

# A COMPARISON BETWEEN DBFM CONTRACTS AND CONCESSION CONTRACTS FOR URBAN AREA DEVELOPMENT

**FRED A.M. HOBMA, LL.M., PH.D.**

Department of Real Estate & Housing  
Delft University of Technology  
The Netherlands  
F.A.M.Hobma@TUDelft.nl

## **Abstract**

*The most integrated contract for building projects is the DBFM contract. The contractor bears responsibility for the design, building, financing, maintenance and sometimes operation of the building. DBFM-contracts are usually labelled under 'Public Private Partnerships' (PPP). According this view, PPP includes, among other contracts, DBFM contracts. However, this paper argues that from an analytical viewpoint it is incorrect to gather DBFM under the notion of Public Private Partnership. Seeing DBFM as a form of PPP does not do justice to the thought of 'partnership'.*

*Integrated contracts are well-known for building projects. Recently, interest has grown to apply integrated contracts to urban area development projects, such as the development of a residential quarter. These contracts are called concession contracts for urban area development. This paper explores the similarities and differences between DBFM contracts for building projects and concession contracts for urban area development projects. The paper identifies two 'difficult' problems that are common for DBFM and concessions. It argues that, in attempting to solve these problems, users of DBFM contracts and concessions contracts could learn from each other.*

**Keywords:** integrated contracts, DBFM, public private partnership, concession contracts, urban area development, unforeseen circumstances, flexibility, periodical assessments.

## **INTRODUCTION**

To an increasing extent clients prefer integrated contracts. Many clients are inclined to prefer integrated contracts above the so called traditional contract. Motifs of cost reduction underlie this preference. More and more clients merely want one partner as a contact point/contractor. This implies a 'change of roles': many contractors now bare the responsibility for several building process functions. The most integrated contract is the DBFM contract. The contractor bears responsibility for the design, building, financing and maintenance of the building. Sometimes the 'operation' of the building is included in the contract as well (DBFMO).

DBFM-contracts are characterised by long term obligations between client and contractor. Usually these contracts are labelled under 'Public Private Partnerships' (PPP). According this view, PPP includes, among other contracts, DBFM-contracts. However, in the first part of this paper I shall argue that, from an analytical viewpoint, it is incorrect to gather DBFM under the notion of Public Private Partnership. DBFM does not do justice to the nature of 'real' Public Private Partnership.

Integrated contracts are well-known for building projects. More recently, interest has grown to apply integrated contracts to urban area development projects, such as the development of a residential quarter. These contracts are called concession contracts for urban area development. The second part of this paper explores the similarities and differences between DBFM contracts for building projects and concession contracts for urban area development projects. It identifies two fields in which users of DBFM contracts and concessions contracts could learn from each other.

### PPP CONCESSIONS AND PPP ALIANCES

#### A definition of PPP

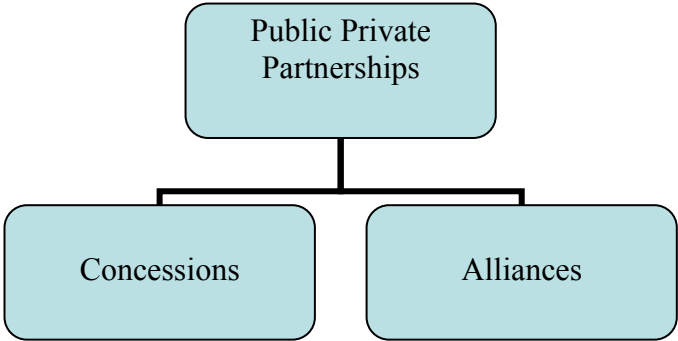
In the first part of this paper I shall explore the nature of a DBFM-contract. Furthermore, I shall examine whether it is justified or not to gather DBFM under the notion of PPP. In order to be able to do so, I start with reproducing a definition of PPP that normally is being used. Many definitions of Public PPP exist today. Bult-Spiering and Dewulf give an overview of definitions in their well-structured book *Strategic Issues in Public-Private Partnerships* (2006: 16). After considering several definitions they come to their own definition (Bult-Spiering and Dewulf, 2006: 19):

‘Co-operation between public and private parties

- at all stages of the project
- in a project-specific organization
- involving all project risks
- under contractual arrangements
- with contribution from all parties
- with added value for all parties
- with opportunities for generating cash flow’.

