



**Sustainable Water
Integrated Management (SWIM) -
Support Mechanism**



Project funded by
the European Union

Water is too precious to waste

**Introduction to PPP Concept
and contractual arrangements**

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Context

- ✓ Joint Activity : SWIM-SM and Horizon 2020 CB/MEP
- ✓ Water Finance Agenda in the region : Finance Chapter in the Strategy for Water in the Mediterranean, Arab Water Strategy, Private sector involvement to depollute the mediterranean,...

Definitions

World Bank :

There is no one widely accepted definition of Public Private Partnerships (PPP). Broadly, PPP refers to **arrangements between the public and private sectors** whereby part of the services or works that fall under the responsibilities of the public sector are provided by the private sector, with **clear agreement on shared objectives** for delivery of public infrastructure and/ or public services.

Definitions

International Monetary Fund (adopted by OECD) :
Arrangements whereby the private sector provides infrastructure assets and **services that traditionally have been provided by government**, such as hospitals, schools, prisons, roads, bridges, tunnels, railways, and water and sanitation plants.

Definitions

What we should keep in mind:

- **Generic Terminology : various models**
- **Collaboration between public and private sector**
- **Achieve common objective for service delivery while pursuing own interests**

Why PPPs

To overcome public sector limits (limited efficiency and financial resources, political interference, no separation between operation and monitoring functions...) as well private sector limits (market malfunctioning, prices exceeding, depletion of scarce resources,...)

- ➔ Improve efficiency in service delivery through private managerial techniques and reduce costs**
- ➔ Source of funding for some PPP**
- ➔ Contribute to long term sustainability and favour technology transfer**

Expected benefits

- ➔ **Accelerating services' provision since payments are related to service availability**
- ➔ **Make expertise, experience and innovation capacity of the private sector available for the project**
- ➔ **Integration of operating and maintenance costs in the project design leading to costs saving throughout the project life cycle**

Expected benefits

- ➔ **Implementation of cost accounting (often absent in the public sector)**
- ➔ **application or suggestion of rational pricing, avoiding political interference in managerial decisions**
- ➔ **Mobilisation and development of skills since private companies are involved more frequently at international level in similar projects**
- ➔ **Better performance incentives (return is linked to performance)**

Expected benefits

- ➔ **Efficient management practices**
- ➔ **Flexibility, innovativeness, and speed in decision-making**
- ➔ **Better risk sharing driven by an assessment of the party best able to manage risk (the party best able to influence the probability of occurrence or to deal with its consequences)**

PPP Actors



Tripartite Partnership

1. Government : **Regulation**
2. Private Operator : **Service Delivery**
3. User : **Participation and service payment**

Transfer of Responsibility to the Private Sector



Changing Roles

Brief focus on private operators

Increasing diversity of private actors

- ✓ **International operators** : According to the WB, during 1990-97, five operators accounted for 53% of projects awarded (Suez, Veolia, Thames, Agbar and Saur). Five years later, their share had dropped to 23% (over 2003-2005)
- ✓ **New emergent players** :
 - Business firms whose core activity is not water seeking to diversify (including big users of water: beverage, mining companies)
 - construction or engineering companies moving into water as a business opportunity (innovation in desalination and reuse technologies)
 - Joint ventures with foreign operators
 - Joint ventures between public and private companies
 - Small-scale local actors

Water service characteristics

- ✓ **Monopolistic** : Capital Intensive, long payback periods, low rates of return, important asymmetry of information, inelastic demand → high contractual risks especially in a context of poor initial information and weak regulatory environment
- ✓ **Basic Need** :, high externalities on health and environment, essential input for business, important social and political → justifies public involvement while generating high political interference risk (often materialised by incapacity to adjust tariffs)
- ✓ **Risky sector** : contractual, design and construction, commercial, financial, legal risks → Risk assessment

PPP Models

Vary according to **6 major dimensions** :

- ✓ Asset Ownership
- ✓ Capital Investment
- ✓ Who is responsible of construction
- ✓ Who is responsible of operation
- ✓ Decision-making sharing between the parties
- ✓ Monitoring mechanisms

↳ **Wide range: from service contracts to divestiture**

Service contract or outsourcing

- ✓ Based on commercial agreements
- ✓ Related to specific, time-bound tasks, such as supplying inputs, taking care of planning studies, computing and payroll services or public relations, construction, maintaining assets, installing meters or billing customers,
- ✓ Government : Responsible of financing and operation
- ✓ Private operator : bears very little risk and there is very little uncertainty around the expected outputs
- ✓ Remuneration : fixed fees
- ✓ Contractual specifications to monitor performances
- ✓ Contract Duration : few months to 1-2 years
- 👉 **In recent years, more and more activities have been outsourced that way to the private sector, including the task of reducing non-revenue**

