Advantages of PPP

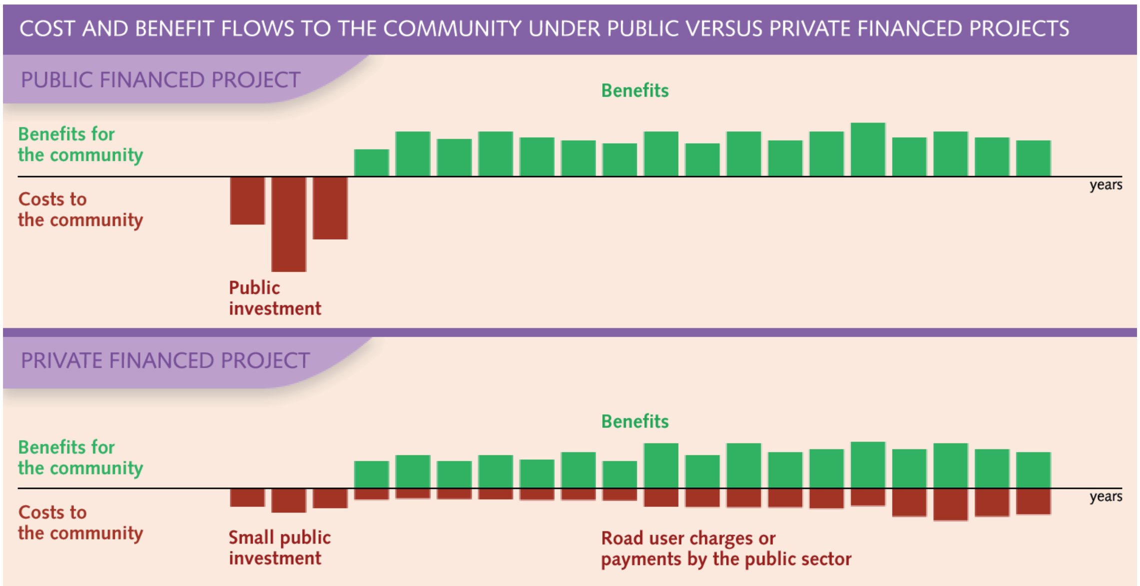
A key advantage of having the private sector provide public services is that it allows public administrators to concentrate on planning, policy and regulation. The private sector, in turn, is empowered to do what it does best, and in particular improve the efficiency and quality of service.

When PPP procurement is applied for the right project and within the right environment, it can produce a win-win situation for both the private and public sectors.

In this respect, it is worth noting that if the public sector does not have the budget capacity to undertake the project, then public opposition based on a comparison of the costs of PPP and conventional procurement, is grounded on the false premise that there is a choice between conventional procurement and PPP.

Increase funding for infrastructure

PPPs financed by the private sectors allow the spreading of the project cost for the public over a longer period of time, in line with the expected benefits (savings on vehicle operating cost, on travel time, on accidents). Public funds are thus freed up for investments in sectors were private investment is impossible or inappropriate.



Source EGIS

On public financed projects, an initial investment is made by the public sector and recovered by the community in the form of the project benefits. On private financed projects the cost for the community is incurred through payments to the private sector over the entire project operation phase, either by payments from the Government or road user charges, notably tolls.

There should be clear distinction between the financial source of investment that could come from the private sector in the form of debt or (to a lesser extent) equity and the source of revenue that will pay back the investment and must come from the taxpayer and/or road users.

Increased funding is only achieved if additional sources of revenues (principally user charges) are mobilized or if PPP investment is considered off-budget for the purposes of public accounting (Module 2 -> Public Accounting). However, in the latter, although the investment is not considered public debt, subsequent payments under shadow toll or availability arrangements shall reduce available public budgets for the duration of the PPP contract. Public budgets may be released in the immediate years but care will need to be taken to avoid over-committing public budgets in future years.

Portuguese PPP Program for Roads (SCUT)

Since Portugal initiated a comprehensive program of road infrastructures in 1995, the country experienced a booming PPP market in this sector which attracted both national and international sponsors, financiers and consultants. Since 1996, Portugal launched 17 tenders in the road sector which led to more than 6.5 billion Euro in initial capital expenditure and to almost 2,000 km of new construction. The Portuguese authorities divided the program between two different concept models, real-tolling and shadow-tolling. A wrong estimate of the public debt impact of the latter, however, damaged the continuity of the program. It is considered today that too many projects were undertaken at the same time, the initial planning did not fully consider the nation-wide dimension, the risk allocation was sometimes inadequate and that expropriations allocated to the contracting authority led to cost overruns and delays. Against this background, future Portuguese road deals might follow the real toll template.

