New Opportunities to Achieve through Public-Private Partnerships

Helping the federal government be more efficient and effective faster, with quality services at a lower cost

P3

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COE Center for Organizational Excellence

An Opportunity May Exist for a Faster More Effective Government at a Lower Cost

A Public-Private Partnership (P3) is a joint relationship between the government and a private company designed to optimize a needed service or product that each entity cannot efficiently or effectively provide independently. It is used when the government has a need without the full expertise required, the resources, ability to move quickly, or funding for an important program. To address the need, the government partners with a private sector entity with the right expertise, ability to move it forward quickly, and realize a result or financial upside for both parties. To succeed, the government needs the capacity of the private sector, and the private sector needs the resources and authority of the government. In a P3, they share accountabilities, decision-making, performance, risk, and financial benefits.

Traditionally, P3s have focused on community needs usually related to support infrastructure projects such as roads, hospitals, ports, prisons, tourism projects, community revitalization, schools, and airports, among others. A recent report indicated that the US needs $3.6 trillion in infrastructure projects by 2020 that can't be immediately funded by federal or state governments. Some countries engage in P3s much more than the US and actually have dedicated P3 offices to initiate and manage them.

The Virginia Route 95 EZPass toll lanes are an example of a P3, one that created more road capacity much earlier than could have been done by the state with both the state and the private sector benefiting from its use through the collection of user fees.

In the federal government, the General Services Administration uses P3s for some property projects. Another example of a different type of P3 is when the Air Force allowed a private sector company to use underutilized depots to service Army contracts. The Air Force received payment for this without which the depots would have otherwise sat dormant and they would be expending maintenance funds without benefit. The Air Force collected over $1 million for its use.

Given federal budget limitations, there is great opportunity to expand the use of P3s into other areas beyond traditional infrastructure projects. For example, the Internal Revenue Service (IRS) uses a P3 for debt collection. P3s could also be used for mail delivery or depot operations.

NOTE

P3s could also be non-revenue generating in nature such as the government working with the private sector to develop solutions to thwarting cyber threats. They work together, each contributing expertise and funding. While the solution may be marketable by the private sector later, the initial intent is not fee or revenue generation; rather it is accelerating a process for quicker results while sharing the load.

This paper, however, focuses on those P3s that require funding to meet a need and where both parties benefit financially.

In another example, the Combined Federal Campaign used it to reduce startup costs for the new technology platform that the Office of Personnel Management (OPM) built to reduce administrative costs and ensure more funding goes to charities. The private company developed the system and receives fees from the charities who registered to use the platform once it was launched and operational. The government benefits by making it easier for federal employees to donate online and reduce the cost of operations by eliminating paper and cash donations. The new system was built much more quickly with little to no cash outlay and modernized in the process at no cost to the government. The private sector company benefits with a continued revenue stream after the program is implemented for a long period of time. The giving community benefits on both sides with charities able to reach more donors at a lower cost and with federal employees having more choice and control.

With P3s, the government can also benefit from having access to thought leadership, the latest technology, and expert resources that can transfer skills to government personnel. They can take advantage of industries ability to innovate faster, without oversight, and being unencumbered by bureaucracy and self-limiting oversight.

Avoid Shiny Object Syndrome

The government should advance its thinking to nontraditional areas that may have P3 possibilities. Imagine using P3s to provide internal human resources (HR) or payroll services or issue grants. P3s could run government training centers; build and operate health record systems and programs; perform data analysis, reporting and analytic function, among many others for a fee. Imagine the private sector providing logistics services or operating parts of Veterans Affairs hospitals on a fee basis. Shared services across all disciplines (HR, finance, grants, etc.) are ripe for a P3, and many companies are ready with the systems and tools to implement with a clear return on investment (ROI) for the government and private partner.

A P3 has:

- A defined need and demand
- A required investment
- The ability for the private sector to provide expertise, development, intellectual property, or technology
- The opportunity for a return on investment for both the government and private sector

Some functions would be difficult to conduct under a P3. For example, while the Social Security Administration could outsource the administration of benefits, pay vendors for this task, and possibly reduce costs, it is not a partnership. It is a function that is highly regulated and not on a fee-for-service basis, which would prevent the sharing of risk, decision-making and accountability. It would also have reduced innovation and little financial upside. It may be an opportunity for outsourcing at a reduced cost, but not a partnership.

