CEE bankwatch network

Never mind the balance sheet:

The dangers posed by public-private partnerships in central and eastern Europe

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This is a summary version. For the full text see:
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Introduction

In recent years the use of public-private partnerships (PPP) schemes in large investment projects has been heavily promoted in central and eastern Europe (CEE). Yet despite the barrage of conferences, workshops and publications promoting PPPs within the region, few CEE countries have to date implemented more than two or three such projects, and even these have often proved controversial.

Discussions in CEE have concentrated on how to best implement PPPs rather than about *whether to implement them at all*. However, in their birthplace, the UK, PPPs have been fiercely criticised, raising the question of whether the CEE countries are in danger of rushing – with strong promotional pressure – headlong into using a discredited investment vehicle.

This report examines the issues surrounding PPPs and, giving examples from the UK and CEE, recommends that public authorities exercise caution over PPPs, examining the evidence carefully before stepping into any more projects. If new PPPs are undertaken, it is crucial that they are carried out with a number of safeguards in place:

- to avoid public funds being over-committed
- to ensure a genuine and fair choice is made between the different available procurement options
- to avoid undue profits for the private sector at public expense.

Where international financial institutions (IFIs) are involved in PPPs, this paper contends, they must take a much more proactive role in ensuring that the public receives good value for money.

What is a PPP?

Public-private partnerships involve commercial contracts between public authorities (state or local) and private businesses in the design, construction, financing and operation of public infrastructure and services that have traditionally been delivered by the public sector, in sectors such as transport, health, water supply or education. They involve either a partnership between a public authority and a private company based solely on a contract, or the establishment of a project company involving both the public and the private sector.[1]

Financing for PPPs comes in part from the private sector, but requires payments from the public sector and/or users over the lifetime of the project, which is often around 25-30 years and sometimes even longer. Payment may come from a public revenue budget – for example in hospital projects – or through direct payments by users, for example toll highways, or by some combination of the two. Payments are also sometimes made by the public authority but based on actual usage of the service or payment especially for the service, for example with 'shadow tolls' for highways where payments are made by the public authority based on the number of vehicles.

Although concessions for such major infrastructure and services projects have been in use for many years, PPPs in the form outlined above effectively began with the UK's Private Finance Initiative (PFI), launched in 1992 in order to allow private capital to be invested in public infrastructure projects. By March 2008, 625 PFI projects had been signed in the UK, with a total capital value of GBP 58.7 billion.[2] PPPs in various forms have since been adopted by many countries, although the degree to which they are used varies widely.

Overview of PPPs in central and eastern Europe

Although the first PPPs appeared in Central and Eastern Europe in the early 1990s, in most CEE countries their use is still at a relatively early stage. So far Hungary has been the most enthusiastic PPP user, partly as a result of its prolonged high level of budgetary deficit. Hungary's PPP programmes involve student hostels, sports facilities, road and rail projects, prisons, waste, wastewater and urban development projects.

The Hungarian M5 motorway, one of the earliest PPP projects in central and eastern Europe. The expected traffic levels failed to materialise and the state has had to buy back a share of the project and guarantee the income of the concessionaire. Photo: CEE Bankwatch Network

PPP projects elsewhere in CEE include the following:

Baltic states: few projects are underway, however the South Bridge in Riga, Latvia, is already causing a scandal due to its constantly rising costs.

Bulgaria: PPPs are planned for various sectors, but the few projects in progress to date are mainly transport infrastructure projects. Existing concessions for Sofia's water supply and waste collection have also attracted public discontent and numerous criticisms due to flaws in their implementation.

Croatia: PPPs have been used for motorway projects, as well as the Zagreb wastewater treatment plant. Only a few new projects are underway.

Czech Republic: several projects are under development in various sectors, especially roads. An attempt to build the D47 motorway by a PPP arrangement failed.

Poland: A section of the A2 motorway and the Gdansk-Torun section of the A1 motorway were built using PPPs. Several other PPP road and rail projects are under development.

Romania: the Bucharest water and wastewater treatment plant are under a PPP concession but most other projects – mainly roads, with some health projects – are in the tendering stage.

Serbia: attempts to undertake a PPP for the construction of the Horgos-Pozega highway ended with the cancelling of the contract. PPPs for Belgrade's waste and water services are being developed.

