INTRODUCTION TO PUBLIC PRIVATE PARTNERSHIPS

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Outline

- Review Lecture 8
- Private Public Partnerships
- Different PPP Models
- Public-Private Partnership Models
- Main characteristics of PPPs
- Risk Analysis
- Competition and Regulation in PPPs

Definition of PPP

- Public private partnerships (PPPs) are **AGREEMENTS BETWEEN GOVERNMENT AND THE PRIVATE SECTOR** for the purpose of providing public infrastructure, community facilities and related services.

- The private sector enter into a contract with government for the design, delivery, and operation of the facility or infrastructure and the services provided.

- The private sector finance the capital investment and recover the investment over the course of the contract.

- The asset transfers back to the public sector at the end of the contract

Why use PPPs?

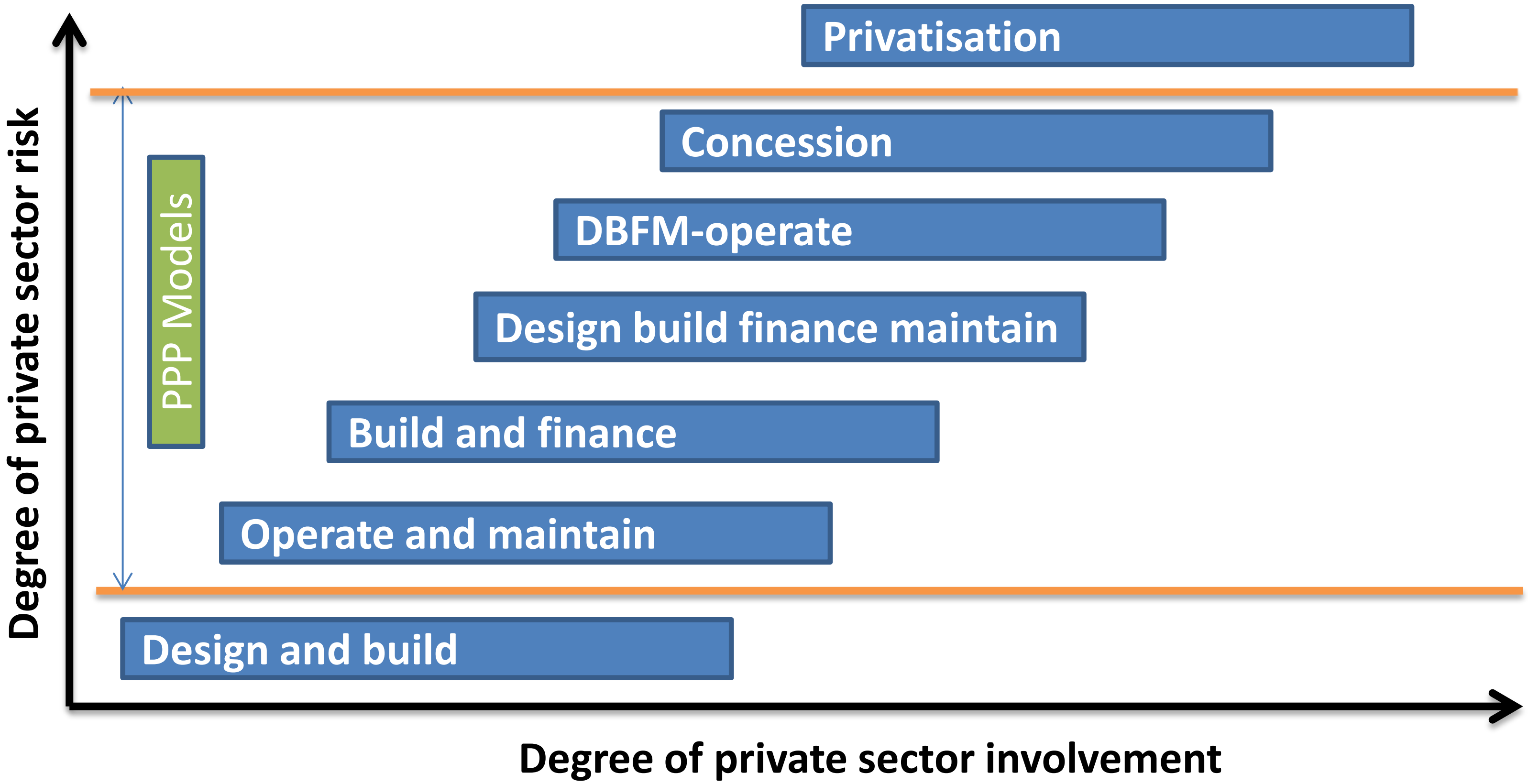
- Focus on outputs
- PPPs make projects affordable
- Better value for money over the lifetime of the project
- More efficiency in procurement
- Faster project delivery with more projects in a defined timeframe
- Risks are allocated to the party best able to manage the risk