OPM's HR solutions function provides support to agencies for a fee in areas such as hiring, classification, human capital planning, training, leadership development, etc. This could potentially be an area for a P3 if a private company can develop and influence service offerings and intellectual property, participate in decision-making, and see a return on its investment based on a steady demand for services. However, it can easily dissolve into a contract relationship if the above conditions are not met and demand is not predictable.

To be a candidate for a P3, an agency must be able to ensure the program or requirement meets certain criteria and considerations. The government needs a mature approach to conceiving and managing P3s. A P3 has financial, operational, and asset requirements that must be considered, and it has to include incentives and accountability for both the government and the private company. Just because you think you have a need, yet have no money, is not a reason to do it. It is important to not have "shiny object syndrome" and move too quickly, but to plan and assess all aspects of a proposed P3 to ensure its success and ensure this approach is best for the government. The government must be cautious that it is not beholden to a proprietary approach or technology that a company promotes only to end up with something that doesn't fit. Due diligence is critical to the partnership, and the government cannot look through rose-colored glasses.

Major Success Factors for P3s

P3 Critical Success Factors:

1. A well thought-out and valid business case with a clearly defined market need or demand
2. Financial and other incentives for both parties
3. Cross-partner consistency in governance, effort, and performance
4. A partnership-based, rather than contract-based, procurement approach

P3s should not be used to outsource the government, and it is not appropriate for every situation. Inherently, government responsibilities must remain in the government — such as defense, the general welfare of its citizens, decision and policy making, etc. — however, where it is appropriate operationally, it must begin with a vision, be well conceived, and ensure it is capable of being successful. In areas where a P3 could help advance the government, it is necessary to take the time to start off right: involve the experts, prepare the agency, stay organized, and think through the partnership. This includes the following factors:

Develop a strong business case. Each P3 idea begins with a vision. If it seems viable, it then develops into a written business case. A strong business case for a P3 has a clear, realistic, and justifiable purpose for what needs to be done, why it needs to be done, and why a P3 is the right approach. It forces you to do your homework and includes outcomes, demand assessment, risk/rewards, a financial model, boundaries, governance, and more. The business case is essentially the design and story for a successful P3, resulting in approval to move forward.

A failed P3's greatest issue is poor business case development. Take the time to think this through and do it right. Additionally, other components that contribute to failed P3 include not having buy-in from the top, unprepared procurement personnel, lack of demand analysis, traditional thinking, and an unengaged private sector. No government or private company would want to invest if the end goal is not clear. "Build it and they will come" is not an option here, it must be proven viable for both parties.

While leadership champions are essential, stakeholders should also be heard. They can participate in the P3 concept or design, serve on an advisory board, or participate in some way to express their views. Scenario planning can be an effective tool, involving everyone to get the concept right and the business case developed, validated, and approved.

Elements of a P3 Business Case:

CONCEPT

- Statement of the problem/need
- Goal and objectives
- Statement of outcomes
- Justification for the P3
- Examples of how it's been applied in other organizations for the specific type of application
- Evidence of private sector interest

MARKET ANALYSIS

- A fact-based demonstration of the stakeholder need/demand
- A description of how the demand is currently being met, if at all

SOLUTION

- Description of how the P3 will meet the need and achieve the required results
- Measure of performance and achievement

APPROACH

- Methods or approach used to achieve the P3
- High-level plan with milestones
- Identification of resources, intellectual or real property, or other assets each party will provide

FINANCIAL PROFILE

- Investment requests
- Estimated cost
- Revenue/fee stream and sharing model
- Anticipated growth or reductions
- Cost and cost/benefit analysis

GOVERNANCE

- The recommended governance model
- Identification of policies, procedures, decision-making, advisory groups, and accountabilities
- The legislative or regulatory basis for performance and any adjustments that may be required
- The need to reform policies or processes before engaging in the partnership

RISK AND MITIGATION STRATEGIES

- Identification of risk/barriers and mitigation strategies — jointly and for each party
- Alternative considerations to a P3 approach with pros and cons

Ensure the financial model is right for both parties. P3s do not employ traditional contractual procurement mechanisms whereby the private sector is paid for services rendered based on meeting government specifications. Instead both parties realize financial benefit at a future date based on fees or a revenue stream, while the government also saves up front development costs. This is not to say the government cannot put up some funding, but it would not have the burden to carry the full load.