#### Two types of PPP

Having given their definitions Bult-Spiering and Dewulf make a division between two types of PPP: concessions and alliances.



**Figure 1:** Two types of PPP

#### Concessions

The first type of PPP is the ‘concession’. In PPP as a *concession* the public client buys a service. Here PPP is seen as a form of tender or contracting-out. The service exists from the

availability of a product for a certain time and a certain capacity. The service is obtained through granting a concession: the concession holder finances the service. The control is with the public sector: the client. The risks are for the private party. Added value in PPP as a concession lies in innovation and quality of product and process, the life-cycle approach, the transfer of risks and efficiency in terms of gain of time and cost savings.

Examples of PPP as a concession are: infrastructural projects, sewer water purification and utility buildings (Bult-Spiering e.a., 2005).

Bult-Spiering *et aliter* explain that DBFM is a form of contract that holds all the elements of the concession type of PPP. Others also argue that DBFM is one of the manifestations of PPP. For instance, in the Netherlands, a recent PPP review book explicitly nominated DBFM as a form of PPP (PPS Netwerk Nederland, 2008: 14). Thus, we can assume that DBFM is accepted as a form of PPP.

### *Alliances*

The second type of PPP is the ‘alliance’. Main characteristic of *alliances* is joint client ship and joint final responsibility (Bult-Spiering e.a., 2005). The control is in public-private hands. Public and private actors both contribute resources. Risks, profits and losses are being shared. Most examples of PPP as an alliance can be found in (inner)city development projects. PPP as an alliance can emerge because of several reasons, like (Bruil, e.a., 2004):

- Broaden the financial basis of a project (bundling of public and private capital);
- Spread risks among parties;
- Bundle know-how (for instance: public knowledge of procedures with private knowledge markets);
- Combine projects of high return on investments with projects with low return of investments;
- Combine land ownership proportions.

The form of contract that fits with alliances is not an output oriented contract like the DBFM-contract, but a ‘partnership agreement’.