Management contract

- ✓ Contract includes managerial services
- ✓ Government : responsible of funding and construction
- ✓ Private operator : manage a utility and provide services to the public for a given period of time (it may agree to employ staff from the administration and be responsible of operations overseeing).
- ✓ Remuneration : fixed fee or it may be linked to the performance of the utility, in which case the private operator bears some commercial risk
- ✓ Contract Duration : 3-5 years
- ☞ **More and more countries resort to this type of contractual arrangement to facilitate transfer of know-how and to develop greater understanding of the implications of involving the private sector as part of a gradual approach to the private sector participation**

Lease

- ✓ Under lease contracts, a property owner allows a tenant to use the property for a specified period of time and a specified rent.
- ✓ Government : responsible of financing investment such as the replacement of major assets or expansion of the network.
- ✓ Private operator : responsible for providing the service at its own risk, including operating and maintaining the infrastructure for a given period of time.
- ✓ Remuneration : Private operator collects user fees
Private operator paid a fixed fee to the public sector
- ✓ Contract Duration : 8-15 years

Affermage

- ✓ Differs from a lease only in terms of revenue for the private sector. In both cases, the private operator collects the tariffs and pays, on top of the operation and maintenance costs, a fee to the public sector. But while this fee is fixed for lease contracts, it is proportional to the volume of water sold in the Affermage contracts.
- ✓ Remuneration : Private operator collects user fees and pays fee to the public sector
Shared revenue
- ✓ Contract Duration : 8-15 years
- ☞ **The contract specifies adjustment formulas, renegotiation modalities...**

Concession

- ✓ Assets ownership : Public
 - ✓ Private operator : responsible of capital investment, network expansion and operation
 - ✓ Government : approves tariffs and monitor service performances
 - ✓ Remuneration : Users charges.
 - ✓ Contract Duration : 25-30 years
- 👉 **High risk transferred to private sector is compounded by the nature of retribution of the operator, mainly based on user charges**

Greenfield concessions

- ✓ Concern generally the construction and eventually the operation of new plants (desalination plant, treatment plant...)
- ✓ Remuneration : from the public party
 - Contracts involve take or pay provisions (revenue guarantees)
- ✓ BOT (Build-Operate-Transfer) : On expiration of a BOT, the assets are returned to the public sector. BOTs for treatment plants constitute the bulk of the new PSP contracts
- ✓ BOT : Build, Operate and Transfer
- ✓ BOO : Build, Own and Operate
- ✓ BOLT : Build, Operate, Lease and Transfer
- ✓ DBFO : Design, Build, Finance and Operate
- ✓ ROT : Rehabilitate, Operate and Transfer (related to existing infrastructure)

Joint Venture & divestiture

Joint Venture

- ✓ A new company is formed that joins two or more parties – private or/and public
- ✓ Created to facilitate the transition to privatization
- ✓ Additional investments are under the responsibility of the private sector

Divestiture

- ✓ Ownership of the existing assets and responsibility for future upkeep and expansion are transferred to the private sector
- ✓ Governments : approves tariffs
- ✓ Very few countries have adopted complete divestiture with the notable exceptions of Chile and the UK

	Service Contracts	Management Contracts	Lease/ Affermage	Concession	Greenfield Contracts	Joint Venture	Divestiture
Assets Ownership	Public	Public	Public	Public	Private (Returned to Public)	Public/ Private	Private
Capital Investment	Public	Public	Public	Private	Public ou Private	Public/ Private	Private
Construction	Private –depending on the contrat	Public	Private	Private	Private	Public/ Private	Private
Renovation	Public	Public	Private	Private	Private	Public/ Private	Private
Tariff setting	Public	Public	Private Public Regulation	Private Public Regulation	Public	Public/ Private	Private Public Regulation
Facturation des usagers	Public	Public	Private	Private	Public	Public/ Private	Private
Operation /Maintenance	Public	Privé	Private	Private	Private	Public/ Private	Private
Labor (Service)	Public	Private	Private	Private	Private	Public/ Privé	Private
Duration	1 month to 5 years	3 to 5 years	8 to 15 years	15 to 30 yeras	10 years and +	unlimited	unlimited

Key points

- ✓ We should keep in mind that this PPP categorization is indicative : debate on terminology
- ✓ PPPs are highly **dynamic processes**
- ✓ PPPs arrangements are designed and adapted to the specific circumstances