Slovakia: the D1 motorway is being developed as a PPP pilot project. The government has been strongly criticised for exempting several sections of motorways planned for PPPs from the 'state expertise' assessment, which would help to ensure that the projects offer value for money.

Elsewhere in CEE, PPPs are at an early stage. The modernisation of Tirana airport in Albania is one of the very few PPP projects in the Western Balkans. In Ukraine, PPPs are expected to take off in advance of the Euro 2012 football championship, raising fears of hastily carried out projects without proper assessments and safeguards, while Russia's first PPP highway project, the St Petersburg Western High Speed Diameter, is causing concerns with its rapidly growing costs.

Overall, the results of the PPPs implemented in CEE so far have not been impressive, and it is not clear that they have performed better than public procurement on its own would have.

An important question remains:

Is the potential success of PPPs in CEE mainly a question of gaining experience – which would imply a need to put more effort into institution-building and developing projects – or do PPPs, by their very nature, contain so many potential pitfalls that they should be used sparingly, if at all?

Snapshot of IFI involvement in PPPs

The IFIs promote PPPs not only by making direct equity and loan investments into PPP projects, but also by making private sector participation a part of otherwise public projects, and by using their advisory capacity to promote private sector participation in major investment projects.

The European Bank for Reconstruction and Development

The EBRD has been involved in PPPs in the transport sector since 1993 and in municipal and environmental infrastructure sector since 1996. By the EBRD's own admission, *"Within the Bank's countries of operation, few countries met the above conditions [for financing PPPs], although the Bank has financed PPPs in 15 countries."*[3] Over the past ten years, the evaluation unit at the EBRD has assessed the success of 14 PPP projects that the bank has financed in power and energy, municipal infrastructure and transport. The conclusion from these evaluations is that the bank has had uneven success in PPP projects.[4]

In spite of this, the EBRD has become a vocal advocate of PPPs in countries such as Albania, Georgia and Kazakhstan. The EBRD has also undertaken concerted efforts to develop PPPs in Russia, with the Western High Speed Diameter road project in St. Petersburg currently in line to become a flagship project.

The European Investment Bank

Until 2002, the EIB's PPP investments consisted almost entirely of transport projects. However, in subsequent years the share of the bank's health and education investments involving PPPs dramatically increased, making up around half of investments by 2004.[5]

Almost all of the EIB's PPP investments have been within the EU, with only three such projects backed in CEE – the A2 motorway in Poland, and two sections of the M6 in Hungary.

Unlike the World Bank and the EBRD, the EIB states that it is neutral as to whether PPPs should be used.[6] This position follows EU law.[7] However, particularly in the case of the Trans-European Transport Network, the European Commission and the EIB do actively encourage PPPs,[8] for example through their Loan Guarantee Mechanism for PPP projects in the Trans-European Transport Network, as well as a new European PPP Expertise Centre established in September 2008 and housed in the EIB's Luxembourg headquarters.

The EBRD, EIB and World Bank are all interested in financing the EUR 6.9 billion St Petersburg Western High Speed Diameter PPP. Photo: Save Yuntolovo Public Environmental Movement

Concerns about PPPs

Infrastructure schemes in CEE – whether they involve the PPP approach or not – often suffer from governance problems. Some consist of resurrected plans from several decades ago when neither value for money nor nature protection was an issue. While there are some improvements, even new projects are often not the result of thorough and systematic analysis but a combination of clumsy and unimaginative planning, lobbying, and personal interests. Corruption remains a problem in the region, and tender processes are not always satisfactory.

Too often public officials lack experience with balancing the wishes of the private sector with the best interests of taxpayers, and the costs of projects often rise. Many officials are insufficiently committed to wide consultation and consideration of all alternatives. Consultation processes are too often carried out as a formality, at a late stage, and with no real intention of taking public opinions into account.

Public access to information on such projects is often poor. While occasional scandals emerge about very high profits for the private sector from PPP deals, in general this information is considered commercially confidential. The public is not able to see how much the same project would have cost if it was publicly procured, nor usually how much a PPP programme will cost over its contracted lifetime, i.e. the next thirty or so years.

Due to the possibility of hiding behind 'commercial confidentiality' as an excuse for failing to provide public information, there is very little space for public scrutiny during the preparation of the projects. Where there have been successes in stopping poor deals, such as the Trakia Highway in Bulgaria and the Horgos-Pozega motorway in Serbia, these have mostly taken place after the contracts have been signed, representing a waste of time and money for everyone.

