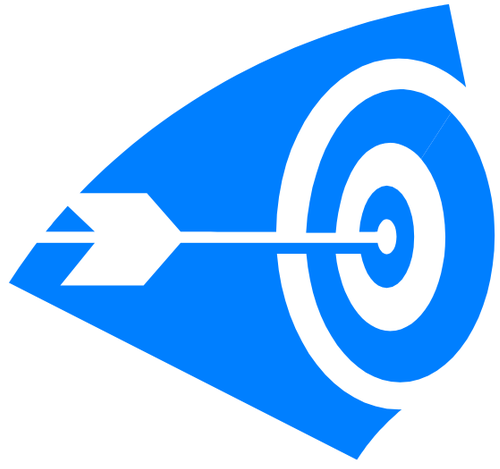
Course: e-Governance Project Lifecycle

Day 3 : Session 1

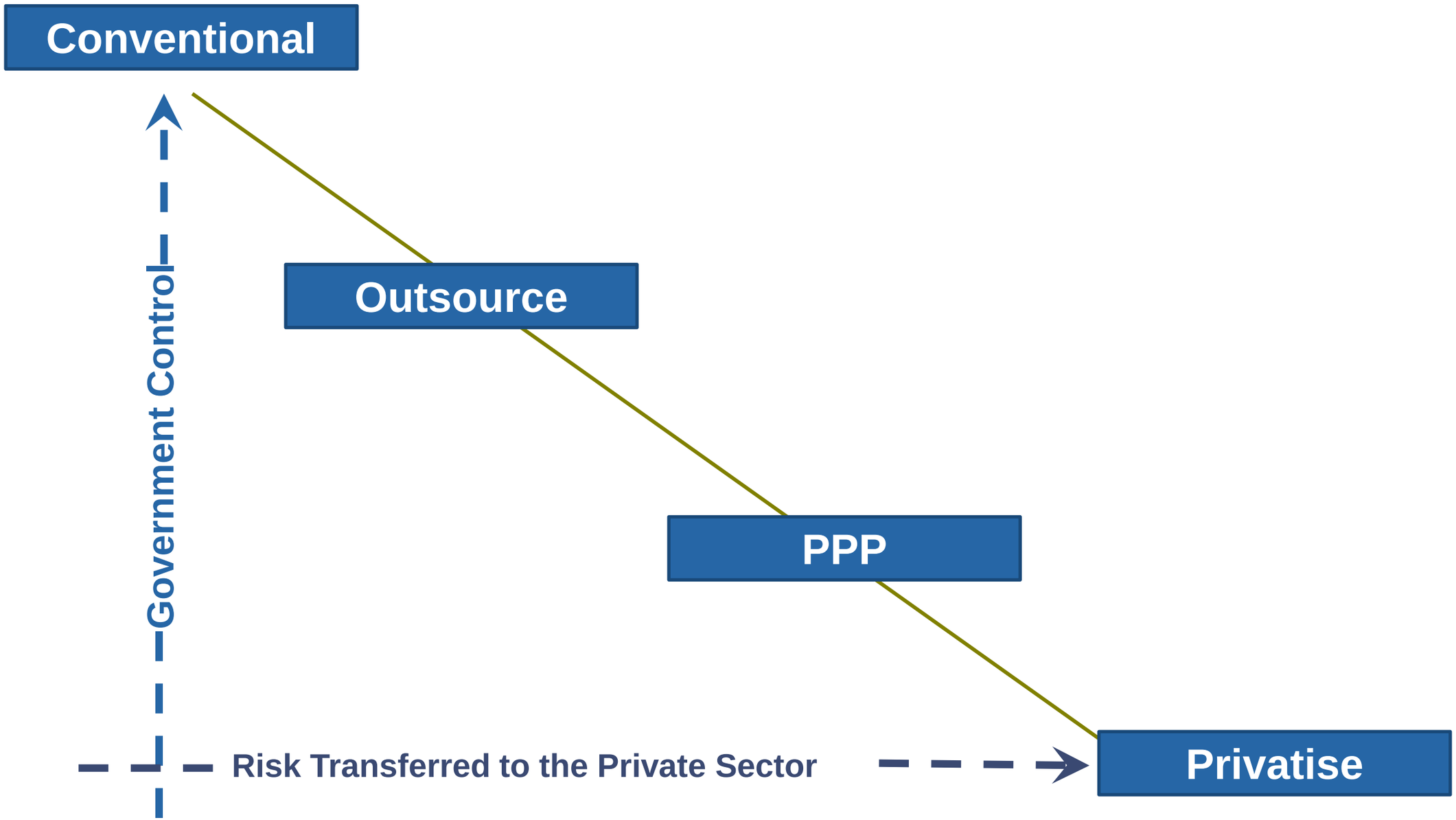
Introduction to Public Private Partnerships (PPP)

