Rethinking the Government – Business Relationship: Collaboration in Public-Private Partnerships

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Where are PPPs Being Used?

Physical Infrastructure
- Infrastructure
- Transport
- Energy
- Telecommunications

Social Infrastructure
- Schools
- Health
- Agriculture
- Economic Development
A Public-Private Partnership is a **contractual agreement** between a **public agency** (federal, state or local) and a **private sector entity**. Through this agreement, the **skills and assets** of each sector (public and private) **are shared** in delivering a service or facility for the use of the general public.

In addition to the sharing of resources, **each party shares in the risks and rewards** potential in the delivery of the service and/or facility.

source: www.ncppp.org
What’s Different About a Public-Private Partnership?

Three primary PPP considerations: ownership, structure, and risk.

Ownership refers to the party that has and controls the rights or interests of an asset or service enterprise.

Structure refers to the resulting contractual arrangements that are used to facilitate P3s.

Risk refers to the financial and or legal responsibilities that are undertaken by the designated party – public, private or both depending on the terms and conditions of the contract.
Infrastructure Spending: Megatrends

Worldwide infrastructure spending to grow from $4 trillion per year in 2012 to more than $9 trillion by 2025.

Growing urbanization will drive infrastructure investments in water, power, & transportation

Five key infrastructure sectors include extraction, utilities, manufacturing, transport, and social. Financing will drive investment!

- Megatrends: Demographic changes, regional economic growth, urbanization, technology, resource scarcity, climate change, and natural resources
Demand for investment; but how to increase investment, without increasing public investment? Raising capital

Demand for infrastructure – how to prioritize projects?

Demand for logistics, upgrade economic competitiveness

Governments look to private investment

PPPs are important tool

Different projects and sectors require different approaches
Motivation for Public-Private Partnerships

- Financing and Risk Transfer
- Market driven – Competition and efficiency
- Leverage private sector expertise and experience
- New technologies and personnel development
- Creation of new assets, upgrading deteriorated assets
- Overcome political, legislative, and budgetary battles
- On time, under cost – incentives to meet range of goals
- Increased accountability
Concerns about Public-Private Partnerships

- Unrealistic expectations about risk
  - (Currency, war, terrorism, civil disturbance, breach of contract)
- Complexity of project
- Optimism bias – expectations about costs & benefits
- Financing schemes
- Need for effective legal and regulatory frameworks
- Vision needed for supporting infrastructure
- Requires government leadership
- Demands political and administrative stability
Anticipated Growth in Infrastructure

During the next 25 years, modernizing and expanding urban infrastructure will require approximately $41 Trillion

Projected cumulative infrastructure investment needed during the next 25 years to modernize obsolescent systems and meet expanding demand, broken down by region and sector.

Source: Strategy + Business magazine (Spring 2007) by Booz Allen Hamilton, Inc.
Institutional Sophistication and PPP activity

http://individual.utoronto.ca/siemiatycki/PPP%20Sophistication.html
Impact Investor Engagement by Sector

Number of respondents with allocations to a sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>Number</th>
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<tr>
<td>Food &amp; Ag</td>
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<td>Arts &amp; Culture</td>
<td>18</td>
</tr>
<tr>
<td>Other</td>
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</tbody>
</table>

Source: GIIIN

Sovereign wealth fund (SWF) is a state-owned investment fund investing in real and financial assets such as stocks, bonds, real estate, precious metals, or in alternative investments such as private equity fund or hedge funds. Sovereign wealth funds invest globally. Most SWFs are funded by revenues from commodity exports or from foreign-exchange reserves held by the central bank (http://en.wikipedia.org/wiki/Sovereign_wealth_fund).

SWFs collectively manage more than $6 trillion USD (Infrastructure Investor, November 2013, p.7)
What Kind of Partnership Design to Use?

What each letter means:
D – Design
B – Build
O – Operate or Own (set by context)
F – Finance
L – Lease
M – Maintain / Manage
T – Transfer to public ownership

Put them together to create a model for a PPP
BOO, BOOT, BOT, DB, DBO, DBOFM, BLOT
Continuum of Partnership Type

New Projects

Design-Build
Design-Build-Maintain
Design-Build-Operate
Design-Build-Operate-Maintain
Build-Own-Operate-Transfer
Build-Own-Operate

Public Responsibility

Service Contracts
Management Contracts
Lease
Concession
Divestiture

Private Responsibility

Existing Services and Facilities

National Council for Public-Private Partnerships
What Private Organizations Should Know About Working With Government

• Political, legal, bureaucratic, and regulatory processes exist for a range of reasons – Need to understand processes
• Public institutional control and authority – these matter
• Stakeholder engagement is diverse, active, and necessary
• Government is not an open checkbook – corruption & accountability are high on the public’s agenda
• Coordination can be difficult & costly; still necessary to do
• Media, courts, and political institutions are powerful
• Private sector needs to build its own PPP capacity (technical, political, etc.)

