financing, construction was late getting started, there were cost overruns that the City had to absorb and the City's borrowing power was reduced substantially as a result of the long-term lease.[ix] Ownership changed hands several times and when the project failed the City found itself with the highest debt level in the province. The tax increase to residents of Cranbrook alone for this project was 7% and fees increased considerably from what was charged at the city-owned rinks.[x] The facility was brought in house.[xi]

PUBLIC FINANCING ALTERNATIVES

Governments have options. Firstly, the cheapest way to finance any project is through public borrowing, because municipalities typically have the best credit rating around and thus have access to the lowest borrowing rates.[xii] Secondly, many new, and tried and true mechanisms exist to leverage public funds for infrastructure.

- **Tax-exempt bonds** allow municipalities to borrow funds at lower rates of interest than they would pay on regular bonds.

- **Crown corporations**, like the Canadian Mortgage and Housing Corporation, wholly owned by the federal government, can issue bonds and have significant borrowing power. With sufficient pressure from municipalities, the federal government could create an infrastructure corporation, structured as a wholly owned crown corporation similar to CMHC.

- Municipal financing authorities exist in most provinces, which allow municipalities to benefit from **pooling of debt**. These can be expanded.

- Dedicated infrastructure funds, subsidies from senior levels of government, and innovative solutions like Public Interest Companies (PICs), are all viable options.

Lewis Auerbach who formerly served as Director in the Audit Operations Branch of the Auditor General of Canada has addressed governments' opinions in this way:

> "*Governments can decide not to make funds available, or to make them available for some kinds of projects and not for others. In other words, the constraints that lead to the choices are self-imposed. It (P3) is a choice especially difficult to comprehend when it leads to higher, rather than lower cost to taxpayers*".[xiii]

COMMUNITIES ARE CHOOSING TO KEEP IT PUBLIC!

After years of debates, proposals and expenditures on negotiations and public hearings, in the spring of 2005 the **City of Oshawa** finally chose the most affordable option to finance its new Downtown Sports and Entertainment Complex: public financing.

In the year 2000, the **City of Nelson,** BC was looking to develop a recreation complex. It was to be about the same size as Cranbrook's, at a projected cost of about $19 million. They received proposals from three private sector companies but decided against taking the P3 route. Instead they borrowed the money from the Municipal Finance Authority. "We thought we might as well take the risk and lower (borrowing) costs," the Mayor stated.[xiv]

QUESTIONS FOR MUNICIPALITIES CONSIDERING P3 RECREATION FACILITIES:

- Will the municipality do a proper comparative analysis of public versus private financing, considering all associated costs from conception to completion over the life of the contract?

- Should the project fail to provide adequate return for the private proponent, is the municipality prepared to pick up the tab of the full project at the higher cost incurred by private sector borrowing?

- Can the municipality guarantee that the project will deliver appropriate and sustainable services in exchange for public investment or is the city prepared to subsidize corporate profits through tax dollars with little return for the community?

- Can the municipality ensure that all negotiations and contracts will be available for public scrutiny? If not, is the municipality willing to compromise its own commitments to transparency and democratic accountability in order to "partner" with the private sector?

P3s result in increased public costs, hide public debt, reduce accountability, and allow public funds to be directed away from community priorities.

P3s mean compromises on quality and contribute to increased social inequality by reducing access to City services.

Public debt is more cost-effective and allows municipalities to retain public ownership and control of assets.

Public ownership ensures that there is a process where elected officials can advance community concerns.

For more information on the dangers of privatization and public alternatives please visit: www.cupe.ca/www/privatization

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Research/wptext/CONTRACTING OUT/P3s/Arenas August 2005.doc

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[iii] Parliamentary Report, www.parl.gc.ca/InfoComDoc/36/1/CHER/Studies/Reports (28/04/2005)
[iv] Canadian Council for Social Development, Insight report, Spring 2001
[v] Town of Newmarket, Parks, Recreation and Culture Report 2003-38, Ascertaining Priorities, re: Public/Private Partnerships, December 23rd, 2003.
[vi] Goldsworthy, Rachel, " Replacing Victoria's Memorial Arena long saga," July 14, 2003, Journal of Commerce, Vol 92, No. 55
[vii] Metroland Papers, Wednesday October 22, 2003: byline: Martin Derbyshire
[viii] Metroland Papers (Guelph), p.1, "A tale of two public private partnerships".
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[x] Cranbrook Daily Townsman, May 15, 2001, "Cranbrook taxes to go up almost 11%."
[xi] The Daily Townsman (Cranbrook): August 3rd, 2004, page 4, Barry Cloutier; August 4th, 2004, "Questions remain concerning Rex Plex employees, Kootenay Ice," page 1, Mark Hunter.
[xii] CUPE Research, Telephone conversation with representative from Niagara Credit Union, August 2004.
[xiii] Auerbach, Lewis. *Issues Raised by Public Private Partnerships in Ontario's Hospital Sector*, 2002
[xiv] Nelson Daily News, December 11, 2001