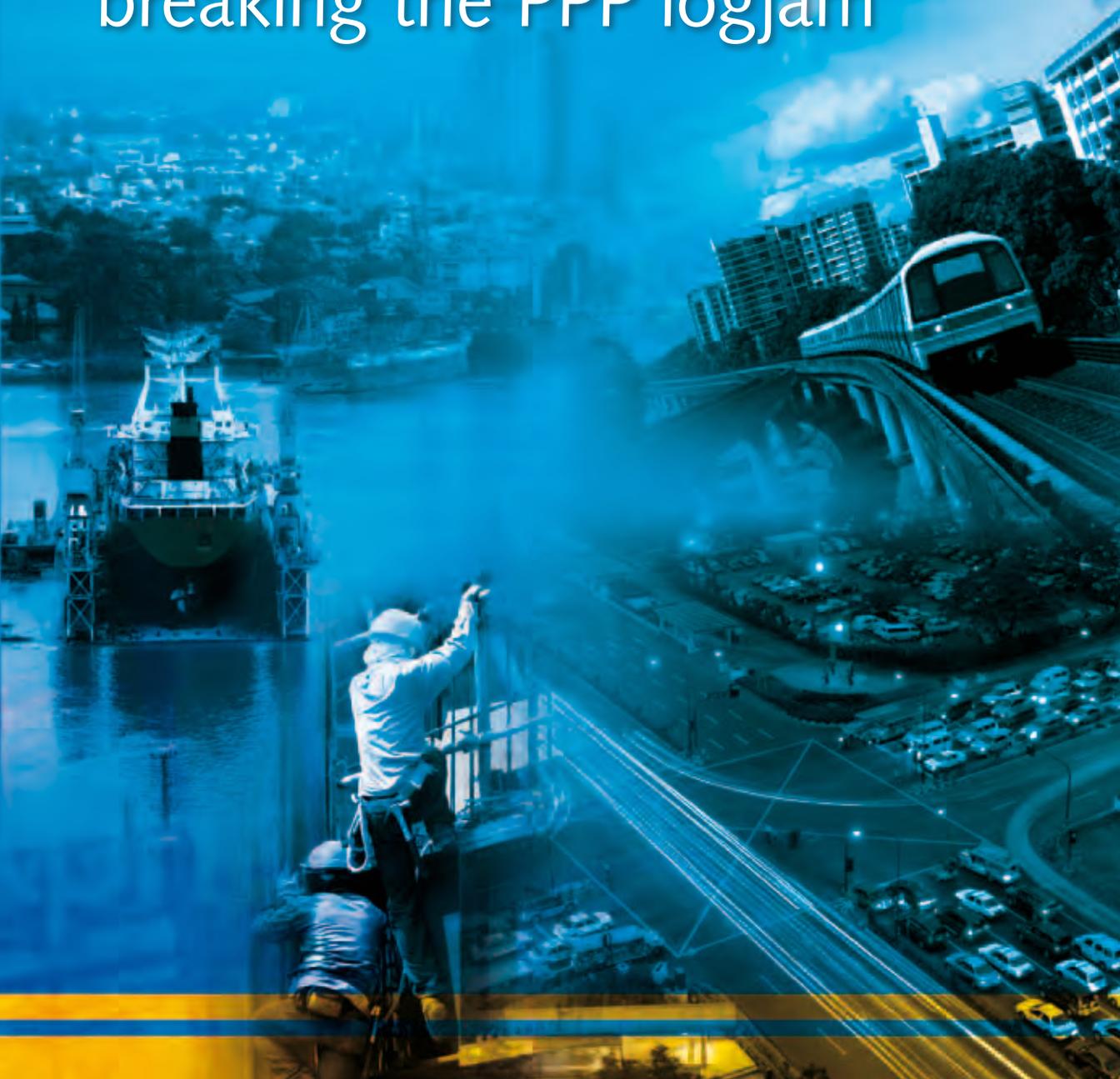




Asia-Pacific
Economic Cooperation

Meeting APEC's infrastructure challenge: breaking the PPP logjam



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Report prepared for the 17th APEC Finance Ministers' Meeting, Kyoto, Japan

6 November 2010

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Foreword

Meeting the present and future infrastructure needs of the APEC region is a formidable undertaking. A large and growing gap now exists between needed infrastructure and the availability of financing for investment in new projects. The scale of this challenge is so large that it will require the contribution of both the public and the private sector in order to be met.

Both emerging and advanced economies within the region are affected by this challenge and are under increasing pressure to deliver quality infrastructure in the most efficient, timely and cost effective manner possible.