Agenda



- Introduction to PPP
- Rationality for a PPP
- Introduction to PPP models
- Structuring considerations in a PPP
- Pre- feasibility and feasibility analysis: Financial, economic, technical and Political
- Risks and challenges in PPP

Various Models for Private Sector Participation



Defining Public Private Partnerships

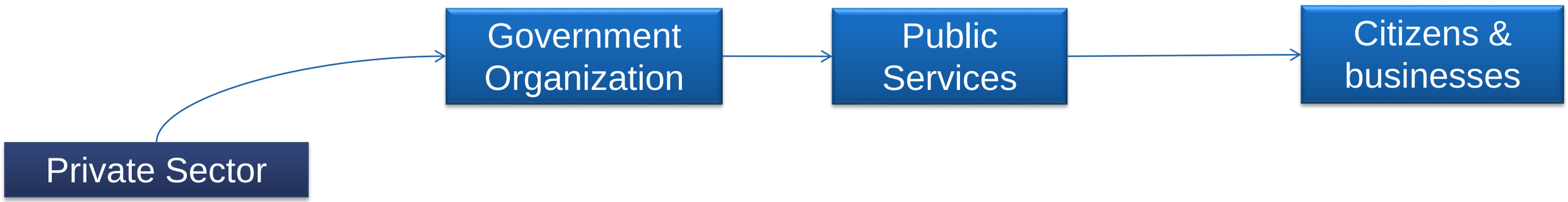
A public private partnership or PPP involves:

- government and private sectors working together to deliver infrastructure or services that are traditionally provided by government
- private financing, implementation and management of key infrastructure and with the primary objective of improving public services

PPP is a generic term for the relationships which are formed between public bodies and the private sector with the aim of introducing private sector resources and/or expertise to provide and deliver public sector assets and services.

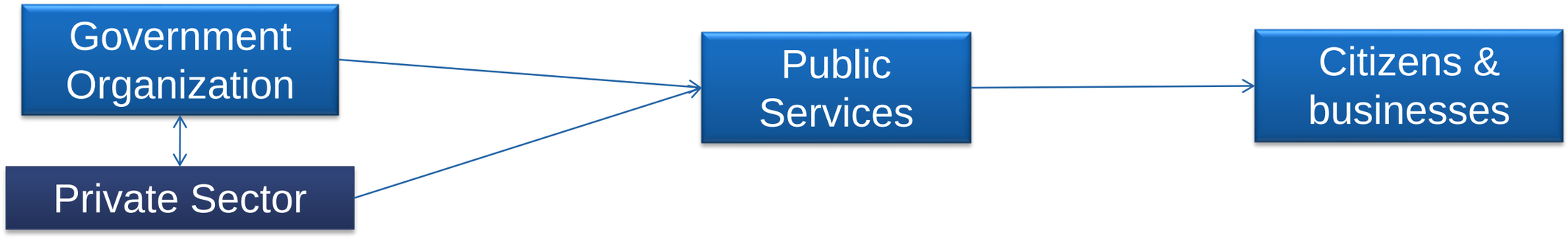
Defining Public Private Partnerships

Traditional Model of Public Service Delivery



Private sector was supporting the government in delivery of public services to citizens…

