

PPP Resources

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The Value of a Proper Enabling Environment for PPP's in Infrastructure Investment and Development

Lloyd Richardson

About the Author



Lloyd Richardson is an attorney with 20 years' experience in Infrastructure Finance and Public-Private Partnerships who has been named to "Best Lawyers in America." He is currently an Advisor to the U.S. Department of the Treasury consulting on P3s for emerging market countries. Before practicing law, Mr. Richardson was in the U.S. Foreign Service, with tours in Taipei and Washington, D.C., and speaks fluent Chinese. Mr. Richardson has written extensively on Asia and has been published in *Policy Review*, a journal of the Hoover Institution at Stanford University.

Abstract

Why do I need a special statute to do PPP projects? This article addresses why so many governments expend the time and effort to develop a specific regulatory framework for PPP, and discusses some of the implications for attempting PPP projects under traditional procurement mechanisms.

Rationale for Specific Statutes for PPP Procurement

Clients often ask, "Why do I need a special statute to do Public-Private Partnership projects?"

The general answer is that they do not - *assuming* the governmental entity undertaking the project has the power to do so under its enabling act or general law, it can undertake a Public-Private Partnership ("PPP") project—in fact it can undertake any number of PPP projects.

Why then do so many governments expend the time and effort to develop and seek legislative enactment of a specific regulatory framework for their PPPs, including both a PPP statute and, typically, detailed implementing regulations as well? The answer lies less in legal than in political and business considerations.

Time and cost considerations

Consider the goals and objectives of using PPP projects. One important goal is to reduce the time and cost involved in implementing and maintaining projects through the traditional governmental procurement process. This goal is closely related to a second goal that governments have in using PPPs: they want to be in a position to see a large number of aggressively-priced, high-quality proposals, submitted competitively from the private sector for projects that will benefit the public.

If a PPP project opportunity is developed on an *ad hoc* basis, the project may be able to be tendered through the traditional government procurement process- notwithstanding that it is a PPP. In most if not all jurisdictions, a project bid out in this fashion will be subject to rules regulating the use of organized labor on government projects. This in turn means that labor on the project will have to be paid at the highest possible wages, rather than wages determined by the marketplace. This obviously drives up the overall cost of the project. For example,

in the US, the most recent major transportation project done as a PPP is the I-595 redevelopment done by the State of Florida, which achieved financial close in the spring of 2009. In that case, the winning private bid came in at just under \$1.8 billion, and the bidder agreed to complete the project in five years; by contrast the State Department of Transportation estimated that if it had done the project itself, the cost would have been nearly \$2.1 billion and would have taken 12 years to complete. The time savings illustrates another problem with the use of organized labor on a project: being subject to union rules, the contractor loses substantial flexibility in scheduling the pace at which the project is completed. The resulting delay in project completion will almost certainly drive up the overall cost of the project as well, inasmuch as both labor and material prices tend to rise over time. All of these factors in turn conspire to drive up the price of bids.

Transparency

But if we set aside normal government procurement rules, what set of rules is to take their place? Procurement rules exist for good reason, mainly to ensure transparency. Under effective procurement rules, all bidders know they will be treated fairly, in accordance with a single set of criteria (burdensome though they may be). Fair treatment of all bidders maximizes the number of bidders who will participate in the process, which increases competition and lowers the pricing of a project. Fair treatment reduces cost in a second way as well. If bidders understand the rules and feel they are fairly treated, they are less likely to file a protest or sue the government—with all the time and expense that that eventuality will entail. Finally, fair treatment of bidders reassures the public that their government is not allowing itself to become corrupted through these interactions with the private sector. Corruption itself, where it exists, represents an additional, albeit hidden, project cost.

This much is Procurement 101 and should be obvious. The key point here however is that it is not enough simply to declare a project to be a “PPP” and therefore exempt from procurement rules. Some framework must be put in place to replace or amend those rules. This explains in part why a dedicated PPP statute is often desirable. Countries as diverse as South Africa, Chile, Slovenia, and the UK have taken this approach. In the United States PPP statutes are enacted at the state level; of those now in effect, Virginia has one of the best recognized, where the statute has provided the framework for nearly 100 PPP projects of all types.

Dealing with Unsolicited PPP Proposals: Key Considerations

In the context of bids solicited through some type of competitive bidding process, one would expect the rules applicable to PPP projects to look very similar to the traditional procurement rules; after all, they aim to accomplish the same objectives. But what about *unsolicited* proposals?

Many advocates of PPPs would suggest that the ability to handle unsolicited proposals represents the real power of PPPs and is the characteristic of PPPs that most distinguishes them from traditional government procurement methods. In the unsolicited proposal, a private company takes it upon itself to figure out an often novel way to approach a particular problem. In some cases, it may be a problem that the government, with its limited resources, has not even thought to address. Typically, the private bidder takes on not only the design and implementation challenges of the project, but how it is best to be financed. To do all this of course, the proposer will have to invest substantial amounts of its own resources, both financial and intellectual, in the project before it even knows whether it will win the bid. But for this to occur, the proposer must have a high degree of confidence, in submitting an unsolicited proposal, that its interests will be

carefully protected from competitors. These considerations cry out for confidentiality and back room deals, and fly directly in the face of government's and the public's desire for transparency.

It is in these situations that a PPP statute can prove invaluable. Through the PPP mechanism established under such a statute, a government can balance the need for transparency with the need for confidentiality. This balancing is generally accomplished by giving public notice that the proposal has been received by the government and inviting competing bids. That notice however will prescribe a relatively short time period for competing proposals. At the same time, the original proposer's proprietary information will be carefully protected. Thus the original bidder still retains some advantage in the competition, but the ensuing process will be undertaken under public scrutiny. From the perspective of the original proposer, knowing that there may well be competing bids, it will want to keep its pricing aggressive in the initial proposal; at the same time, knowing that competitors will have a relatively short time to work up a competing proposal, the original proposer will have a reasonable chance to win the project, and so will not be deterred from making its proposal in the first place.

Conclusion

We have said that a well-designed PPP statute can provide certainty for bidders as well as the public. But it can also provide certainty for one other critical player in any successful PPP project—the credit markets. The credit markets, and the diverse elements within them, are more likely to get involved in a project when it is clear that the government sponsor is organized to deal effectively with the PPP process and that local law protects the creditors in that process. Well-written PPP statutes reassure potential creditors on both counts. And over time, as the regulatory framework is shown to accomplish its goals, potential creditors will look forward to the opportunity to invest in such jurisdictions.

Please address questions about this article to the author at Richardson.lloyd@gmail.com.

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