An attempt to build the Czech D47 motorway with a PPP failed as there was no competitive tender.
Photo: Mirek Patrik, Děti Země

Build now, pay heavily later

PPPs seem attractive to public authorities because they sometimes move projects off the government's balance sheet. Instead of up-front capital investments, PPPs use annual instalments from revenue budgets to pay for infrastructure, so governments do not need to directly take loans. However they do often need to provide loan guarantees for the private sector, which can also add to public debt commitments.

The idea – often cited by proponents – that PPPs mobilise extra financial resources for projects that would otherwise have to wait several years to be implemented is highly misleading. **In fact, with PPPs, no extra money is available, it is just borrowed from public budgets for around the next thirty years**. This myth, often duly swallowed by officials, encourages decision-makers to carry out projects that may not be affordable.

In addition, new international accounting guidelines are set to move most PPPs back onto public balance sheets in countries which decide to align their national accounts with the guidelines. Thus the main attraction of opting for PPPs is on course to become a legal dead-end. [9]

So far there has been little discussion in the CEE countries about the future budget burdens that may be caused by PPPs. As the authors of a recent World Bank paper on PPPs in CEE note:

> "EU8 countries ... have only limited information on the risks involved in PPPs and limited understanding of the long-term fiscal cost of PPPs. Moreover, these countries make very little of such information publicly available. PPP contracts and their content are considered confidential. This makes it difficult for policy analysts to assess the long-term fiscal cost of PPPs – and for the public to exercise appropriate pressure on policymakers for fiscal prudence."[10]

The affordability of PPPs is already a serious issue in the health sector in the UK, where the money for capital costs that hospital trusts receive from the government is not sufficient to pay the capital costs for PPP schemes, with the result that the PPP fees are paid for by reductions in service.[11]

In CEE affordability has already been identified as a problem in both Hungary and Croatia, and both countries have been criticised for being too ambitious with their road sector development programmes at the risk of burdening future governments with large liabilities.[12]

Value for money?

Most practioners agree that value for money should be the driving factor in any decision to use a PPP. However it is unlikely that the private sector can build and operate infrastructure more cheaply than the public sector, given that:

1) Private finance is much more expensive than public sector borrowing. For example, the overall finance cost for Scottish PPP schools between 1998 and 2001 was 7–13 percent per year, whereas the public sector loan rate was 4.2–5.9 percent [13]
2) Unlike public authorities, private companies expect to make a significant profit on their investment.[14]
3) The preparation of PPPs is long and costly.[15]

An important tool in assessing the cost-effectiveness of PPPs is a Public Sector Comparator (PSC) calculation, which compares the costs of a PPP with that of the same project carried out through public procurement. Although the UK's PSC calculation has been widely criticised for biasing calculations in favour of PPP schemes ,[16] a PSC calculation does need to be carried out, and the methodology needs to be clear and publicly available to enable scrutiny and improvements.

> In many CEE PPPs, there is no evidence of value for money assessments having been done at all, and where it does take place, the methodology is not publicly available.

The Zagreb wastewater treatment plant has been criticised for offering poor value for money. Photo: UZOR

This is sometimes justified by the claim that there is no way of using public funds anyway, so it is "PPP or nothing". However this claim should be treated with extreme caution, as **it is not likely that a PPP is affordable if a publicly procured project is not**.

A PSC also only makes sense if the possibilities being compared are actually similar. However there have been cases in which PPP projects have been developed to be larger than necessary, in order to make it more appealing for the private sector to participate, for example the Zagreb Wastewater Treatment Plant in Croatia and the Walsgrave hospital in Coventry, UK.[17]

Efficiency through competition?

The main claim justifying PPPs in spite of their higher financing costs is the increased efficiency presumed to come from the competitive tender and the private sector's supposed operating efficiencies. However, in practice, PPPs have been plagued by a lack of competition, resulting in increased costs that may have wiped out the value for money justifications for using PPPs in the first place.

In several PPP cases in CEE there has not even been a competitive tender, for example the Czech D47 road project, the Croatian Bina Istra and Zagreb-Macelj road projects, and the Bulgarian Trakia Highway.