Shift in Public Service Delivery



Private sector is participating in public services delivery to citizens…

PPP Basics

PPPs are concerned with services, not assets

- The government does not need to own infrastructure to deliver services
- PPPs are a procurement option, not a novel method of developing public infrastructure
- PPP policy sits alongside other procurement methods – ie conventional, outsourcing, leasing etc.
- Suitable to some public projects, not all projects
- PPPs are not “new money”
- Service outputs must be paid for, whether directly (eg user charges) or by appropriation
- Must therefore be affordable – either to users (user charges) or to the Budget

PPP Basics (contd..)

- The government retains political responsibility/accountability to deliver services for the community;
- The government defines the timeframe in which the services must be delivered; and the quality and quantity of services needed;
- The private sector delivers the services and finances or part finances the project;
- Private sector remunerated through services charges/transaction fees/gap funding..
- A mid/ short-term relationship is established, typically(in e governance) between 3 to 5 years, depending on the nature of the facilities, assets or services to be delivered;
- The different functions of system design, development, maintenance and operation are integrated to release the synergies between them and discourage low-capital/high-operating expenditure solutions;
- Risks are allocated between the public and private sectors;
- There is an emphasis on output-based specifications;

PPP - Basics

What distinguishes PPP ?

- Sharing of risk
  - Private party bears significant financial, technical and operating risk
  - Promise of a sustained service
  - Financial rewards to private sector linked with output
- Capital investment and capacity building
  - Significant private capital deployed for citizen services or use of already developed capabilities
  - Building capacities for servicing at a faster pace
- Joint ownership
  - Well defined roles and responsibilities
  - Clarity in ownerships and other terms
  - Full control by Government over key data
  - Concessions and Guarantees from and to the Government

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The principle of risk transfer is fundamental for all PPP type transactions

What does this mean?

Typical Project Risks

- Land acquisition, planning and permissions
- Design
- Construction
- Commissioning
- Latent defects
- Operating performance
- Operating and maintenance costs
- Third party revenue
- Demand (volume)
- Residual value
- Inflation
- Regulatory
- Taxation
- Force Majeure
- Changes in requirement

Risk Allocation

- Key considerations for risk allocation:
  - Who is best placed to reduce the probability of risk occurring?
  - Who is best placed to manage the cost of risk if it does occur?

Minimising the expected cost of risk is crucial for maximising returns

Risks should be allocated to the party best able to understand and manage them..

Risk Allocation

Risks should be allocated to the party best able to understand and manage them..

- Land acquisition, planning/permissions
- Demand risk (?)
- Changes in requirements
- Latent defects (existing)

- Inflation
- Regulatory
- Taxation
- Force majeure

- Design and construction
- Commissioning
- Operating and maintenance costs
- Operating performance
- Latent defects (new)
- Third party revenue

What Should Private Partnership Bring?

- **Real financial benefit** and a better utilisation and allocation of public funds;

- **Development of efficient public infrastructures/projects** in shorter terms than otherwise;

- **Ensure** of good quality public services;

- **Economic growth** and boosted direct investment by private sector

- **Efficient control** over the formation of long-term private sector liabilities;

Role of Government in PPP

- Set policy, identify opportunities, and define objectives;
- Decide amongst competing priorities for public resources;
- Ensure transparency and probity in the procurement process;
- Identify needs in terms of output specifications that encourage flexibility and innovation in the manner of performance;
- Set and ensure the achievement of standards;
- Establish, monitor and enforce the levels of service;
- Ensure value for money is achieved;
- Determine and manage reward mechanisms and tariff structures;
- Identify and propose the allocation of risks;
- Provide a clear regulatory framework and perform regulatory functions; and
- Safeguard the interests of customers and the general public.