In a partnership model, the private company is usually bearing a significant risk and should also see a reward that is higher than the normal profit margin on a traditional contract. They are putting up capital to get the project off the ground, experiencing risk, and taking on the burden of the cost of capital with deferred remuneration.

Both parties should plan for a return within a reasonable timeframe, and the cost of capital should be included in that return. The amount of the investment should be defined up front, and the private company should be able to recover a defined amount of money from the government if the demand estimates are not realized or the government business case is flawed.

The government must also do significantly more due diligence to ensure the private company selected has the financial strength, motivation, and realistic expectations to achieve the solution and ensure it is right for the government.

Both parties should benefit from efficiency gains created during program operation. Since the private sector is traditionally more experienced at cost containment, it can usually identify and realize savings in process and output, making a higher fee or cost of capital more easily absorbed.

If post-deployment efficiencies are realized, there should be a formula based on a risk profile for sharing the cost efficiencies between both parties. Efficiency sharing should be based on who holds the primary burden of the risk and costs and therefore may not be equal. While it may be both a science and art to design, the efficiency sharing arrangement could be 80/20, 60/40 or any other appropriate ratio.

Small- to mid-tier companies may not have this opportunity, as they may not have the capital and resources to invest up front. To combat this, the government should consider allowing for the cost of capital to be recovered, so these firms can then have the opportunity to be considered. If lenders are involved, they will want to review the potential P3 and be confident that a return is possible within a reasonable timeframe. Also, the government could require that a percentage of the overall work be subcontracted, which will allow them to participate. In this case, small companies should participate in the financial upside. Also, perhaps small companies could provide surrounding services such as requirements gathering, PMO services, stakeholder management, marketing, training, change management, etc.

Examples of Nontraditional Public-Private Partnerships:

Program Federal Government Shared Services

Description Provides fee-based transactional services for all federal agencies. This can include payroll, human resources, financial management, grants management, etc.

Partnership Private sector provides services using their technology and capacity on a volume-based, reduced-per-head cost, consistent with laws, regulations, and reporting requirements. Government maintains ownership of the data and provides policy and oversight. Joint activity on reengineering and preparing the system for contemporary and future use. Upside to both parties for increased efficiencies as process matures.

Investment Upfront cost of developing secure technology systems, reengineering, change of regulations, legislation, change management, training, etc.

Shared Risks Agencies may not be willing to participate unless government leadership strongly backs and requires it resulting in reduced adoption. Too many perceived one-offs and bureaucracy could weigh down performance and an ROI. It would require reengineering of data, policy, and processes before developing the tools and offering services. Data security required. Shared governance could add bureaucracy and bottle necks.

Rewards

Government

- Lower transaction and overall costs
- Maintaining the latest technology without costly upgrade requirements
- Consistency in data standards, product offerings, and customer service
- Full cross-government data analytics capability
- Government focuses on mission

Private Company

- Continuous revenue stream
- Developed IP for applications beyond government
- Market positioning

Program Improper Payment Collection

Description Provide commission-based services to identify, verify, collect, and correct improper payments that are estimated to be over $50 billion. Improper payments can be due to miscoding, sending to the wrong recipient, fraudulent use of funds by the recipient, etc.

Partnership Private sector provides review and collection services and provides input to the government for systemic corrective action. Government provides access to data and recipients as well as rules for engagement and ensures security. Together they prioritize their efforts and share in the return.

Investment Infrastructure, staff, staff training, technology, security clearances, etc.

Shared Risks Private sector has the risk of reduced return on investment if review and collection process is not effective. If done right and corrective actions are taken, demand for service should reduce over time. Government has the risk of improper or overzealous action by the private sector partner as well as time wasted with little return. Secure control of PII is necessary.

Rewards

Government

- No operating costs
- Return of payments and/or redirected to rightful recipient
- Reduced fraudulent use of tax payer funds
- System or process that caused the improper payment is reduced or eliminated

Private Company

- Continuous revenue stream
- Market positioning
- Systems and tools for use in other markets on a large scale
- Reputation

Examples of Nontraditional Public-Private Partnerships (continued):

Program Federal Government Training Center Delivery and Operations

Description Provide fee-based technical and soft skills training for government employees on a government-wide basis on a per-head fee basis. Could be technology-based, classroom-based, and simulation-based. Include the development and implementation of knowledge management tools and systems, job performance aids, and measurement. Could be used to support shared service implementation.