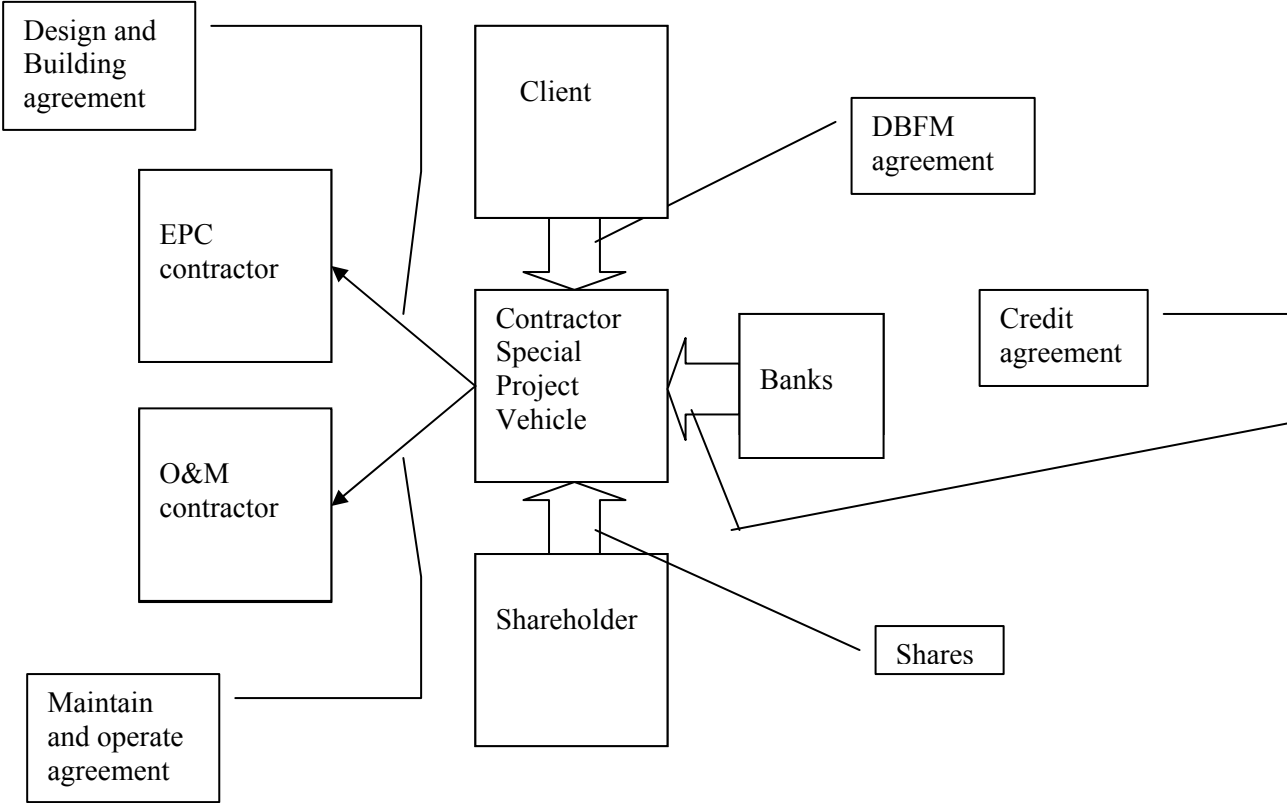
	<b>Concession</b>	<b>Alliance</b>
Division of risks	Risks are for the private party	Risks are shared by public and private parties
Type of relationship	Public client buys a service	Joint client ship
Type of contracts	Output oriented contracts	Process oriented contracts
Forms of contracts	Design Build Finance Maintain (Operate) contracts	<ul style="list-style-type: none"> <li>• Partnership agreements</li> <li>• Setting up a legal entity: Private Limited Liability Company/Limited Liability Company or Limited Partnership/Partnership under a common firm</li> </ul>

**Figure 2:** *Characteristics of concessions and alliances*

**CAN DBFM BE CONSIDERED TO BE A FORM OF PPP?**

**Elements and structure of a DBFM contract**

So far we have seen that PPP is a broad concept that comprises to types: concessions and alliances. Furthermore, DBFM contracts perfectly fit within the concession type of PPP. I now continue to explore the elements of a DBFM-contract. Figure 3 below shows the elements and structure of a ‘common’ DBFM contract. I completely took this figure from an excellent article by Van Wassenauer in Tijdschrift voor Bouwrecht (Van Wassenauer, 2009).



*Figure 3: Elements and structure of a DBFM contract. Source: Van Wassenauer, 2009.*

Van Wassenauer explains: EPC stands for Engineering Procurement and Construct. That means that this contractor carries out all design and building activities for a fixed price and with the same risk division as laid down in the DBFM agreement. O&M stands for Operation & Maintenance. This is the party that after the ‘delivery’ of the project, during the rest of the duration of the DBFM agreement, runs the built ‘asset’ and actually is responsible for the availability (Van Wassenauer, 2009).