Role of the private parties

- Achieve defined levels of performance in service delivery;
- Provide expertise and innovation;
- Provide access to private financing, as appropriate; and
- Provide a sufficient return to investors and other stakeholders.

- Do not take the responsibility of risks which cannot be managed by the private sector
- Understand the contractual terms comprehensively as the government contracts are rigid.

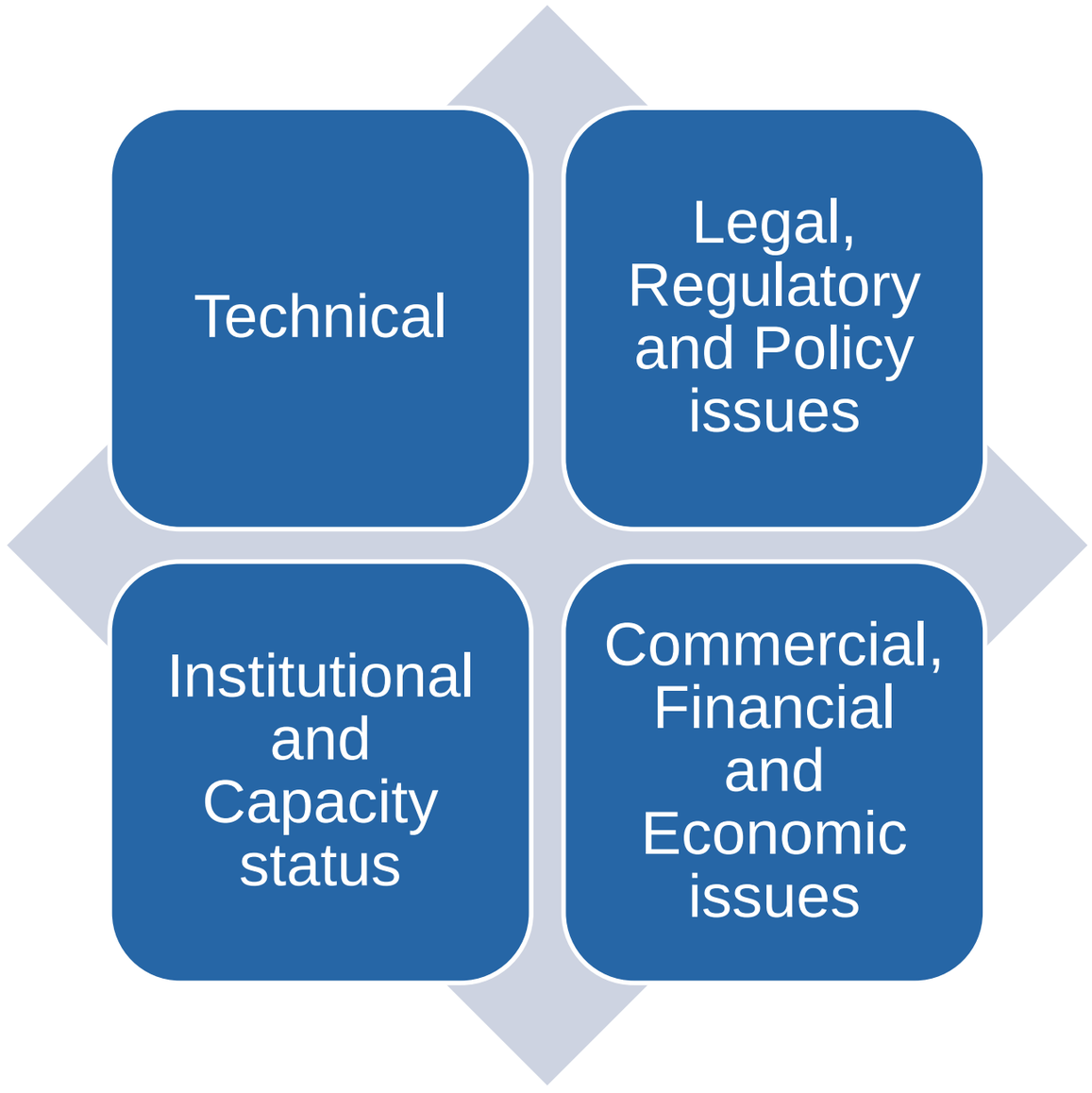
Benefits of PPP

- Allowing the government to concentrate on its core activities
- Allocation of Risk and Responsibility where it can be best managed
- Unity of responsibility leading to improved delivery of public services
- Reduced lifecycle costs of a project;
- Quantifying more accurately the costs of service delivery;
- Reduced risk of cost overruns;
- Increased revenues;
- Maintaining an efficient government and a lean civil service;
- Spreading the government’s capital works expenditure over the life of a project;
- Invoking private sector skills, experience, access to technology, and innovation;

PPP is now Omnipresent

Power	Water	Hospitals	Schools (Grants in Aid)
Stadiums	Air ports	Information technology	Housing
Roads	Tourism	Ports	Citizen interface

Diagnostics for a PPP



Technical Issues

- Present delivery system
- Proposed delivery model
- Defining and documenting the desired outcomes
- Identifying differentiating factors in each of the components of a project
- Procurement plan for each of the components
- Defining the metrics for performance measurement

Legal Regulatory and Policy Frameworks

- Understanding of regulatory bodies, regulations;
- Major sector institutions and government entities related to the sector;
- User charges and subsidy policies and arrangements;
- Existence and applicability of legally mandated service quality standards;
- Environmental and health regulations;
- Relevant labor laws and regulations
- Arbitration frame works
- Audit of performance standards and service level agreements

Institutional Structures and Capacity

- Institutional and legislative frameworks to support the business model
- Capacity to match the role and responsibilities of stake holders
- Institutional structure to delegate the responsibilities to private sector