Deciding on PPP arrangement

Depending on :

- ✓ **Gouvernement objective : bridge funding gap, improve management efficiency, service expansion,...**
- ✓ **Allocation of responsibilities and therefore risk- sharing**
- ✓ **Cost- benefit analysis**

Government Objective	Service Contract	Manag. Contrat	Green-field	Lease Affermage	Concession.	Divestiture
Improve Efficiency	+	+	+++	+	+++	+++
Capital investment transfer	0	0	+ / +++	0	+++	+++
Improve service quality	+	+	+++	+++	+++	+++
Control service delivery	+++	+++	0	+	+	0

Don't forget the objective of the other partners :

→ Private sector : return on investment

**→ User : benefit in terms of service quality and cost
(whether perceived directly through tariffs
or indirectly through taxes)**

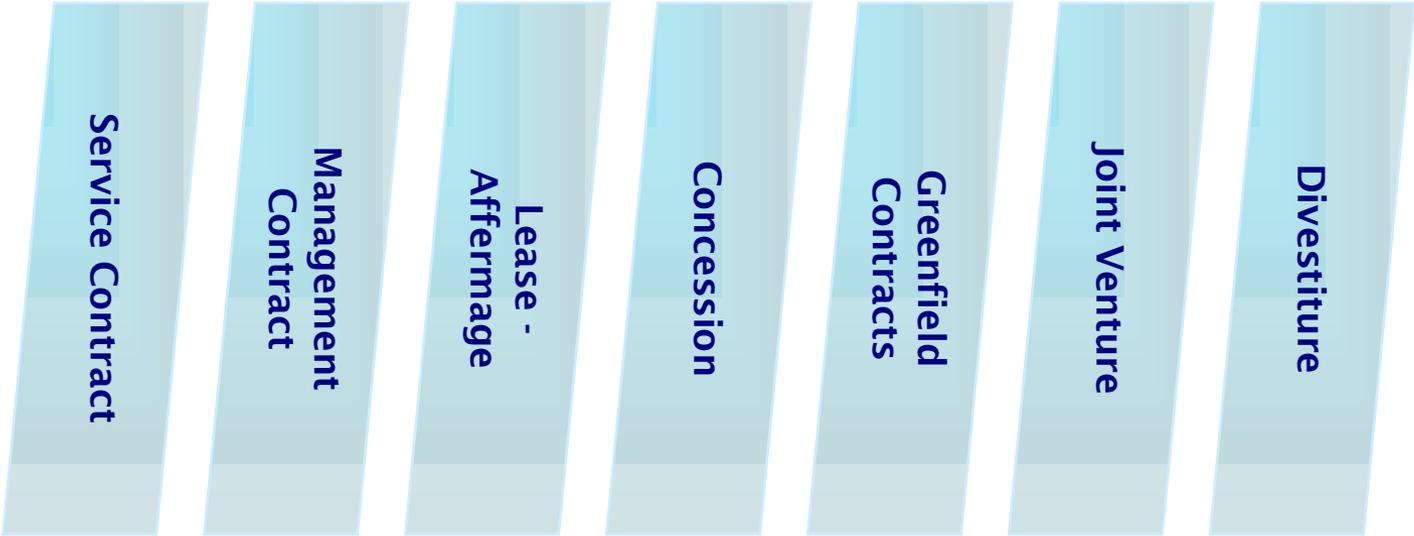
Risk Transfer

Responsibility Transfer → Risk Transfer

The risk taken by the private company increases with its participation

Remuneration sought by the private company is more important when the risk is high

Risk sharing matrix



PPP limits

- ✓ **PPP implementation process can be long and expensive**
- ✓ **Financial cost (both on loans and shares) for PSP is higher compared to the public loans. This additional cost actually reflects the risks that are not considered when dealing with government loans**
- ✓ **Political engagement is essential in order to create the enabling environment and ensure arrangements compliance**
- ✓ **Change in the traditional functioning of public sector : its role evolves from service provider and daily tasks manager to regulation, planning and performance monitoring**

PPP limits

- ✓ **market should include sufficient number of companies in order to allow competition (fundamental principle to improve efficiency)**
- ✓ **Private sector should have enough experience to bring more expertise and added value and improve service efficiency**
- ✓ **Defining outputs and required performances is difficult, in particular that PPPs are long-term contracts**
- ✓ **Risk evaluation is difficult, costs might be swelled if not well estimated**
- ✓ **PPP structure may be relatively inflexible and rigid to be adapted to rapid developments**



THANK YOU