## **Real PPP**

In my opinion, the concession type of PPP, and with that DBFM contracts, should not be rated as Public Private *Partnerships*. The characteristics of concessions (figure 2) and the structure of DBFM contracts (figure 3) explained above, show that they are focussed on procurement and not on cooperation or partnership. What are parties really doing *together* in concessions? Often parties precisely stand *opposite* each other. The core of concessions/DBFM is a client - contractor relationship between parties. Nevertheless, as shown above, the literature labels concessions/DBFM under Public Private Partnerships. The argument for it is the long relationship between client and contractor, often 20 to 30 years. In itself I do not find this to be a strong argument.

In my view, we should reserve the term PPP for alliances. An alliance is a joint venture. It is not about *dividing* responsibilities and risks, but about *sharing* responsibilities and risks. In a sense it is *real* partnership (Koppenjan en Van Ham, 2002). Or, as Bult-Spiering and Dewulf put it: 'The emphasis in joint venture PPPs is on togetherness or sharing, while concessions are about transfer of risks and revenues' (2006: 18). The thought of 'partnership' is expressed through alliances, not through concessions like DBFM. My conclusion, therefore, is that DBFM cannot be considered to be a form of 'real' Public Private Partnership.

Alliances/joint ventures are, for that matter, not only possible with urban area developments, but also with buildings. With buildings, they are commonly known as 'project alliances' (Koolwijk en Geraedts, 2006). This is a matter of 'true' partnership. Concessions/DBFM should not be considered PPP. In my opinion we could better stick to the term 'integrated contracts' for this type of agreements. Integrated contracts include, as far as I am concerned, all contracts with integration of building process functions. So from Design and Build through contracts in which finance plays the leading role (DBFM).

## **CONCESSION CONTRACTS FOR URBAN AREA DEVELOPMENT**

I now come to the second part of this paper. In this part I shall bring forwards the usefulness of comparing DBFM with concession contracts for urban area development.

Recently, in the Netherlands, interest has grown to apply integrated contracts to urban area development projects, such as the development of a residential quarter. These contracts are called concession contracts for urban area development. The contracts show similarities with DBFM contracts, although, of course, the scale is different.

A concession for urban area (re)development is a contract closed between a local authority and a property developer. It is a temporary cooperation. It has a clear financial agreement beforehand. It has an intentional shift (transfer) of risks, revenues and accountabilities towards a private party. The private party takes care of the development of plans, the preparation, realisation and if desired the management and operation of the whole area. In doing so, the private party is bound by preconditions set by the local authority, which are accepted by the private developer. Limited by the preconditions, the property developer can optimise his plan for the area that is to be developed.

Concession contracts in urban area development aim at an effective and efficient division of roles and tasks and a clear division between public and private sectors accountabilities. The control by the public sector (local authorities) is limited to a periodical assessment/inspection/checking of the services delivered or performance agreement.

As far as land ownership is concerned, two possibilities exist. The private developer can have ownership beforehand of all the land in the plan area (by having it acquired from previous owners). Or the land can be sold by the local authority to the private developer.

	<b>DBFM contracts</b>	<b>Concession contracts for urban area development</b>
Risk transfer	Risk transfer to contractor	Risk transfer to property developer
Client	(Usually) national government	Local authorities
Type of project	Infrastructure, buildings	Urban areas
Financing	By contractor (Special Project Vehicle)	By property developer
Optimisation	Design – Build –Maintain	<ul style="list-style-type: none"> <li>• Density, house prices, ratio built-unbuilt</li> <li>• Land development – property development</li> </ul>
Assessment/inspection by client	In between	In between
Payment	Periodical payment by client from the moment the infrastructure/building/service is delivered	Payment beforehand <ul style="list-style-type: none"> <li>• Developer pays local authority (l.a.) in case much land is transferred from l.a. to developer.</li> <li>• Or l.a. pays developer in case of anticipated operation deficit (polluted area etc.)</li> </ul>
Specifications	Output specifications in advance laid down by client	Preconditions (rough visual quality, exact quality requirements for public space, program in headlines, urban planning conditions) laid down by local authority

**Figure 4:** Characteristics of DBFM contracts and concession contract for urban area development

Figure 4 shows the similarities between DBFM contracts and concession contract for urban area development. Both types of contracts share the same philosophy, which we can summarise as follows: a clear division of public and private sectors. The basic assumption underlying both contracts is that each party does what he does best: the public sector sets preconditions and the private sector fulfils the role of entrepreneur.