Why use PPPs? (2)

- Deliver certainty of budget and outcomes
- Better asset utilisation and social and economic benefits
- Sustainable development and improved regulation
- Public sector only pay when services are delivered
- Injection of private sector capital

Range of PPPs

- Adapted from Canadian Council PPP 2009



Public-Private Partnership Models

- **Design-Build-Operate (DBO):** Under this model, the private sector designs and builds a facility. Once the facility is completed, the title for the new facility is transferred to the public sector, while the private sector operates the facility for a specified period. This procurement model is **also referred to as Build-Transfer-Operate (BTO).**

Public-Private Partnership Models (Cont.)

- **Build-Own-Operate-Transfer (BOOT):** The government grants a franchise to a private partner to finance, design, build and operate a facility for a specific period of time. Ownership of the facility is transferred back to the public sector at the end of that period.

- **Build-Own-Operate (BOO):** The government grants the right to finance, design, build, operate and maintain a project to a private entity, which retains ownership of the project. The private entity is not required to transfer the facility back to the government.

BOT Project Type	Characteristics
Build Own Operate Transfer (BOOT)	• The service provider is responsible for design and construction, finance, operations, maintenance and commercial risks associated with the project. • The service provider owns the project throughout the concession period • The asset is transferred back to the government at the end of the term, often at no cost.

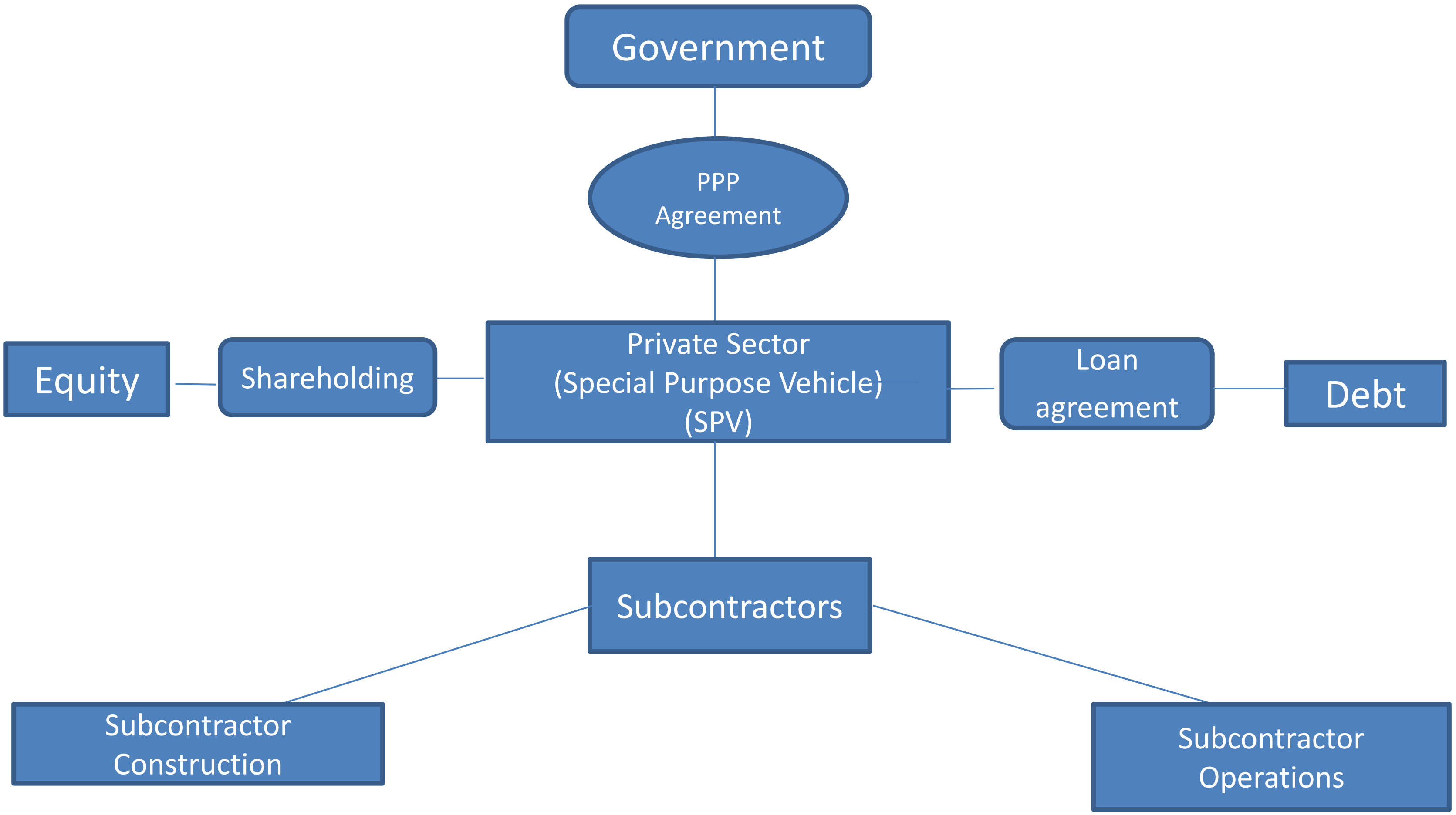
Build Own Operate (BOO)	• Similar to BOOT projects, but the service provider retains ownership of the asset in perpetuity. • The government only agrees to purchase the services produced for a fixed length of time

