PPP
Public Policy
Requirements and
Assessing Risks

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PPP PROJECT DEVELOPMENT THROUGH TOOLKIT MODULES

PPP FRAMEWORKS & PRELIMINARY PROJECT LISTS

Modules 1 & 2
- **SETS THE BROAD FRAMEWORK**
  - PPP or not Types of PPP Concepts Characteristics

Module 3
- **ROAD SECTOR PLANNING**
  - Public sector programs and projects
  - Preliminary identification of potential PPP projects

Module 4
- **DRAFT STANDARDIZED CONTRACTS**

Module 5
- **SPECIFIC PROJECT IMPLEMENTATION**
  - **STAGE 1:** Identification, Prioritization and Selection (Multi Criteria / Value for Money)
  - **STAGE 2:** Due Diligence and Feasibility Studies (Feasibility Study / Consultation / Market sounding) Packaging / Draft Tender Documents / Prepare Bankable Projects
  - **STAGE 3:** PROCUREMENT (PQ and bidding)
  - **STAGE 4:** CONTRACT AWARD
  - **STAGE 5:** CONTRACT MANAGEMENT

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The Toolkit presents a wide definition of PPP including:
Performance Based Maintenance Contracts (PBMC)
Overview

• Public Policy related to PPP
• National PPP program
• Institutional Arrangements
• PPP Policy Framework
• Regulatory Framework
• Legal Framework
• Allocating PPP Risks
• Pros & Cons of PPP
• Some Lessons for Success
PPP Public Policy

- A key objective is to capture the entrepreneurial skills of the private sector
- Essential to ensure these skills generate:
  - benefits for the community
  - profits for the concessionaire
- PPP projects must be consistent with public policy and plans
- No project should be accepted only to provide a commercial return to its developers
PPP Public Policy

• Government must:
  – maintain control over policy, and
  – Ensure that private capital balances social benefits with the returns to investors

• PPP projects should be subject to full social cost-benefit assessment:
  – to ensure public as well as private benefits
  – to establish need, and provide basis, for public participation in financing

• Public Sector Comparator must be used to test “Value-for-Money”
Establishing a National PPP Program

- The launch of a national PPP program is a major policy initiative, whether it is for a single stand-alone project or a pipeline of potential PPP projects.
- Three key steps are required:
  1. Establish institutional structure for PPP
  2. Develop and articulate a PPP policy framework
  3. Identify initial projects and assess PPP option
Institutional Structure for PPP

• Central/National Level: (Ministry of Planning, Economy or Finance) responsible for:
  – Policy, Regulations, Guidelines, Studies, Finance, Knowledge, Monitoring

• Implementation Level (Line ministries, Agencies, etc) responsible for:
  – Sector Planning, Project Selection, Studies, Finance, Contracting, Monitoring

• Joint/Combined ( Separate PPP Unit)
  – PPP Framework, Studies, Funding, Monitoring

• Importance of advisors
  – PPP Project Development Transaction Specialists
Policy Framework

• A Policy Framework brings together the elements of promotion and control by Governments to:
  – Encourage PPP Investment
  – Inform widely within Government
  – Inform widely Stakeholders including consumers/users

• Benefits:
  – Facilitates planning and implementation
  – Instils confidence and understanding
  – Provides an enabling environment for PPP
  – Defines the role of the Government in the support and regulation of PPP
Content of the Policy framework

- PPP policy framework should include:
  - Overall Policy, objectives, direction, benefits, costs, etc.
  - Legal and Regulatory framework
  - Risk Management Framework
  - Procurement guidelines & Model PPP contracts
  - Financial guidelines (inc. tolls and public sector support)
  - The Project Cycle and the role of Advisors
  - Technical design and service standards
  - Approvals Framework (inc. dispute resolution)
Types of Government support

SELECTING GOVERNMENT SUPPORT OPTIONS (SCHEMATIC)

- Impact on ability of project to raise debt
- Debt guarantees
- Exchanges rate guarantees
- Grants
- Subordinated debt
- Minimum traffic/Revenue guarantees
- Shadow tolls
- Revenue enhancements
- Concession term extension

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• Market forces should be preferred to regulation, however ...

• Regulation is important when:
  – The transport infrastructure or service involved is a natural monopoly (e.g. bridge or tunnel with no effective alternative)
  – There is significant market power (e.g. highway with alternatives that are congested or in very poor conditions)
  – The rights and obligations in a PPP concession agreement rely on regulatory interpretation.