Source : EIC Memorandum of Frequently Asked Questions, European International Contractors, September 2006

If an initial investment in a PPP project falls outside of the public budget, this enables the public sector to make or accelerate investments in infrastructure which would not otherwise have been possible, or would have been delayed until later. Thus the realistic choice, given budgetary constraints, is generally not between a PPP and conventional procurement but between a PPP and no investment at all. PPPs are thus undertaken in addition to other forms of public-sector investment and not in substitution for it.

The scope for increased road user funding is illustrated by the consideration that government budgets currently finance over 95% of investment in highway networks worldwide, while less than 5% is financed directly through tolls (ie direct charges by the user).

IRF Bulletin PPP - Key Principles for Infrastructure Financing and Charging.
IRF Bulletin Special Edition, January 2008.

Introduce private sector efficiencies

The efficient practices of the private sector are already recognized by conventional procurement practices which outsource construction, maintenance and design activities to the private sector. PPP allows to significantly increase private sector efficiency due to the whole lifecycle approach of the PPP contract.

The lifecycle approach allows the private sector to achieve efficiencies in the following four main areas:

- **Work planning and organization.** Long-term contracts allow an improved planning and programming of the work by the contractor. The private sector has greater flexibility in adjusting its resources (personnel, equipment and materials) to a constantly changing situation which can, notably, ensure timely performance.
- **Optimization of lifecycle costs.** In a well-designed PPP contract, both construction and rehabilitation-maintenance tasks are taken into account over a long period; the contractor is thus able to balance expenditure over the project life and make effective trade-offs between investment, maintenance and operation costs subject to environmental, social and economic considerations. A private operator can ensure optimal rehabilitation and maintenance works are performed on the pavement deterioration cycle outside of constraints of public funding availability and tendering which often delay necessary works under the conventional procedure.
- **Risk management.** With proper risk identification and allocation, international experience shows that works performed under PPP contracts tend to meet cost predictions and deadlines better than conventional contracts.
- **Innovation.** The life-cycle approach of PPP provides an incentive for contractors to define alternative solutions to meet performance requirements at lower cost and/or with higher efficiency. Research and development can allow the improvement of quality and efficiency of construction techniques, processes and equipment. It is also becoming recognized that the least-cost solutions may also be the environmental solution (eg pavement recycling, energy-efficient hot mixes etc), as they will tend to require the lowest use of resources.

On heavily trafficked roads where congestion and safety can be critical, private sector involvement can deliver more diversified services optimized to respond to road users' needs and expectations. Innovative systems and services for traffic management or stand-by services for accidents are more efficiently provided by the private sector.

IRF Bulletin PPP - Public-Private Partnerships (PPPs) in Road Works: A Prosperous Marriage, Michel Démarre. IRF Bulletin Special Edition, January 2008.

The competitive tendering process must ensure that the greatest share of the efficiency gains introduced by the private sector is transferred to the public sector through a reduced lifetime cost for infrastructure.

Competition is the primary factor motivating managers to cut waste, improve operational performance and allocate resources efficiently. Furthermore, since many road projects involve the utilization of public property, it must be allocated competitively in order to obtain its maximum value and hence protect the interests of the Community. Two mains forms of competition can be used.

Competition in the market (Competition between private firms or transport modes in a market with no regulation on entry) is not easy to put in place in the road sector. The requirement of long-term and comprehensive contracts to maximize efficiency gains and the practical impossibility of having several firms providing the same services on the same road are conflicting with this principle. On a case to case basis, measures can however be put in place to prevent abuse of dominant position firm the private operators. Contracting simultaneously several firms to provide similar services on comparable portions of the network will provide good benchmarking references and naturally regulate the market. On toll roads, allowing alternative routes on the same corridor (roads or other transport modes) can also have stimulating effect when not jeopardizing financial viability.

Competition for the market (Competition between private firms for the right to provide services on a particular road or a portion of the network) is best obtained by selecting private firms through competitive bidding procedures. Under this provision, competition is concentrated in the few months of the procurement period while the benefits are expected to be brought throughout the entire operation period.

One of the tangible results of private sector efficiencies is improved projects delivery.

In the UK, which has one of the largest PPP programs worldwide, improved projects delivery was reported by the NAO (National Audit Office) in its report PFI: Construction Performance, February 2003.It may be noted that PFI is the national terminology for PPP.