Design Build Operate (DBO)	• A design and construction contract linked to an operation and maintenance contract. • The service provider is usually responsible for financing the project during construction. • The government purchases the asset from the developer for a pre-agreed price prior to (or immediately after) commissioning and takes all ownership risks from that time.
Lease Own Operate (LOO)	• Similar to a BOO project but an existing asset is leased from the government for a specified time. • The asset may require refurbishment or expansion.

Principles of PPPs

Output based specification	• Contracting Authority defines the service required • Design of the works to deliver that service lies with the private sector
Long-term contractual arrangements	• The contract can be for 25/30 years plus
Value for money	• Cost measured against conventional procurement. • Whole life costs and quality are combined to gauge VFM
Transfer of risk	• Transfer of design and construction risk • Risk of ownership transferred to the private sector
Market competition	• Competition will drive best value • Gives public sector access to innovation
Whole life costing	• Long term responsibility for building operation and maintenance • Focus on reducing cost

Typical SPV structure for PPPs



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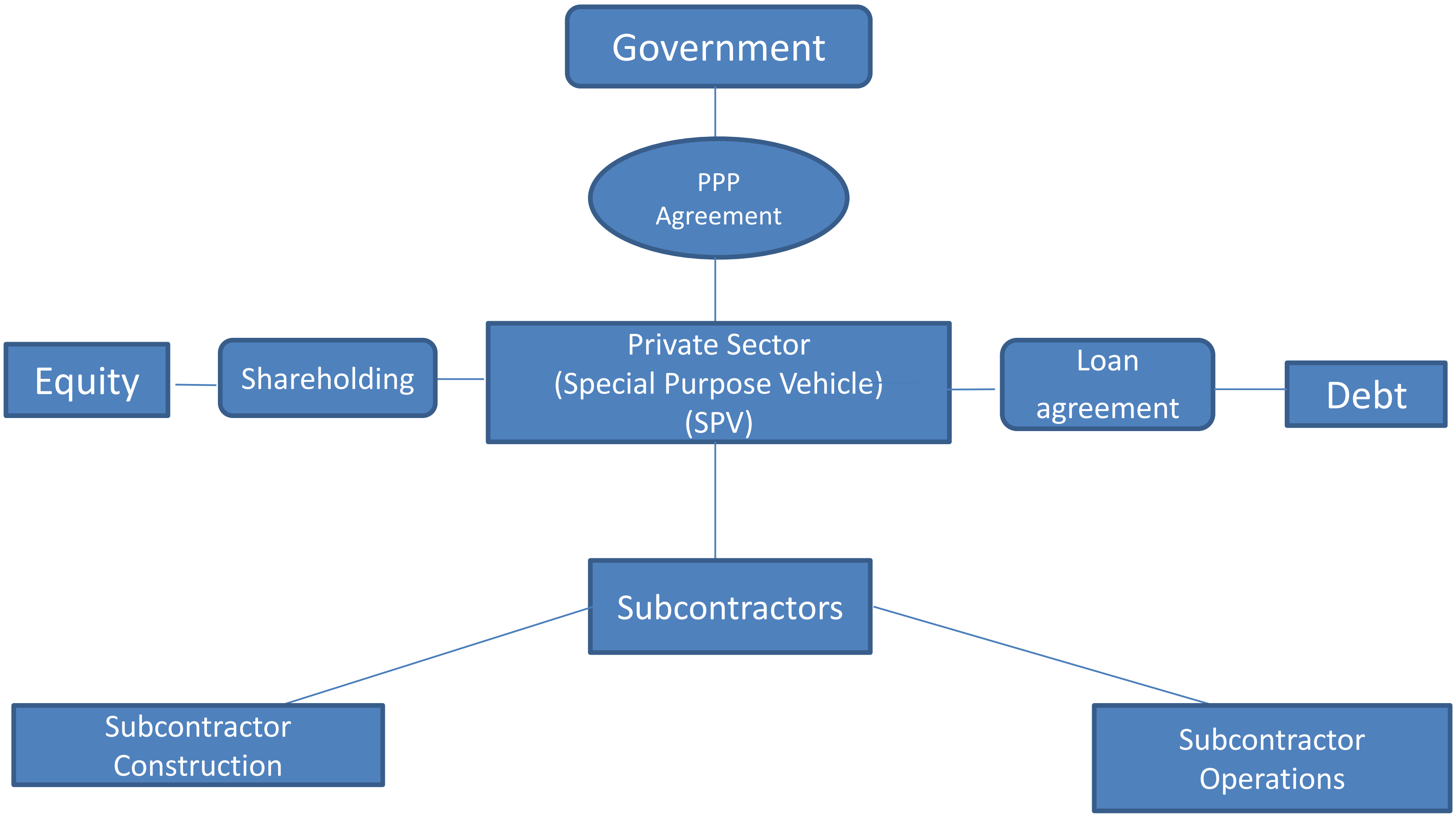
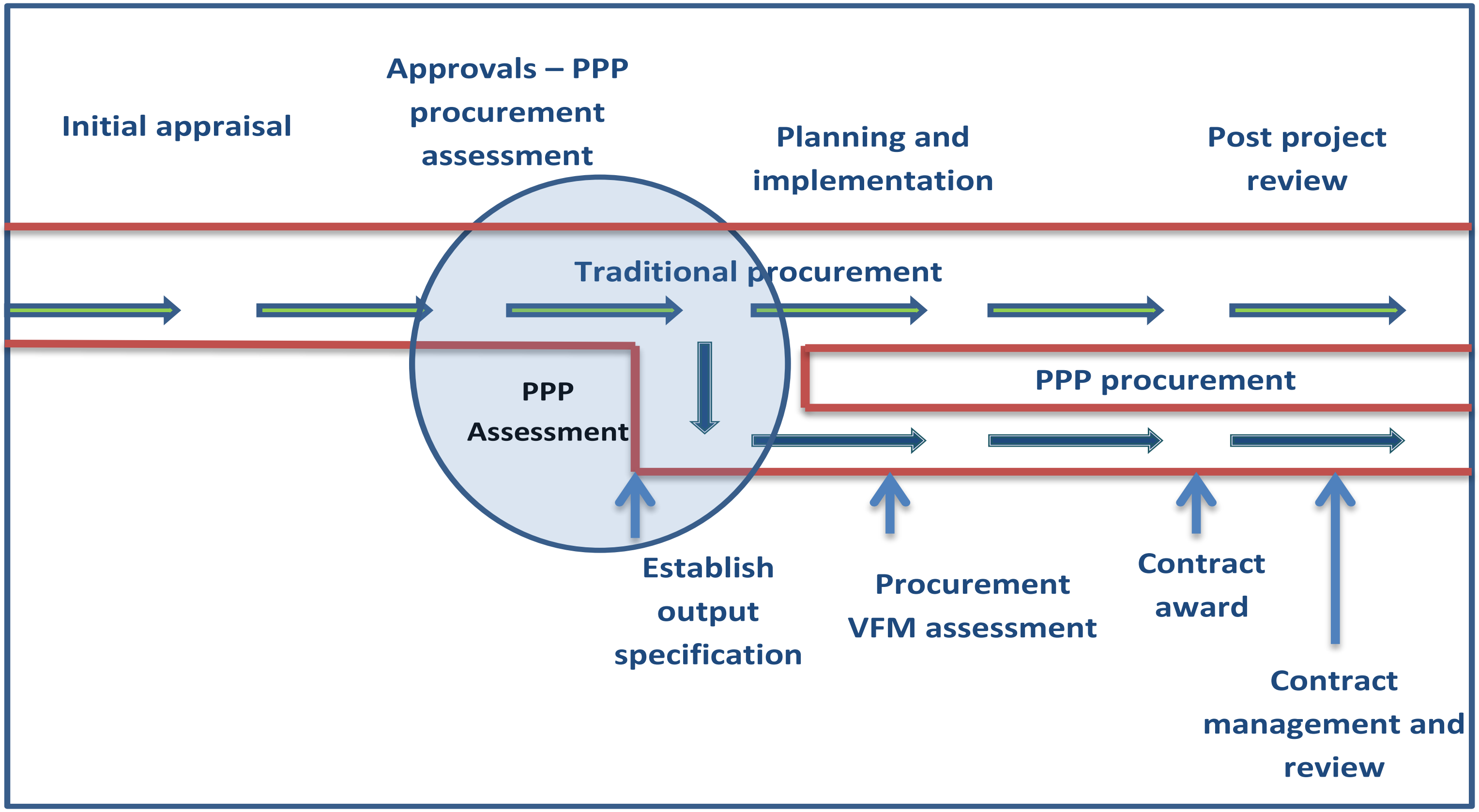