Croatian motorways: Bina Istra and Zagreb-Macelj
The Bina Istra (Istrian Y motorway) and Zagreb-Macelj (Slovenian border) are so far the only two motorways in Croatia that have been constructed using PPPs – with the Zagreb-Rijeka motorway being constructed by a concessionaire owned entirely by the Croatian government. The two PPP concession contracts were negotiated with single bidders, making it "*unlikely that they offer best value, though this is not easy to confirm, due to the lack of best value reviews undertaken to date, and the lack of available time and data/records to carry out a more detailed benchmarking exercise at this stage.*"[18]

In an overview Atkins consultants pointed to poor quality guarantee systems in the concessions contributing to a lack of value for money and user benefits. In both cases the Croatian government (or HAC, the government–owned motorway company) owns 49 percent of the project company, and the state supports the project in the event that projected traffic volumes fall below certain levels. Additionally, the project finance packages have relied heavily on Croatian government support, which effectively guaranteed debt service to project lenders, regardless of how the schemes perform. It is therefore questionable how much of the risk has been transferred to the private sector.

The government's involvement in the concession companies also means that the schemes still involved public borrowing and therefore an increase in public sector debt.[19]

While the IFIs do not usually finance projects where no competitive tender procedure has been implemented, competition in PPPs has often been limited.[20] The St. Petersburg Western High Speed Diameter case shows that where a tender results in only one bidder, IFI finance may still be forthcoming, in spite of the strong negotiating position for the bidder created by having no competitors.

Even when there are several bidders, the 'preferred bidder' stage, in which negotiations are carried out with one selected bidder to fine-tune the details of the contract, often results in an increase in the price or specifications of the project.[21] A survey of the capital costs of 15 English PFI hospitals at the Outline Business Case stage and at the contract stage shows an average increase in cost of 114.6 percent.[22]

Efficiency through meeting deadlines?

The other main justification for PPPs has been the idea that the private sector is more efficient at construction and providing services, but more and more evidence is emerging that many of the claims made for PPPs are false or based on questionable assumptions.

> It is commonly claimed that 88 percent of PFI schemes in the UK have been delivered on time,[23] whereas 70 percent of non-PFI projects were delivered late and 73 percent over budget.[24] However these statistics have been exposed as fictitious.[25]

An EIB evaluation of its involvement in PPP projects pointed out that PPP projects had resulted in on-time and on-budget completion as a result of the fixed-price, fixed-term turnkey construction sub-contracts, which could also have been applied to public procurement.[26]

Public services: Cutting costs or cutting corners?

Relatively little attention has been paid by PPP promoters to whether this transfer of traditionally public-sector functions to the private sector will benefit the delivery of services. There has, as the EIB's Armin Riess puts it, been "*a sometimes uncritical, if not ideological presumption that private sector participation in the provision of public services can do no harm.*"[27]

If the design, construction and operation of a facility are bundled together in a PPP contract, the private sector partner theoretically has more incentive to make cost reductions than if three separate companies were contracted by the public sector to perform each stage. However, cases from the UK suggest that margins are often already so high [28] that there may be little additional incentive to cut costs.

Neither is cost cutting always desirable, as it may decrease the quality of service. In theory, service provision can be maintained through contractual obligations and sanctions for non-performance. However contracts can never foresee all eventualities. This is particularly relevant for education, health, and prison services. Rail networks are also seen as unsuitable for PPPs due to the high need for public safety taking precedence over opportunities for cost cutting.[29]

Prison PPPs have often included some core services and have been highly controversial. Serious doubt has been cast on whether the provision of services in prisons by the private sector can be adequately measured, as the companies risk paying performance penalties whenever incidents such as assaults or the smuggling in of drugs take place in the prison, and there is therefore an incentive to under-report such events. Several PFI prisons in the UK also seem to have problems with recruiting and retaining suitable staff. [30]

It is not only in core services that PPPs have caused problems, but also in accommodation. Since PPPs are so expensive, there has been an average of 30 percent cuts in bed capacity and 20 percent reductions in staff in hospitals financed through PFI in the UK.[31]

The shortfalls caused by having to pay for the PFI hospitals also affect publicly-owned hospitals because PFI capital and service costs are to a large extent fixed, and it is therefore easier to make cuts in the **non-PFI hospitals. In other words, non-PFI public services suffer because of the affordability problems caused by PFI projects**.[32]

There have also been problems with the design and construction of PPP buildings. For example at the Princess Margaret Hospital in Swindon, UK, the recovery room is located 80 metres from the operating theatre.[33] Wider problems have been identified by the UK Commission for Architecture and the Built Environment (CABE), which found that 9 out of 10 of the most poorly designed schools in the UK were built under PFI.[34]

In spite of these weaknesses, sanctions have resulted in a low level of payment deductions:[35]

The contract for the National Palace of Arts in Budapest has been criticised for its failure to define penalties in case of underperformance by the project company.