This report is the result of work undertaken by member economies during 2010 through the APEC infrastructure pathfinder initiative. The program of capacity building and knowledge sharing was delivered jointly by the Australian Treasury, the Indonesian Ministry of Finance and the Thai Ministry of Finance. The World Bank also provided invaluable technical support for this initiative.

The report raises a number of key issues for consideration by APEC Finance Ministers. There is the important technical issue of achieving optimal risk transfer outcomes in public private partnership (PPP) infrastructure projects. Pressing implementation issues also need to be addressed as only a small number of PPP projects in emerging APEC economies have been brought to completion in recent years.

In order to continue to address these complex and difficult challenges, we urge APEC Finance Ministers to support an 'APEC Pilot PPP Mentoring Scheme' in 2011, as a joint initiative of Australia, Singapore and the World Bank. This scheme will provide hands-on technical training and impartial expert advice to officials working on developing and implementing actual PPP projects in emerging APEC economies.

The pilot scheme is designed to lead to a notable increase in the number of PPP infrastructure projects that are delivered within the Asia-Pacific region. Such a contribution would be a big step in meeting APEC's infrastructure challenge and thus helping unlock the region's vast potential.

We commend this report to our colleagues.



The Hon Wayne Swan
Deputy Prime Minister and
Treasurer, Australia



The Hon Agus D.W. Martowardojo
Minister of Finance, Indonesia



The Hon Korn Chatikavanij
Minister of Finance, Thailand

Acknowledgement

Our key partners in the delivery of the APEC infrastructure pathfinder initiative provided invaluable support in developing the capacity building program and in ensuring that on-the-ground delivery of each workshop was highly successful. They were also instrumental in the preparation of this report.

In this regard, we extend our sincere thanks to the Indonesian Ministry of Finance, the Thai Ministry of Finance and the World Bank Singapore Hub. We also wish to thank the Monetary Authority of Singapore and the Singapore Ministry of Finance.

The initiative would not have been a success without the enthusiasm, knowledge and hard work of participants from each of the following economies:

■ People's Republic of China	■ Philippines
■ Chinese Taipei	■ Russia
■ Indonesia	■ Thailand
■ Papua New Guinea	■ Vietnam
■ Peru	

We would like to thank key resource people and eminent experts in the field of PPP infrastructure projects from the following organisations:

■ Asian Development Bank (ADB)	■ Leighton Contractors
■ APEC Business Advisory Council (ABAC)	■ Linking Melbourne Authority
■ Department of Treasury and Finance, Victoria (including Partnerships Victoria)	■ Macquarie Bank
■ Infrastructure Australia	■ P3 Canada
■ International Monetary Fund (IMF)	■ Plenary Group
■ Japan Australia Business Council	■ PricewaterhouseCoopers
■ Japan Bank for International Cooperation	■ World Bank (Jakarta)
■ Korean Ministry of Strategy and Finance — PPP Policy Division	

In particular, we would like to extend our thanks to Mr Mark Johnson of ABAC and Mr Kamran Khan of the World Bank for their ongoing support of this initiative and for their constructive comments at many points along the way. We would like to thank the numerous members of the Steering Committee for this project who provided invaluable assistance in helping to shape the pathfinder in its initial stages.

Thanks are also due to the APEC Secretariat, the Chinese Taipei Economic and Cultural Office, the Consulate General of Japan (Melbourne), the Japanese Ministry of Finance (and the SFOM Chair), the Melbourne Convention Centre, and the US Embassy (Jakarta and Canberra).

The Australian Agency for International Development generously provided the funding support for the APEC infrastructure pathfinder initiative and for the publication of this report.

The Australian Department of Foreign Affairs and Trade provided advice and guidance on issues relevant to the development of this initiative within the APEC process.

We are very grateful to our consulting partners Ernst & Young for their hard work and expertise in delivering the capacity building components of the initiative and for their invaluable contributions to the contents of this report.

We also wish to thank Mr Kula Subramaniam, Managing Director of Just Change Management Consultants, Malaysia, for his key role as expert facilitator at each of the capacity building workshops.

This report was prepared by Mr Liam Findlay and Mr Nathan Wonder under the leadership of Mr Leslie Williams. Overall guidance and direction was provided by Mr Bill Brummitt. All are staff members of the Australian Treasury.



Executive summary

The Asia-Pacific region has considerable unmet infrastructure needs. To fill this growing infrastructure gap, it has been estimated by the Asian Development Bank that the region must spend a further \$US8 trillion over the next 10 years on critical energy, transport, communications and other physical and social infrastructure.