- Alignment of risk and reward with the ability to manage the risk by a stake holder
- Capacity to monitor the performance and service lvel agreements

Commercial, Financial and Economic issues

Commercial

- Suitability of the business model
- Funding arrangements
- Win-win strategy
- Commercial viability to the private sector

Financial

- Design of realistic pricing of user charges
- Social responsibility of the government
- Need for subsidy and viability gap funding
- Business case analysis

Economic

- Cost –benefit analysis
- Benefits analysis in qualitative terms

PPP: Basic Options

Service Contracts	Management Contracts	Lease Contracts
BOO/ BOOT..	Concessions	Joint Ventures

Service Contracts

- Similar to the Outsourcing model discussed in the previous session
- Government maintains complete control on the project creation, execution and assets
- Government funds the project investments for the capital and operational expenditure during the project tenure
- Government leverages private sector strengths for creation of the project or maintenance of the project or both
- Risks are allocated to the government and private sector based on the responsibilities (e.g. government will have the risk of project demand, the private sector will carry the risk of performance and quality of the services delivered to the government)
- Does not attract capital investment
- No deeper impact on the services delivery

Management Contracts

- Similar to the Outsourcing model discussed in the previous session
- Contractual arrangement for the management of a part or whole of a public enterprise by the private sector
- Allows private sector skills to be brought into service design and delivery, operational control, labour management and equipment procurement.
- Public sector retains the ownership of facility and equipment.
- The private sector is provided specified responsibilities concerning a service and is generally not asked to assume commercial risk.
- The private contractor is paid a fee to manage and operate services.
- Normally, payment of such fees is performance-based
- But longer period may be used for large and complex operational facilities such as a port or airport.