For the Netherlands, concession contracts for urban area development are rather new. The vast majority of urban development has taken place with different types of contract, most

notably joint ventures. In these joint ventures the local authority and the private property developer share the risks of land development of the area that is to be developed. That is, among other things, the costs of (a) acquiring land, (b) demolition of structures, (c) the clean up of polluted land and (d) preparing the land for construction are shared by public and private sectors. The concession contracts for urban area development however transfer the risk of land development towards the property developer. Of course, in concession contracts for urban area development not only risks and costs are transferred to the private sector; the revenues also accrue to the property developer.

## SUGGESTIONS FOR MUTUAL LEARNING

### **Difficult problems experienced in DBFM and in concession contracts**

Now that we have seen that DBFM contracts (for infrastructure and buildings) and concession contracts (for urban areas) share the same philosophy and basic assumptions, it is conceivable that both contract types can learn from each other. After all, both types of contract experience 'difficult problems'. Two typical problems users of both DBFM contracts and concession contracts for urban area development experience are:

- Unforeseen circumstances and flexibility
- Periodical assessment/inspection/checking

It is logical that *unforeseen circumstances* are an important issue in long term contracts like DBFM and concessions for urban area development. After all, during the duration of the contract it is very well possible that what was assumed at the beginning of the contract did not realise in the way parties expected. The deviation of the expectations can occur on the side of the client/local authority and or the side of the contractor/developer. The deviation of expectations can lead to a wish for changes. These are changes regarding the realised building/infrastructure or changes regarding the realisation of the urban area. The proposed changes, sought after by one of the parties, usually deviates from the contractual agreements. Easily questions can arise such as: under which circumstances is it reasonable that the other party agrees with the wish to change the building or development of the area? How is the price assessed that has to be paid for the changes?

The second problem often occurring in DBFM and concession contracts alike refers to the *periodical assessments* by the client/local authority. These are periodical assessments during the construction of the building or the development of the area in order to check if the contractor/developer fulfils his tasks in agreement with the contract. Sometimes specific 'products' of the contractor/developer need approval by the client/local authority.

Contractors and developers often are unsatisfied with the assessments carried out by the client or local authority respectively. More than often they feel that the client/local authority goes much further in its assessment than is reasonable. For instance, in urban area development many developers feel that the civil servants very critically judge the designs from the developer, going much further than 'merely' checking whether the design remains within the preconditions. Related to this is another problem: sometimes assessments are executed by civil servants who are not fully aware of the contract and their specific role as a civil servant under this contract. Their specific role is checking whether the offered designs etcetera remain within the preconditions; their role is not – if the design remains within the preconditions – to force adjustments. Yet another problem is that assessments may take too much time, thus causing problems for the contractor/developer.

## **Mutual learning**

The problems described above give rise to the question: can users of DBFM contracts and of concession contracts for urban area development learn from each other in order to avoid or alleviate these problems? Most likely they can.

### *Unforeseen circumstances/flexibility*

Take the problem of unforeseen circumstances and flexibility. It is common that DBFM contracts hold specific regulations concerning unforeseen circumstances/flexibility. These regulations usually lay down (Koster et al., 2008: 28):

- a distinction between two sorts of proposals for changes: minor and major changes, with major changes following a specific procedure
- who is authorised to propose changes of the contract
- information that has to be provided for a proposal to change
- legitimate grounds to refuse a proposal for change
- financial consequences of a proposal for change; which financial settlement system is applied?