Partnership Private sector develops and offers curriculum, operates the training centers, measures results and reports to the government on a fee basis with easy funds transfer system. Government participates in job and needs analysis, serves as board members, and ensures the legitimate use of funds.

Investment Adoption and operation of existing training centers, staff, curriculum development and program maintenance. Development of alternative performance improvement tools and systems.

Shared Risks Private sector has the risk of ensuring demand meets operating costs and government policy, budgets, or redirection does not dramatically change the business model. Both parties share the risk of having qualified trained federal employees prepared to execute position requirements at the levels required. Government has the risk of misuses of funds. May not easily meet unique specific agency requirements.

Rewards

Government

- No operating costs
- Reduced per head fee costs for training, technology, etc.
- Consistency of training across the government
- Complete cross-government measurement and reporting of training and performance
- Easy access to best training solutions and renowned speakers
- Consistent cross government knowledge management
- Government known for high-quality employee development.

Private Company

- Continuous revenue stream
- Increased volume of serviced customers
- Market positioning
- Systems and tools for use in other markets on a large scale
- Reputation

Program Detroit Michigan Water System Cleanup and Operation

Description Provide fee-based water services to the public with an initial investment to clean the water and waste delivery systems.

Partnership Private sector provides costly treatment technology and systems, operates and manages those systems, manages the billing and collection of fees. Government regulates the requirements for clean and sanitary systems, and use of customer data. Both benefit by delivering safe potable water to citizens and share in the fees paid.

Investment Upfront cost or revitalizing the water system, monitoring technology and operations.

Shared Risks Both parties share the risk of ensuring the sanitation system meets health standards. Large investment required, may require a combination of private investment and public bonds. State and local interests must be addressed.

Rewards

Government

- Quicker response to health emergency
- Faster delivery of sanitary water to citizens
- Eliminates continual reinvestment and maintenance costs
- Little to no upfront investment
- Operating efficiencies and better service to residents

Private Company

- Continuous revenue stream, after significant investment
- Maturing of business model for cross-country applications to utility operations

How you govern can make or break a P3's success. A P3 requires significant monitoring, nurturing, trust, and well-defined processes, outcomes, and effort. Honesty and transparency are critical; trust is nonnegotiable. Since nontraditional P3s would be new to government, a well-defined governance system is critical, although learning and adjustments can take place as the program progresses, especially when the players are new to this way of getting things done.

A partnership — rather than a traditional contract relationship — requires collaboration and cooperation in achieving goals and objectives. Both sides of the partnership must have resources and interest. Both sides get to participate in decision-making (solution, implementation, policy, etc.), which must be clearly defined, and both parties' interests must be considered. There must be a defined financial model, as well as any share in asset ownership defined (product, intellectual property, data, etc.). Risks must be fully assessed up front by both parties and discussed openly and completely, and each party must appreciate and support the risks of the other.

There may be legislative or policy opportunities or barriers to be considered and addressed before the P3 can exist. Also, P3 policies, process, and procedures, must be developed and agreed on by both parties.

Both parties must define how the P3 will operate and how government and private company resources will work together to develop and operate. Both partners must live up to their part of the deal, effectively deploying agreed to resources and plans together. Mechanisms, such as dispute resolution or a governance board, may need to be put in place to address obstacles, issues, growth opportunities, and changes.

The government culture must support the P3. Within a P3, it is necessary to have full transparency, shared information, facts, and a process for sharing the evolution of facts in real time. Accountability, matched effort, equal attention to time and details, and quality of performance on both sides is critical with each party bringing intellectual and performance compatibility to the table. This does not mean each party carries half the load, but they must execute the load they agree upon flawlessly. Both sides must trust each other. Therefore, the roles and responsibilities must be clearly defined and well executed. Collaboration must be unencumbered by rules of engagement and interests, while the intentions, capacities, and diligence must be openly proffered and discussed.