• Typically, the functions of a regulator include:
  – Establish standards for the terms and conditions for supply of services
  – Regulate rates (tariffs) and other service charges
  – Establish market rules for the sector (issue, review and cancel licenses)
  – Monitor performance of the regulated entities
  – Arbitrate and settle disputes within the sector
Types of Regulation

Different regulatory options can often coexist:

- Independent Regulation: Independent regulator sets tariffs and regulates access, quality of supply, customer service dispute resolution.
- Regulation by contract: Regulatory regime (including tariff setting) prespecified in detail in legal instrument.
- Advisory regulators: Regulatory outsources some supports functions.
- Expert panels: Independent reviews.
- Outsourcing or regulatory functions to third parties: Consultants or expert panels undertake or assist with tariff reviews, standard setting, monitoring, arbitration.

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Legal Framework

• Ensures transparency, fairness, sustainability and proportionality:
  – Asserts specific rights and obligations for each party
  – Requires relevant institutions to implement the rights, i.e., an independent judiciary system

• Legislative framework includes two types of laws:
  – ‘Enabling laws’ such as a concession or PPP law or a sector specific law (e.g. toll road legislation)
  – ‘Impact laws’ such as public procurement, foreign investment, property, dispute resolution, company, security, tax, labor, environment, competition, etc.
Allocating Risks

- Risk transfer is key to any PPP arrangement, particularly for highways
- There must be a well thought & thorough definition of risks and structure for risk allocation
- Risks should be allocated to the party best able to manage them
- Concession bidding should be rational within a well defined risk allocation matrix:
  - not a lottery due to uncertainties in the risks assumed by the concessionaire
PPP Risks

- Political and Policy issues
- Traffic and Revenue forecasts
- Engineering design & construction
- Financing structure & parameters
- Private Sector monopolies
- Legal framework
Political and Policy Risks

- Political stability
- Government decides to provide additional or competing capacity
- Fiscal or other measures affecting the use of cars or trucks
- Changes in standards,
  - safety and axle weights
- Contract transparency, including in the award process
  - lack of transparency
    - reduces value for money
    - deters some bidders
Allocating Policy Risks

• Political, economic and demographic risks are beyond reasonable control of concessionaires
• Project development (obtaining the necessary permissions):
  – Environmental certificates, social mitigation, other safeguards
  – Some public underwriting is necessary
• Guarantees can be used to mitigate against political & policy risks
Traffic and Revenue Risks

- Closely related to:
  - National and local economic and local demographic growth
  - Willingness to pay by road users
  - Estimated time savings
  - Perceived value of time

- Dependent on accuracy of forecasts:
  - Long term traffic volumes
  - Forecasts are more likely to be optimistic than pessimistic
Financing Risks

- The main risk should be with the concessionaire.
- Exchange risks, if internationally funded, should be with Government.
- Repatriation, if local currency is not fully convertible, and international finance is required, is best with Government.
Other Risk Factors

• “One-off projects” require higher provision for risks, so cost more than "Basket of Projects"

• Monopolistic Behaviour:
  – competition is for the concession, not in the market once let
  – concessionaire may seek to exploit monopoly
  – concession agreement must protect public interest
PPP Pros & Cons

• Preparation of PPP projects costs much more than public sector projects
  – design, legal, financing costs
• Concessions contracts for PPP projects are much more complex than standard FIDIC contracts
  – legal and financial advice costs much more
• The cost of debt for the private sector is higher than for the public sector
  – especially for "one-off" private projects
• The whole process can be much more time consuming
• The contingent liability for the Government depends on the risk allocation
PPP Pros & Cons

• Many governments seek to increase the capital available for investment in highways through off balance sheet accounting

• A cost premium might be politically acceptable if the project is recorded as off balance sheet

• EuroStat guidelines:
  – Private partner assumes Construction risk and Availability or Traffic demand risk

• IMF criteria for off-balance sheet accounting:
  – Proven VFM through Public Sector Comparator
  – “Significant” risk transfer to private sector
Main Lessons for Success

• A well defined legal framework with well developed model concession contract
• Simple and transparent procurement
• Shared risk-reward concession structure
• Appropriate Government revenue support system
• Projects should have social benefits as well as commercial viability
• Particular attention to revenue forecasting
• Public sector comparator is a must
• Need for institutional capacity to manage PPP projects with external expert advice
PPP should be a true “Partnership”
Discussions