What does Government not understand?
What Government Should Know About Private Partners

- Assessments of risks and potential benefits
- Incentives and reputation matter
- Communication – interaction and dialogue are critical
- Changes, delays, and indecision cost money
- Businesses need to make a profit & politicians cannot keep rates artificially low for their own re/election benefits
- Streamline legal, bureaucratic, and regulatory processes
- Traditional processes will need to change for PPP success
- Remember – you choose firms for their expertise and experience
- Micromanaging costs money and someone has to pay

What does the Private Sector not understand?
Eight Keys to Successful PPPs: A Summary

1. Statutory and Political Environment
2. Organized Structure
3. Detailed Business Plan
4. Guaranteed Revenue Stream
5. Stakeholder Support
6. Managing Relationships
7. Risk Management
8. Pick Your Partner Carefully

source: www.ncppp.org
Public Opinion – What do we know?

• Citizen engagement is critical for: Information exchange, voice, access, legitimacy, ownership, technical, schedule, and financial costs can be high in the absence of public support.

• Citizen perspective – what can we predict from socio-demographic and economic characteristics in terms of supporters & opponents.

• Customizing public participation
  • One set of process & outreach strategies for specialized elites
  • Need for inclusive involvement mechanisms for citizens

• Citizen engagement is more than legislative/regulatory compliance

• Transparency and community buy-in

• Avoid optimism bias & improve performance
Spectrum of Public Participation

Adapted from the International Association for Public Participation (IAP2)

Inform
- Fact Sheets
- Web Sites
- Open Houses

Consult
- Public Comment
- Focus Groups
- Surveys
- Public Meetings

Involve
- Workshops
- Deliberative Polling

Collaborate
- Citizen Advisory Committees
- Consensus-Building
- Participatory Decision Making

Empower
- Delegated Decision Making
- Deliberative Democracy

Engagement Processes
Participation Processes
Democratic Processes

One-Way Communication

Two-Way Communication

Deliberative Communication
Key Findings: Public Involvement in PPPs

- **Pre-Contract Award** Public Involvement Activities:
  - Most effective when implemented early on in the project design process (across deliberative activity types)
  - No distinction between virtual and in-person events
  - The use of web-based forums on their own, mid-way in the delivery process, can have a negative effect on PPP outcomes

- **Post-Contract Award** Public Involvement Activities:
  - Target key constituents, not elected leaders for feedback
  - A range of solicitation activities can be beneficial to a wide spectrum of outcomes
  - Personal (in – person meetings) and impersonal approaches (surveys, web forums) can have contradictory results on contractual terms and political support, respectively.

Boyer, Van Slyke, and Rogers 2016
Importance of Public Involvement in PPPs: Integrated Urban Development

Innovative participation processes

City platforms: learning processes and exchange

Future Sessions
Workshops
Online Dialogue
Surveys and Polling

Workshops
Excursions
Public Events
Telefon conferences

SYRACUSE UNIVERSITY
Maxwell School
Relationship Dimensions

**Open Communication**
- Collaborative decision-making and risk-sharing

**Stakeholder Engagement**
- Level of personal and professional commitment between individual employees of a PPP and institutions overseeing the design and implementation of the PPP

**Role Attitudes**
- Different perceptions of private sector and public sector strengths and weaknesses must be accounted for in the design and implementation of a PPP

**Behavior Rules**
- Public and private actors are motivated by different incentives and goals which inform the way they make decisions in the context of their relationships with one another
Relationship Examples: Open Communication

Case example: APA Nova Water Treatment Project – Bucharest, Romania

Public Participants: Municipal Government, City of Bucharest

Private Participants: Vivendi Universal (owner of APA Nova)

Key Issues:

High Levels of Coordination Between Partners: The co-ordination and decision making between the two parties – Apa Nova and Bucharest city government - were regulated by a board on which both parties were represented. A Director General was responsible for the day-to-day management of the operations.

Contract Mutually Beneficial: Bucharest is receiving reliable financing for upgrading and improving the quality of its water system. It is able to access the required expertise and technology and can potentially share a profitable dividend. The private operator is expecting economic profits by improving operational efficiency and ensuring that revenues from the water tariff are effectively collected.

