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FISCAL RISKS: BEST PRACTICE IN THE OECD

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OECD
BETTER POLICIES FOR BETTER LIVES

The promise of PPPs

- Well-designed projects
  - On time and within budget
  - Innovation (from bundling stages)
  - Private sector expertise (financing/project management)
  - Whole-of-life approach (maintenance)
  - Output-based approach

PPPs outperform TIP on timeliness, construction cost and quality but transaction costs are higher

Based on the general experience of your government, **how do PPPs perform relative to traditional infrastructure procurement** with regard to the following dimensions?

	Better than TIPs	The same as TIPs	Worse than TIPs	Not enough data
Timeliness e.g. being completed on-time/according to projected deadline	14	1	0	2
Construction cost e.g. projects completed on or under expected budget	12	2	0	3
Operating cost e.g. projects operate on or under expected budget	7	3	1	5
Quality of the finished project e.g. projects comply with code, innovations, etc.	10	3	0	4
Transaction costs	4	1	7	4

PPPs remain a complement

For the 2011 fiscal year, what **percentage of public sector infrastructure investment** flow (total asset value, public and private components included) took place through PPPs?

Australia	>10% - 15%	**Korea**	>5% - 10%
Austria	No PPPs	**Luxembourg**	>5% - 10%
Canada	>1% - 3%	**Mexico**	>15%
Czech Republic	>0% - 1%	**New Zealand**	>1% - 3%
Estonia	No PPPs	**Norway**	>3% - 5%
Finland	>10% - 15%	**South Africa**	>3% - 5%
Germany	>3% - 5%	**Spain**	>3% - 5%
Hungary	No PPPs	**Sweden**	No PPPs
Italy	>1% - 3%	**Switzerland**	No PPPs
		UK	15%

P. Burger & I. Hawkesworth. 'Capital Budgeting and Procurement Practices'. OECD forthcoming (2013)

OECD Principles

- Three overarching considerations

1. Institutional framework
2. Value for money
3. Budgetary transparency

- Need involvement throughout the process

Desirable features when building capacity

- Create a consistent, clear and predictable legal/regulatory framework
- Make PPP expertise available
- Ensure that there is underlying value for PPP projects
- Ensure a value for money criteria for selecting PPP
- Prepare the projects to a sufficient level of quality
- Build a dialogue with the private sector; needs and limits
- Start with a relatively simple projects and build gradually
- Establish a pipeline of projects

Public sector vulnerabilities

- Fiscal space
  - Availability payments
  - Viability gap payments
- Contingent liabilities
  - Re-negotiation
  - Contractual terms
  - Guarantees
  - Provider of last resort

Project selection

- Infrastructure/strategic plan
- Robust CBA
  - Compare with other approaches and ensure a value for money perspective
  - Consider as public sector “due diligence”
- “Depoliticise” choices
- Budgetary implications
  - Avoid bias towards selecting PPPs (cash-flow basis, off budget)

Value for Money tests are often used, but more so for PPPs

Table 13. In general, does your government apply an absolute value-for-money analysis (such as a cost-benefit or cost effectiveness analysis) and/or relative value-for-money analysis (such as public sector comparators) that takes a whole-of-life (net present value) approach to prospective capital projects? (Select the most relevant option.)

Absolute value-for-money assessments (e.g. cost-benefit analysis)	PPPs	TIP
Yes, for all projects	8	5[1]
Yes, for all those above a threshold	2	7[1]
Yes, on an ad hoc basis	4	9
No	2	1
Other	3	4
Relative value-for-money assessments for PPPs (e.g. public sector comparator)	**PPPs**	
Yes, for all projects	12	
Yes, for all those above a threshold	3	
Yes, on an ad hoc basis	1	
No	1	
Other	2	

Motives for doing PPPs may be mixed

Do the following make PPP more attractive in comparison to TIP?

	The project generates debt that is not on the balance sheet of government	The project requires high level of constant maintenance	The project requires a high level of service delivery performance	The project requires skills that are more readily available in the private sector, compared to the public sector
Yes	*5*	10	12	10
No	*9*	2	0	2
Sometimes	*4*	6	5	6
Not answered	*3*	3	6	3
Total	*21*	21	21	21

P. Burger & I. Hawkesworth. 'How to attain value for money'. OECD Journal on Budgeting, No. 1, 2011

Budgeting transparency

- Explain the nature of PPPs to Parliament
- Make terms of the contract public to the extent possible
  – Including substantial changes to contracts
- Reduce incentives for shifting off budget
  – Appropriate accounting
  – Interaction with fiscal rules
  – Difficulties in accounting for guarantees

Assessing the fiscal consequences

- Report PPPs – cover the whole of the public sector
  - On or off balance sheet, supplementary annexes, separate summary documents
- Medium and long-term budgeting,
  - Report contractual payments during the project life, including end-of-contract costs
  - Present how PPPs fit in long-term fiscal strategy report
  - Show debt/debt servicing scenarios
- Annual PPP/Concession and contingent liability report
  - Quantify or explain
- How will these affect fiscal space?