The regulations for unforeseen circumstances/flexibility in DBFM contracts appear to be much more developed than in concession contracts for urban area development. Most concession contracts for urban area development hold a confined regulation for unforeseen circumstances/flexibility. Usually it is limited to the provision that in case of unforeseen circumstances parties agree to enter into (re)negotiations. It seems that concession contracts for urban area development can learn from DBFM contracts in this respect.

### *Periodical assessment*

The other way round the users of DBFM contract could learn from concession contracts for urban area development regarding periodical assessments. The fact is that some – but my no means all – concession contracts for urban area development in England hold effective provisions for periodical assessment/inspection/checking by the local authority. These provisions include that the assessment must be rounded of within a certain time limit. Furthermore the provisions prescribe that the assessment is exclusively done by civil servants having adequate knowledge of the specifics of the contract. These civil servants are aware of the fact that their role is limited to checking whether the designs etcetera of the property developer remain within the preconditions that have agreed on – and not forcing the developer to extra adjustments. These and other provisions of concession contracts for urban area development could be of help to DBFM contracts.

In this second part of my paper I hope to have demonstrated that (a) DBFM contracts and concession contracts for urban area development have much in common and (b) it is worth the effort to compare both types of contract in order to learn from each other.

## **CONCLUSIONS**

In the first part of this paper the elements and structure of a DBFM contract were examined. DBFM was compared with alliances/joint ventures. DBFM as well as alliances/joint ventures are seen as forms of Public Private Partnerships. I argued that DBFM cannot be seen as a partnership. There is no real partnership idea behind this type of contracts. In my opinion we

could better stick to the term 'integrated contracts' for this type of agreements. I propose we reserve the notion PPP for alliances/joint ventures. They express the real partnership idea by *sharing* responsibilities and risks instead of *dividing* them, such as in DBFM contracts.

In the second part of this paper I pointed out that DBFM contracts (for infrastructure and buildings) and concession contracts (for urban areas) share the same philosophy and basic assumptions. This allows for a useful comparison between both types of contract in order to let users learn from each other.

DBFM contracts and concession contracts for urban area development in practice both are confronted with difficult problems. It can be fruitful for users of DBFM contracts to learn from ways in which users of concession contracts for urban area development successfully addressed a certain problem. This goes, the other way around, for concession contracts for urban area development. I suggested two fields in which both contract types can learn from each other. These are: unforeseen circumstances/flexibility and periodical assessments. It seems promising to compare these fields and others as well!

## LITERATURE

Bruil, I., Hobma, F., Peek, G.J. en Wigmans, G. (eds), *Integrale gebiedsontwikkeling; het stationsgebied 's-Hertogenbosch*, SUN, Amsterdam, The Netherlands, 2004.

Bult-Spiering, M., Blanken, A. and Dewulf, G., *Handboek publiek-private samenwerking* Lemma BV, Utrecht, The Netherlands, 2005.

Bult-Spiering, M. and G. Dewulf, *Strategic Issues in Public-Private Partnerships; An international perspective*, Blackwell, Oxford, 2006.

Koppenjan, J. en Van Ham, H., Introductie: de moeizame totstandkoming van publiek-private samenwerking. In: Van Ham, H. en Koppenjan, J. (eds.), *Publiek-private samenwerking bij transportinfrastructuur*, Lemma BV, Utrecht, The Netherlands, 2002.

Koolwijk, J.S.J. en R.P. Geraedts, *Projectalliantie. Procesinnovatie bij complexe bouwprojecten*. VSSD, Delft, 2006.

Koster, J.J.W. et aliter, *DBFM Handboek; een verkenning van contractonderdelen*, Ministerie van Financiën, Den Haag, The Netherlands, 2008.

PPS Netwerk Nederland, *PPS: van belofte naar realisatie*, PPS Netwerk Nederland, Zeist, The Netherlands, 2008.

Wassenaer, A.G.J. van, PPS-projecten en de kredietcrisis: reddingsvesten aan, *Tijdschrift voor Bouwrecht*, nr. 3. maart 2009.