PPP and Traditional Procurement



Main characteristics of PPPs

- Main characteristics of PPPs are:
  1. Private sector is given responsibilities for one or more of the following tasks:
     i. Defining and designing the project
     ii. Financing the capital costs of the project
     iii. Building the capital physical assets (road, bridge)
     iv. Operating and maintaining the assets in order to deliver the product/service
     v. Significant risks is transferred from the government to private sector

  2. Allocation of the financing task, private financing.

Public Private Partnerships (PPPs)

Why PPPs have become an alternative to traditional methods for the provision of public services?

1. Private sector firms compete to do project (*Ex ante* Competition)
   - Competition at the bidding stage/*ex ante*.

2. Scarce/rare Skills
   - Private sector has skills not available in the public sector
   - Allocate certain tasks to a private partner who has the skills and also the incentive to reform at a high level

3. Poor Labor Relations
   - Private sector through the forces of competition may offer a skilled, efficient and flexible labor force.

Public Private Partnerships (PPPs)

4. Innovation
   - Some parts of the project may need new approaches and innovative thinking

5. Risk
   - Major risk can be managed better by private sector (ex. construction-delay risk, being contractor and operator give incentive to minimize such risk)

6. Economies of scale
   - Private sector is taking advantage of economies of scale from the operation of similar project in other jurisdictions, the PPP option becomes more attractive

Public Private Partnerships (PPPs)

7. Observability and measurability of quality
    - Concerns about the quality of services
    - The partnership agreement should specify the required quality, provide the measurement of verification of quality and provide for enforcement of the contracts’ requirement.

Risk Analysis

- PPPs involve a range of risks:
  - Construction risks: relate to design problems, building cost overrun and project delays
  - Financial risks: variability in interest rates, exchange rate and other factors affecting financing costs
  - Availability risks: relate to continuity and quality of service provided and in turn depend on “availability” of an asset
  - Demand risks: relate to ongoing need for the service

Risk Analysis

- <u>Pricing of Risk</u>
  - To use PPPs, government must compare cost of public investment and provision of service with using PPPs to provide the service
  - PPPs sometimes are an efficient way for government to relieve its risks
  - Government has to pay for the risks that it transfers to the private sector

Risk Analysis

- ***Market risk*** reflects the economic developments that affect all projects and cannot be diversified and should be priced properly
- private sector demands a discount rate that includes a risk premium on the risk free discount rate that typically government uses

Prerequisites for PPPs Success

- Political commitment
- Good governance
- Government expertise
- Effective Project Appraisal and Selection

Conclusion

- Public private partnerships (PPPs) are **AGREEMENTS BETWEEN GOVERNMENT AND THE PRIVATE SECTOR** for the purpose of providing public infrastructure, community facilities and related services.

- PPPs make projects affordable Better value for money over the lifetime of the project More efficiency in procurement

Thank You