Lease Contracts

- Assets are owned by the public sector
- operator takes lease of both infrastructure and equipment from the government for an agreed period of time
- government maintains the responsibility for investment and thus bears investment risks
- The operational risks are transferred to the operator
- Fixed facilities and land are leased out for a longer period than for mobile assets.
- Private sector is responsible for the service delivery
- Under a lease, the operator retains revenue collected from customers/users of the facility and makes a specified lease fee payment to the contracting authority
- Under an affermage, the operator and the contracting authority share revenue from customers/users

Concessions

- In this form of PPP, the Government defines and grants specific rights to an entity (usually a private company) to build and operate a facility for a fixed period of time
- Private sector is the concessionaire
- The Government may retain the ultimate ownership of the facility and/or right to supply the services
- In concessions, payments can take place both ways:
    - concessionaire pays to government for the concession rights
    - government may also pay the concessionaire, if necessary to make projects commercially viable and/or reduce the level of commercial risk taken by the private sector,
- Private sector invests in project design, construction, implementation and operations based on the concessions provided by the public sector
- Revenues from the project are accrued to the private sector and private sector pays for concession rights to the public sector (if agreed).

BOT (Build Operate and Transfer)

- A concession type of arrangement
- Private sector is the concessionaire
- Similar to ‘Project Finance’ model discussed in the previous session
- BOT is a common form of PPP in all sectors in Asian countries. A large number of BOT port and road projects have been implemented in the region.
- the concessionaire undertakes investments and operates the facility for a fixed period of time after which the ownership reverts back to the public sector
- operating and investment risks can be substantially transferred to the concessionaire
- By retaining ultimate ownership, the government controls policy and can allocate risks to those parties best suited to bear them or remove them
- Other variants of this model include BTO (Build Transfer Operate), Build Lease Transfer (BLT)…

BOO (Build Own Operate)

- This model refers to private ownership of assets or privatisation of the services
- The Government grants licenses to private undertakings to provide services such as fixed line and mobile telephony, Internet service, television and radio broadcast, public transport, and catering services on the railways.
- licensing may also be considered as a form of “concession” with private ownership of assets.
- private sector remains responsible for design, construction and operation of the project/facility
- in some cases the public sector may relinquish the right of ownership of assets to the private sector
- This is the most common form of private participation in the power sector in many countries

BOO(T) (Build Own Operate Transfer)

- The government retains political responsibility/accountability to deliver services for the community;
- The government defines the timeframe in which the services must be delivered; and the quality and quantity of services needed;
- Private entity receives concession from government to finance, design, construct, implement and operate the project
- Private sector is remunerated through services charges/transaction fees/gap funding..
- The assets of the project are transferred to the government at the end of the concession period

BOT types

	Own	Design	Build	O&M
Design-Build	Public	Private	Private	Public
Build-Operate-Transfer	Public	Private	Private	Private/public
Design-Build-Finance-Operate	Public	Private	Private	Private
Build-Own-Operate	Private	Private	Private	Private
Build-Own-Operate-Transfer	Private [Public after Transfer]	Private	Private	Private

Comparing the Options

Option	Asset Ownership	Operations & Maintenance	Capital Investment	Commercial Risk	Contract Duration	Compensation terms
Service Contract	Public	Public & Private	Public	Public	1-2 years	Unit prices
Management Contract	Public	Private	Public	Public	3-5 years	Fixed fee liked to SLAs
Lease	Public	Private	Public	Shared	8-15 years	Fixed/Sharing of Revenues
Concession	Public	Private	Private	Private	Varies on the project: generally long term	All or part of user charges
BOT/BOO	Private/ Public	Private	Private	Private	Varies on the project	All or part of user charges
Joint Venture	Private /Public	Public & Private	Public & Private	Private	Indefinite	Revenue sharing

PPP Options and the prerequisites

Option	Political commitment	Recovery through user charges	Regulation requirement	Capacity requirement for contracting
Service Contract	Low	Low	Low	Moderate
Management Contract	Moderate	Moderate	Moderate	Moderate
Lease	Moderate	High	High	High
Concession	High	High	High	High
BOT Variations	High	Variable	High	High

End of Session