> "...the UK experience also highlights the need to increase the means of effectively monitoring and influencing the performance of the private sector. To this end, credible sanctions, performance measurement and payment deduction provisions have to be designed and carefully implemented. Most importantly, contract termination must become a credible threat."[36]

It is hard to see how this can be done, as the public authority has an interest in the project company continuing to function. If the company collapses, the public authority will have to either re-nationalise the project, support the company or bear the expenses of re-opening the PPP.

In CEE this problem is likely to be even more acute, as experience has shown that monitoring capacity and enforcement is in general at a very low level in many CEE countries, whether for environmental, corruption, or other violations. It is therefore unrealistic to expect PPP performance standards to be strictly enforced.

PPPs should, therefore, be avoided for particularly socially or environmentally sensitive services such as health care, schools, prisons and water supply as there is a potential temptation to cut corners, and there are inadequate enforcement mechanisms to ensure that this does not happen.

Efficiency through risk transfer?

In theory, risks in PPPs are transferred to the party most able to limit and control the risk. In practice, however, whenever the private sector takes on risk it often charges considerable fees for doing so.

Poorly allocated risk has been one of the largest problems in CEE PPPs. Sometimes it has led to contracts guaranteeing profits at the cost of taxpayers (for example, the Trakia Highway in Bulgaria and Zagreb wastewater treatment plant in Croatia), while at other times it has led to financial problems for the concessionaire and subsequent attempts to extract income guarantees from the public sector.

A2 Motorway, Poland

The A2, linking Warsaw with Poznan and the German border at Slubice, is the largest transport project in Poland with the involvement of the private sector, and has a total financing need of EUR 870 million. A 150 kilometre stretch connecting Nowy Tomysl and Konin was awarded as a BROT (Build–Rehabilitate–Operate–Transfer) project in 2000 with a concession for 40 years. Construction began in 2001 and was completed by 2005, but few people are willing to pay the toll. At least 60–80 percent of trucks are estimated to bypass the tolled stretch of the highway. At the time of writing the government and the concessionaire are negotiating compensation payments.

The Nowy Tomysl - Konin stretch of the Polish A2 motorway, completed in 2005, has failed to attract the expected levels of traffic

The most problematic projects in terms of risk transfer in CEE are often toll highways.[38] The persistent over-estimation of traffic figures by CEE decision-makers not only leads to difficulties with the concessionaire's income or the public budget's expenditures, but also leads to attempts to actually increase the amount of traffic using the motorways,[39] in complete contradiction with the environmental objective of reducing road traffic.

Unfortunately, taxpayers always end up footing the bill, whether through guarantees for the concessionaire's income or though the renationalising of the project.

Excess profits through refinancing

Among the most scandalous aspects of PPPs has been the issue of re-financing gains. Re-financing involves the private partner paying off its original loan by taking out a new loan after the construction of the infrastructure is completed.

Since most of the risks for the project have been removed at this stage, financing is available at much lower interest rates than before the construction, and thus the price of the project decreases. However, the fee that the public sector has to pay is calculated to cover the original, higher price loan, and unless there are relevant clauses in the contract to include gains for the public sector from refinancing deals, there is a danger of excessive private profits. Several scandalous cases have arisen in the UK such as the Norfolk and Norwich Hospital in which the Octagon consortium gained GBP 82 million and the investors' rate of return increased from a predicted – and already high – 19 percent to 60 percent.[40] So far in CEE there has been little coverage of this issue, but nevertheless it needs to be considered.

Working for whose good? The role of the IFIs in PPPs

The World Bank has admitted it made a mistake in trying to insist on the employment of a foreign management operator in its Lviv water project

The presence of the IFIs in PPP projects should bring public benefits and deliver goods and services for affordable prices or tariffs, as well as ensuring commercial fairness to both the contracting party and the private sponsor and good financial standing for the bank.