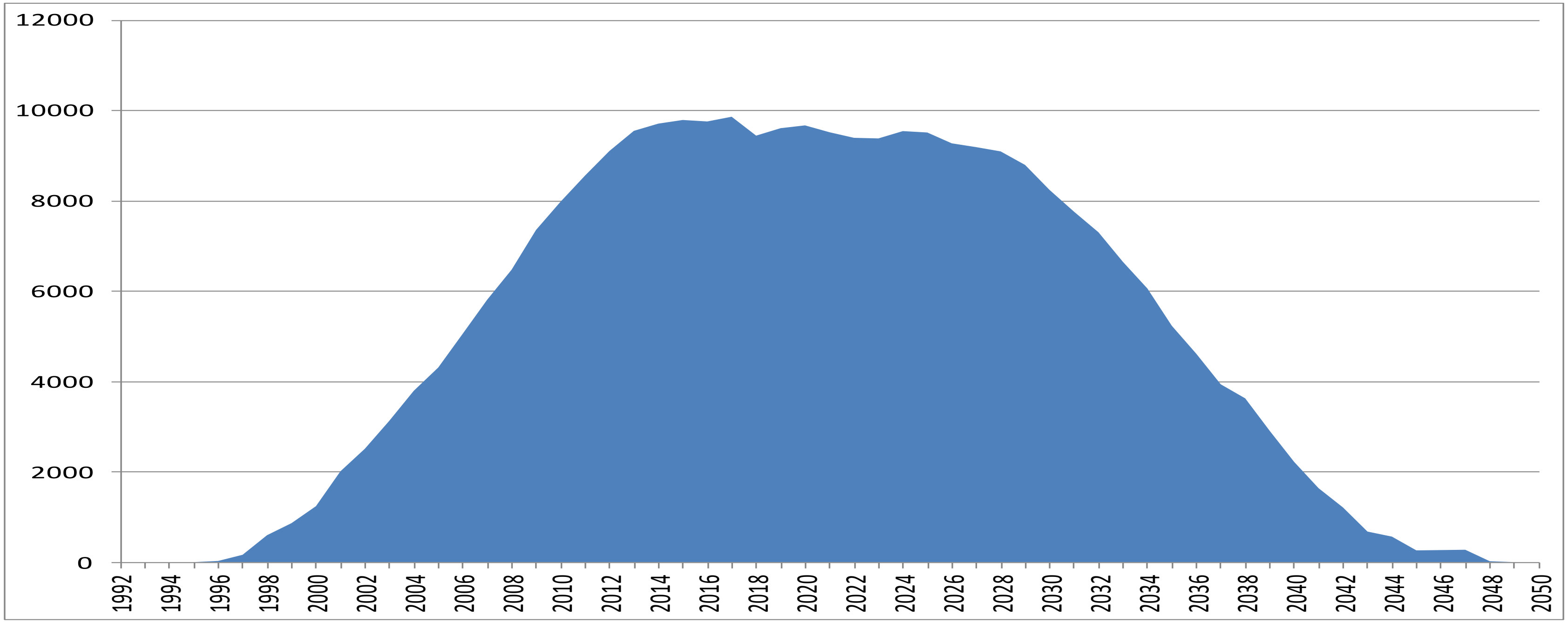
Affordability: Demonstrate the project fits into the budget and medium-term plans

Should a government department demonstrate that a new infrastructure project **falls within its existing budgetary envelope** and expected medium-term resource allocation before it can proceed?

	PPPs	TIP
Yes always (100% of the time)	13	16
Yes very often (>75, but <100% of the time)	2	4
Yes often (>50-75% of the time)	0	0
Yes sometimes (>25%-50% of the time)	1	0
Yes rarely (>0, but <25% of the time)	0	0
No, not required	2	2
Other, please specify	2	1

The implications for fiscal space can be long-lasting

PPPs can demand **considerable fiscal space** as they are **Long term** obligations with **limited flexibility.** Thus requiring **public budget affordability analysis.**



Total unitary charges of UK PFI projects of all projects signed as of November 2011 (GBP millions)

M Treasury, "PFI Signed Projects List" http://www.hm-treasury.gov.uk/ppp_pfi_stats.htm

Budget execution – key issues

- The main responsibility of budget execution is the procuring ministry/agency
- The central budget authority (CBA) should assess potential risks and monitor problematic projects
- The procuring agency, CBA, PPP Unit should have the requisite skills
- Data should be collected for use in subsequent procurement processes
- Performance information should be made available to the political level, the public.
- Budget execution reports should cover PPPs, concessions

Minimising fiscal risks: Contracting

- Need capacity to contract
  - Strengthen the legal and regulatory framework
  - Establish centralised support units
  - Consult independent bodies
- Contract terms
  - Not suitable when technology and demand conditions change rapidly or are hard to forecast

Minimising fiscal risks: Renegotiation

- Opportunistic behaviour a common problem
  - Provider of last resort weakens government's bargaining position as private sector seeks to increase allowable costs, raise user fees, etc.

- Contracts:
  - Specify conditions when renegotiation is allowed
  - Place limits on private sector debt
  - Specify how to share upside and downside risks
  - Reduce planning and environmental licensing uncertainties

Further lessons

- Learn from experience
  - Build in ex post review and feedback
  - The supreme audit institution should have a role in assessing PPPs
- Encourage greater competition
  - Open bidding and establish project pipeline
    - Danger when quality poorly observed, but important component of costs

THANK YOU

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