Implications: PPPs should consider implementing a governance structure and contract design that formalizes shared responsibility and joint-decision making thereby ensuring a potentially higher degree of interdependence.
Relationship Examples: Stakeholder Engagement

Case example: Results from Survey of Employees of British National Hospital Service PFI

Public Participants: National Health Service Hospital

Private Participants: Private Sector Healthcare Provider

Key Issues:

Commitment Focus Shifts Among Employees Working for New Private Sector Provider: Employees’ ties with their employing organization, the hospital, were weakened as employees began seeing themselves primarily as the private partner’s staff. They felt a loss of organizational affiliation after the transfer. This feeling is reinforced in that other hospital staff still employed by the public sector see the outsourced employees as no longer a part of the hospital and more as part of the contracted workforce.

Implication: The design and execution of a public-private partnership can have significant effects on organizational citizenship; it can shift both the level of employee commitment to the public organization and influence the institutional culture of the partnership.
### Types of Risk

<table>
<thead>
<tr>
<th>Risk Type</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Planning Risk</strong></td>
<td>Risk that poor planning between public and private partners does not translate into action efficiently</td>
</tr>
<tr>
<td><strong>Operational Risk</strong></td>
<td>Risk of environmental hazards and liabilities, operating costs and overruns, delays in service</td>
</tr>
<tr>
<td><strong>Capacity Risk</strong></td>
<td>Risk of a lack of sufficient technical and / or organizational expertise and / or technical capital to facilitate a PPP goal</td>
</tr>
<tr>
<td><strong>Execution Risk</strong></td>
<td>Risk of partnership failing to incorporate key knowledge / data acquired during planning stage, thus leading to flawed execution of partnership</td>
</tr>
<tr>
<td><strong>Financial Risk</strong></td>
<td>Risk that transaction costs are ignored or underestimated</td>
</tr>
</tbody>
</table>
Risk Example: Operational

Case example: The Failure of Latrobe Regional Hospital (Victoria, Australia)

Public Participants: Victorian Government

Private Participants: Private consortium of health care providers

Key Issue:

Failure: Hospital fails two years after operations begin, September 1998

Cost Overruns: The private consortium had unreasonable assumptions about government subsidies and costs. It misunderstood the case-mix funding model and its impact on future funding levels. The operator was unable to make a profit from the delivery of services at the performance level desired.

Implication: Cost overruns can stem from poor communication or misunderstanding in the planning stage of a project. What role does government play, if any, when private partner financially underperforms?
Risk Example: Technical Capacity

Case example: Lebanese Telecom Industry

Public Participants: Lebanese Government

Private Participants: Cellis, Libancell (French telecommunications companies)

Key Issue:

- **Partnership:** In the late 1990s, Cellis and Libancell partnered with the Lebanese government to form Lebanon’s first telecommunications network.

- **Early Challenges:** A dispute emerged between the government and cellular operators over a subscription cap of 125,000 mandated by the government. The government issued a $1bn fine against to the operators. The telecommunications companies denied the legal validity of this cap.

- **Lack of Public Sector Technical Knowledge:** The Ministry of Telecommunications lacked the technical or organizational expertise to adequately oversee the mobile concessions.

Implications: PPPs in which one partner (typically the private sector) has greater technical and organizational capacity and sophistication than the other partner can lead to poor governance.
Risk Example: Financial

Case example: Ireland’s Public Schools

Public Participants: Irish Government

Private Participants: Jarvis (Industrial Developer)

Key Issues:

School Construction: In 1999 the capital constrained Irish government attempted to use a PPP model to construct new public schools. A private sector consortium led by Jarvis Projects Ltd. was contracted for a DBOF for 5 public schools.

Poor Bid Evaluation: The original bid by Jarvis did not include transaction costs (VAT).

No Evaluation of DBOF Model: Financial differential between an original DBO plan and DBOF plan was not explored.

Underestimation of Costs: The decision to expand the number of schools to be purchased from 3-5 led to a significant underestimation of costs (24%).

Implications: Inadequate financial planning of transaction costs and failure to consider tradeoffs among PPP forms can lead to significant cost overruns that diminish the value-for-money promised by a PPP.
What Investors are Most Worried About: Political Risk

• Regulatory Frameworks that are not well defined & stable

• Implications for Infrastructure:
  Lack of **central** planning. Megaprojects are regional and national in scope. Don’t leave this to local officials. Often legal misalignment.
  Customer rates – politicization of payment structures & rates
  Changes in laws, regulations, and contractual rights
  Currency inconvertibility and transfer risks

Spain and Norway are two examples where governmental ministries cut renewable energy subsidies (Spain) and tariffs for the country’s gas transportation network (Norway). In the EU, Basel III has prompted banking to see off project finance debt on the secondary markets at a substantial discount. Options: Political Risk and Debt Insurance
PPP Governance Objectives