IFIs should enter projects at an early stage in order to ensure that all project components have been included in the project, in order to avoid cost increases later. This was a particular issue, for example, in the Zagreb wastewater treatment plant and South Bridge in Riga.

IFIs should also play a key role in ensuring that a PPP is only chosen if it offers value for money. However, the EIB has stated that it does not normally review the Public Sector Comparator calculation[41] – a serious omission for a bank

that should work in the public interest. Neither does the EBRD regard itself as having a duty to ensure value for money for the public sector. It tries instead to be relatively neutral in order to avoid being drawn into controversy.[42] This is unacceptable for a public institution, which should not hesitate to ensure good value for money for the public.

Unfortunately there have been cases in CEE in which – far from ensuring that the public gets value for money – the IFIs have apparently pushed private sector participation as part of projects without any real justification and even on occasion without support from the relevant public authority.

Lviv water project – PPP, like it or not

In 2001 the World Bank approved a USD 24 million loan for the Lviv Vodokanal (LVK) water company to improve the regularity and quality of the city's water supply, and to institutionally strengthen the water company. The World Bank tried to insist that Lviv Vodokanal employ a foreign, private management operator, which the company objected to, and later this was changed to employing a foreign management advisor, which was also later admitted to have been ineffective.[43]

The World Bank's evaluation spells out the lessons learned:

"It is important for the Bank to carefully assess the merits of its demands on the Borrower when there are clear signs of resistance. In the particular case of the Bank's insistence that the Lviv Vodokanal employ a foreign, private management operator it was obvious that the Client did not favor such a solution. The subsequent substitute of a management contract by expensive, foreign management advisory services was not well advised either given the explicit, strong reluctance of the Borrower to employ a Management Operator.[44]

Recommendations

Given all the disadvantages of PPPs as outlined above, the number and type of projects for which they may bring real advantages is likely to be limited. CEE governments, IFIs, think tanks and consultants need to take a step back and consider whether their promotion of PPPs in the region may be encouraging unaffordable spending, placing a large burden on taxpayers, and crowding out alternative financing arrangements. The following recommendations aim to ensure that PPPs in the CEE region take place only where they are affordable and bring real benefits.

Affordability

- Considering the real danger of undertaking PPP projects which will impose a severe burden on public budgets in years to come, ceilings should be set on how much future taxpayers' money each government ministry or local authority is permitted to commit for PPP projects.
- The fiscal cost of past PPPs should be disclosed [45] before new PPPs are undertaken.
- The annual stream of future PPP payments should be published in government accounts. It must also be clear which budget the annual costs are paid from and what the cash costs to the government and the public will be.

Effect on public services

- PPPs should not be used in certain sectors due to the difficulty of measuring performance and the threat of a decline in service due to cost cutting. These sectors include the operation of hospitals, schools, and prisons, as well as public water supply and resources and railway networks.

Value for money

- When a decision is due to be taken on whether to undertake a PPP, this must be done on a level playing field, with other options open. Governments, IFIs and consultancy companies must not imply or dictate that PPP is the only possibility for a certain project. Where public funding for the project would not be an option, it is not likely that PPP would be affordable either, and, in this context, authorities should prioritise the most important projects, or scale down projects to a more affordable size.
- On the institutional level, this means that procurement should be approached as an integrated topic including a range of public and private possibilities, i.e. public authorities need to set up not centres of PPP expertise, but centres of procurement expertise in order to avoid a myopic focus on promoting PPPs where they may not be the best option.
- An affordability assessment for each project needs to be carried out and to be publicly available.[46] This must include a full assessment of the risks for users, taxpayers, workers and the government, including if the project fails.
- A Public Sector Comparator calculation must be carried out and the results must be made publicly available. The methodology for the calculation must be publicly available and explained, and must avoid overly flexible categories (such as 'risk transfer' in the UK PSC calculation) that can be easily adjusted to weight the calculation in favour of PPPs.

Transparency and accountability

- Draft PPP contracts must be published in order to allow suggestions for changes to limit fiscal risks before the contract is signed.
- In order to limit opportunities for corruption and the inflation of projects, all tender documents, bids and contracts, including financial details, must be published. So far these have usually been regarded as commercially confidential, but if the public is to get good value for money this practice must end.