IMPROVED PROJECT DELIVERY UNDER PPP, UK

	Previous experience (1999 Government survey)	PFI experience (2002 NAO census)
Construction projects where cost to the public sector exceeds price agreed at contract	73%	22%*
Construction projects delivered late to public sector	70%	24%**

NOTES

* None of the increases in PFI price after contract award where due to changes led by the consortium alone. Form example, in some cases the department changed some of the specifications from those for which the consortium had bid, so the price increased to reflect the changes. Some of these specifications changes arose due to new factors affecting the department's needs after contract award. These changes would also have led to price increases under traditional procurement.

** In only eight per cent of PFI projects surveyed was the delay more than two months. No comparative data for this statistic are available for traditionally procured projects. Previous studies of traditional projects had referred to the percentage of time overruns rather than the number of months.

Source: National Audit Office

Associated with this advantage is the ability of PPP to inform conventional procurement policies. Clearly articulated objectives, better appraisal techniques and the formulation of a more refined business case within the public sector can be seen as "spin-offs" from a well-developed partnership approach.

The government and controlling bodies may thus benchmark the performance and quality of services provided by the private sector. This benchmark can be used to measure the quality of services provided by government agencies.

Encourage public sector reform

A PPP program can serve as a catalyst for public-sector reform in a number of different ways

- **Transparency and accountability.** A PPP makes the real cost of the facility clear – it cannot be cut into pieces and buried in the depths of public accounting. In particular, it shows the whole-life cost of the facility, including operation and maintenance, in a transparent way, and forces the public sector to make choices about how services are to be delivered and paid for. Public-sector accounting does not deal with the cost of public infrastructure in the integrated way. The result of transparency is accountability: as public-sector officials cannot hide the cost of choices they must justify them, however uncomfortable this is.
- **Procurement skills.** The PPP process develops procurement skills in the public sector since public-sector requirements have to be analyzed and clearly set out in advance and once decided cannot be easily changed. A major factor in the public-sector construction cost overruns is that the public authority does not specify what it wants in sufficient detail, or keeps changing its mind about what it wants during the construction phase of the project. While cost overruns are not impossible with a PPP, they are certainly less likely. Furthermore, the public authority has to think about the long-term service delivery, operation and maintenance of this facility as part of the overall cost when negotiating a PPP contract, instead of only looking at its capital cost. Lessons in "joined-up thinking" learned from PPP procurements can be applied by the public sector in a much wider context. Ideally the transparency of PPP procurement would also spill over into conventional procurement.
- **Management.** A PPP allows the public authority to act as a regulator and thus concentrate on service planning and performance monitoring instead of being involved in the day-to-day delivery of the services.
- **Contestability.** If a small number of projects are undertaken, these can serve as a benchmark against which cost and service delivery in respect of the large majority of facilities still under public sector control can be compared, leading to improvements in public-sector procurement and service delivery as well. Indeed, a small number of countries (eg Norway) have undertaken PPPs primarily to test them against public-sector procurement rather than for budgetary reasons.

Other advantages are described in: Prud'homme, "A Draft Typology of Public-Private Partnership", extract from Financing of major infrastructure and public service projects, Perrot, 2001.

Reduce risk for the public sector

The transfer of part of the project risks to private partners is one of the key incentives generated by public private partnerships and directly results in a better control by the public sector of the overall project cost, delivery time frame and quality of outputs.

Generally commercial risks are transferred to the private sector including lack of demand for the services or products provided by the facility, the risks related to the costs of the service or product and fluctuations in foreign currency rates or inflation.

By allocating risks to the party best able to manage and mitigate them, the public sector is reducing the likelihood of the risk occurring and the impact in the event that it does occur and is thus obtaining overall efficiencies for the project, translated by a lower overall cost over the lifetime of the project.

Other possible advantages

- Several other possible advantages of PPP are cited below, their actual occurrence and magnitude depending on the characteristics of the particular PPP project.
- Improve level of service, especially for projects requiring road user charges (tolls or other).
- Promotion of economic and social growth by private direct investment.
- Transfer of modern technology to domestic public and private sectors.
- Rigorous project selection and avoidance of political "white elephants".
- Promotion of environmental and social sustainability: the private sector focuses on efficient use of resources and materials over the project lifecycle.
- Extending private ownership and adopting a market-economy approach.
- Stimulating of domestic capital and debt markets.

Source: Egypt, Ministry of Investment, Egyptian Investment Portal

http://www.investment.gov.eg/MOI_Portal/en-GB/Investment/PPP+Strategy/

Tollways, The Learning Issue, pg 66
http://www.ibtta.org/Tollways/issue.cfm?ItemNumber=1176

EIC Memorandum on Frequently Asked Questions.
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Evaluation of PPP projects financed by the EIB, Synthesis Report.
European Investment Bank, 2005