Outcome measures and Key Performance Indicators (KPIs) must be well defined and agreed to, connected to the purpose of the P3, and owned by both parties. The two parties must define quality — in terms of output specifications, Service Level Agreements (SLAs), and performance levels. Security requirements, where appropriate, must be defined and executed.

Traditional procurement approaches will not work. A P3 is different and much more demanding than a traditional procurement, and requires a mature procurement office to support it. This is about negotiating a partnership rather than a contract, where the rights (mutual and independent) are delineated to encourage a collaborative, win-win outcome for the government, private company, and stakeholders. In this partnership, the private company participates in decision-making, and there is shared execution, accountabilities, and financial transparency between the parties. Both parties can experience scope creep, and they require and share due diligence and risk ownership. Furthermore, in a P3, it is necessary to have a different level of "open-book approach." Few agencies may currently have the requisite expertise, which in turn could require outside support.

It is essential to have fairness, reasonability, and a shared benefit. This is an environment in which a contracting officer is ensuring incentive and outcomes for both parties. There cannot be a fight for the Lowest Price Technically Acceptable (LPTA) or specifications that are overly prescriptive and too risky to achieve. Nor should there be negotiations over staffing, skill levels, or system specifications. You do negotiate the solution, accountabilities, roles, SLAs, decision-making, fee structures, etc. Both parties must understand the risk and incentive of the other, and agree to the achievable results, the path forward, and the accountability to each other without abdication.

There is a long-term nature to P3s (some last for 30 years or more), so the relationship is an investment. At a minimum, a nontraditional service arrangement should last at least 10 years to make the investment worthwhile.

It is critical that the government procurement office prepares itself for a new way of thinking.

Risks and Rewards

Both parties have risks and rewards in a P3. More importantly, in a partnership, they share risks and rewards. They must actively help each other minimize the risks and realize the benefits. Risks and rewards depend on the unique characteristics of the provided services; some of the common ones are depicted in the table below. Addressing these considerations will help to minimize these risks and maximize rewards to both parties and stakeholders as well.

	RISKS		REWARDS	
	Government	Private Company	Government	Private Company
FINANCIAL	Needs to protect public funds. Private company does not have the means to execute.	Excessive costs, becomes unprofitable. Time to return on investment becomes prolonged, limiting cash flow. Public believes it is profiting at governments expense. Cost of capital is prohibitive, or lender has restrictions that are not partnership friendly.	Increased value delivered = more revenues/fees. Zero or little upfront investment. Participation in efficiency gains.	Greater than average ROI. Stable long-term participation in efficiency gains.
MARKET	Reputation. The right services or product and demand is accurately determined.	Reputation. The right services or product and demand is accurately determined.	Reputation. Ability to adjust as demands shift. Government receives a marketing and communication engine.	Reputation. Long term opportunity and market ownership.
PRODUCT/SERVICE	Private company does not deliver on its accountabilities or makes promises it cannot keep.	Government does not deliver on its accountabilities.	Improved services to market faster. More sophisticated services. More advanced or innovative thinking and technology.	Additional intellectual property and assets. Capitalized cost of tailoring solutions for government partially absorbed by government.
GOVERNANCE	Change in policy derails investment. Bureaucracy gets in the way of performance and progress.	Change in policy derails investment. Bureaucracy gets in the way of performance and progress. Lack of trust impedes decision-making. Government interferes in solution design.	Skill transfer by working with outside experts.	Can truly contribute to effective government.
PROCUREMENT	Partnership does not appropriately balance accountabilities and contract specifications.	Partnership does not appropriately balance accountabilities and contract specifications.	Balanced partnership that achieves better results in a timely and cost-effective way.	Balanced partnership that achieves better results in a timely and cost-effective way.

Conclusion

P3s may not be for every situation, but if they meet the criteria outlined in this document, are careful thought through, as well as have the right orientation of the people involved and each one willing to share the risks and rewards, there is a clear upside for both parties.

Many opportunities may be ripe for a P3. Think about how you can better focus on mission and be more efficient and effective, saving money, and fulfilling need faster.

About COE

For over 38 years, COE has been a trusted adviser in helping organizations and programs transform to more efficiently and effectively accomplish their mission. We help our clients achieve meaningful and measurable outcomes by designing and delivering solutions in the areas of organizational effectiveness, data innovation, information technology, human capital.

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