• Fair and transparent selection process - Anti-corruption
• Value for money assurances
• Improvement of public services
• Fair incentives and returns for risk takers
• Fair negotiation, dispute mediation, conflict resolution
• PPP more than a financial mechanism
• Mutual Understanding
  • Both parties have different interests
  • Context matters – central vs provincial; megaprojects
Writing Rules & Building Relationships

• **First**, government needs to know what it’s buying
  What can & cannot be specified
  What it will take to design and build it
  Knowing what it knows & doesn’t guides agency in deciding
  - How flexible rules should be
  - How vigilant it manages the vendor

• **Second**, establish a system of rules – a contract
  Reflects level of certainty (specificity) about what it’s buying
  Relationship rules – specify government’s and vendor’s governance roles
  and how to resolve conflicts

• **Third**, build, maintain, and manage relationship with vendor
  Active engagement to learn, adjust, & adapt to the other throughout the
  life of the relationship – who has power, authority, over what
Implications: Need for Governance Rules

- Decision Authority
- Cost Responsibility
- Integrated Partner/Product Teams
- Performance Incentives
- Information Sharing
- Monitoring & Enforcement
- Third Parties

- Described in abstract; harder to execute in practice
Building Capacity

• Private Sector, National Training Programs, and Multilateral Cooperation

• PPP units and task forces within Ministries
  Inter-ministry taskforces, ministerial-level Committee on Infrastructure
  with the Planning Commission and Department of Economic Affairs

• Allows governments to build internal expertise on PPP projects & lessons

• Agencies can develop the PPP market, and provide technical assistance in
  issues that arise throughout the course of a project.

• PPP units are either independent agencies, a unit within a finance
  ministry, or are dedicated units within one or more line industries

• Engagement with Development Banks (e.g., IADB) & Use of external
  advisers

• As of 2009, over ½ of all OECD countries have governance units of some
  kind
# PPP Units and Their Roles

**PPP Units and Their Roles**

<table>
<thead>
<tr>
<th>Economy</th>
<th>PPP Unit¹</th>
<th>PPP Policy guidance and capacity building</th>
<th>PPP Promotion</th>
<th>Technical Support</th>
<th>Gatekeeping (Approval of PPP Projects)</th>
<th>Procurement of PPPs</th>
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<tr>
<td>Cameroon</td>
<td>National PPP Council CARPA</td>
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**Source:** Benchmarking PPP Procurement 2015

¹ We consider the PPP Unit the one suggested by the majority of our contributors. In Colombia, Peru, Tanzania, and Tunisia, specific units to deal with PPPs also exist within the structure of the Ministry of Finance.

² The PPP Unit has now been absorbed into the Government Technical Advisory Component, which is an independent entity which reports into the National Treasury.
Developing Trust in Partnerships

- Committing to cooperation *ex ante*
  - A mutual commitment to a win-win relationship
- Past experience and reputation
- Consistency and timeliness of response
- Transparency and quality of information exchange
- Predictability of behavior under varying conditions and circumstances
- Discretion and Behavior: Each other’s choices; Project complexity leads to interdependence
Positive Example: I-495 Capital Beltway HOT Lanes

Virginia DOT

- Develop and operate HOT lanes to keep prioritized vehicles free of congestion
- Provide the right to develop, finance, design, build and operate High Occupancy Toll (HOT) lanes. Provide state grants and loan to support part of the finance
- Provide private finance, asset development and run HOT lane operation business

Private Partner

- Conduct highway project management and operation business
- (Construction firms, highway operator)

Partnership Goal: To operate HOT lanes restricted to vehicles with 3 or more people, buses and other toll-paying cars and keep them free of congestion — even during rush hour.

Partnership Activity: To design, build, finance, and operate two (HOT) lanes in both directions of the beltway.

Funding Sources
- State of Virginia grant - $409 million
- Private Equity - $349 millions
- TIFIA Loan - $585 million
- Private Activity Bonds - $586 million

Local Government-Private-Nonprofit
Central Park Conservancy

http://www.centralpark.com/guide/general-info.html
Final Thoughts

- PPPs – NOT A ONE-SIZE FITS ALL APPROACH
  - Variation by sector, region, size, project, PPP type, financing, & Govt. support
- Policy – Alignment among objectives, projects, communication
- Capacity Building – skills, institutions, training
- Legal – Rules, Courts, Processes – Fewer, better, simpler
- Risk Sharing – cooperative sharing, mutual support
- PPP Procurement – transparent, neutral, competitive, fair
- People – participation, accountability, support
- Environment – green, sustainable, government role
- Accountability – institutional mechanisms are necessary?
- CRITICAL IMPORTANCE of POLITICAL LEADERSHIP
THANK YOU!

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