Tender procedures

- Tender procedures must not only be carried out according to EU procurement rules but if there is only one bidder the procedure should be stopped, as there is an extremely low chance of obtaining value for money. If there is no evidence that a new tender would bring different results, the project should be redesigned.
- Ceilings need to be set for the maximum cost changes allowed during the preferred bidder stage, whether the changes are a result of new specifications or not. No substantial changes should be made to the contract, and

'substantial' needs to be clearly defined either at the EU or national level. The public sector also needs to have a clear strategy and clear triggers for walking away from the negotiations if the private sector becomes too demanding in other areas such as risk transfer or the penalty system. If major changes are made the PSC calculation should be done again and the tender procedure re-opened.

Contracts

- Fines for poor performance must automatically exclude the payment of bonuses for good performance in other areas.
- PPP contracts should always ensure that the public sector gains a minimum of 50 percent of any refinancing benefits, preferably with a ceiling for maximum gains by the private sector.
- The contract must include a clause allowing termination in the public interest in case of unforeseen circumstances.
- For road PPPs, payment must not be based on the expected level of traffic as this may lead to efforts to increase traffic volumes, contrary to EU climate targets and sustainable development policy. The private sector partner must bear a significant share of the financial risk of operating the road.
- Contracts must require compliance with environmental standards and labour standards, including union recognition.

Enforcement of contracts

- Public authorities proposing a PPP must show how they will ensure that they have adequate capacity and funds to enforce compliance with performance standards.
- If termination is to be taken seriously, the public partner needs to be aware of when it would be entitled to terminate the contract and must be prepared to use the powers. As part of its contract management procedures, the public sector should draw up and maintain contingency plans for contractor default, even when this is perceived unlikely. [47]
- Public authorities must carry out evaluations for all PPP projects, and these must be publicly available. This should happen twice: first, when the initial investment has been completed and the service has begun to operate, and second 4-6 years after operation has begun, in order to ensure that any problems can be minimised.

The role of the IFIs

The IFIs should:

- be more pro-active in ensuring that an affordability assessment and PSC calculation is carried out in PPP projects in which they are involved and that they rely on reasonable assumptions. As public institutions they should actively ensure that the public sector obtains value for money.
- ensure that the long-term cumulative impacts of PPPs and other public budget commitments are quantified and analysed for their constraints on future public spending
- ensure that public authorities release project documents such as the PSC calculation and methodology, the draft and signed versions of the contract, and information about affordability; this may entail a review of the criteria for withholding project information on the grounds of 'commercial confidentiality'.
- ensure that the public authority has adequately shown how it will monitor and enforce performance standards; where a public authority has low capacity to undertake such work effectively, the IFIs should not finance PPPs.
- consider lending to the public authority rather than the private partner in order to reduce the cost of financing, so that the decision on whether to involve the private sector will not be made on the basis of the potential to rely on off-balance-sheet accounting.
- lend only to those projects where other financing is not available on reasonable terms.
- ensure that all project components have been included in the project, in order to avoid cost increases later.
- set clear limits on the cost increases and specification changes that they are willing to accept during the preferred bidder stage, and be ready to walk away from a project if the public is no longer getting good value for money.
- carry out a publicly available evaluation – with the project named – for all PPP projects, and should consider doing two in order to allow the minimisation of problems that arise during the project. These could be timed as suggested above for the public authority's evaluations. Care should be taken to consult a range of stakeholders in order to ensure well-balanced analyses, and to include information which may not be particularly flattering.
- consider lending for public-public partnership projects for sectors such as water where management improvements are needed, for example where well-run municipal companies can be twinned with ones in need of capacity building.
- shift lending towards sustainable modes of transport, energy and waste management.

Notes

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"Discussions in central and eastern Europe have often concentrated on how to best implement PPPs rather than about whether to implement them at all. However, in their birthplace, the UK, PPPs have been fiercely criticised, raising the question of whether the countries of central and eastern Europe are in danger of rushing headlong – with strong promotional pressure – into using a discredited investment vehicle."

Center for Ecology and Sustainable Development (CEKOR)
www.cekor.org

Save Yuntolovo Public Environmental Movement
sos-yuntolovo.spb.ru

Transparency International – Czech Republic
www.transparency.cz

CEE Bankwatch Network
www.bankwatch.org