Both emerging and advanced economies share this challenge. Fast growing emerging economies need to expand both physical and social infrastructure if growth is to be sustained. Advanced economies need to lift investment rates to sustain and boost growth. In particular, they need to update their aging infrastructure stock and invest in new energy, transport and information technology projects.

To help meet this infrastructure challenge, the APEC infrastructure pathfinder initiative was launched by APEC Finance Ministers at their 2009 meeting in Singapore, aimed at developing a harmonised road map for private sector infrastructure provision.

The initiative, which was delivered in 2010, highlighted that development of public private partnership (PPP) infrastructure markets was an evolutionary process and that economies should not be too ambitious in the early phases. A key step to building market credibility was to deliver one or two key projects.

In the face of strong interest from participating economies in risk transfer issues, discussions among officials and experts also highlighted that guarantees and support from multilateral development banks could be important in the early stages of PPP market development. However, the initiative also developed greater recognition that economies need to maintain a focus on increasing risk transfer as market development occurs. A mature PPP market will see greater value captured by the public sector from a wider range of projects and a growing stock of efficient and well maintained infrastructure that will support growth.

Discussions among officials and experts also highlighted the implementation challenge in actually developing PPP projects, despite all the conferences, courses and capacity building in the region. The scale of this implementation challenge is illustrated by the fact that despite the massive infrastructure needs in emerging APEC economies, only a handful of true PPP projects have been brought to completion in recent years. Factors exacerbating this challenge include: the lack of 'hands-on' experience within many emerging economies at negotiating and delivering PPP projects; and the understandable concern about where Ministers, and others with 'sign off' responsibility on major PPP projects, can go to get impartial advice on complex PPP issues.

To help address this implementation challenge, APEC Finance Ministers' are urged to agree to a Pilot PPP Mentoring Scheme in 2011. This scheme will be a joint initiative of Australia, Singapore and the World Bank. It will involve working with a group of targeted emerging APEC economies to identify and successfully implement prospective PPP projects.

The scheme will seek to provide hands-on technical assistance and advice from Australian experts to remove the impediments to project implementation and to develop strategies for the effective and timely delivery of these projects. The scheme could be evaluated in 2011 at the Honolulu Finance Ministers' Meeting and further decisions on its future taken.

1. Introduction

APEC's infrastructure challenge

The Asia-Pacific region has considerable unmet infrastructure needs. It has been estimated by the Asian Development Bank (ADB) in its well known report *Infrastructure for a Seamless Asia* (2009) that the region must spend a further \$US8 trillion over the next 10 years on critical, energy, transport, communications and other physical and social infrastructure to address its growing infrastructure gap. Rapid growth in the region (that has outstripped the pace of new investment) has created this infrastructure gap and has also led to significantly increased pressure on existing infrastructure. Bottlenecks have emerged which are restraining economic growth. This is a threat both to the sustainability of growth in the region and to continued development and poverty reduction.

The ADB has also noted the significant variation in infrastructure quality within the region. While many advanced economies have infrastructure that is world class, many emerging economies most in need of infrastructure for growth and development do not. Clearly, emerging economies do not have sufficient access to needed sources of infrastructure finance (both public and private).

This is not to say, however, that infrastructure investment is only an issue of relevance to emerging economies. Many advanced economies are faced with a number of challenges of their own. Large investments made in infrastructure in the post World War II period are now in need of renewal, and investments in new power generation (particularly from sustainable sources) and to underpin the growth of cities is also required. The need to invest in new information and communications technology, as economies seek to remain competitive in an increasingly globalised world economy, is also pressing. Infrastructure therefore is an issue of universal importance to APEC economies.

In addition to investment in new infrastructure, better use of existing infrastructure also remains highly relevant. This may require reform to the regulatory environment in order to better facilitate access to infrastructure and maximise efficient usage.

The importance of infrastructure for strong and sustainable growth

The 2010 IMF report, *The G20 Mutual Assessment Process — Alternate Policy Scenarios* highlights the importance of infrastructure to sustaining growth. The report outlines various alternate policy scenarios which, if pursued by G20 economies in the wake of the recent crisis, will result in either a baseline, low or high growth outcome. A critical element of the high growth outcome is greater infrastructure spending to address supply bottlenecks in high growth economies.



In the high growth scenario, the IMF reports that a gradual increase of government investment in infrastructure (and enhanced social safety nets) in the emerging Asia region will increase domestic demand within the region and also improve growth outcomes in the rest of the world. Employment gains within the high growth scenario would also be significant across regions. An estimated 8 million more jobs would be created in advanced economies — over 21 million in emerging Asia and the rest of the world — and global employment would rise by around 30 million jobs. This would lift an estimated 33 million people out of poverty, according to a companion World Bank Report, *G20 and Global Development* (2010).

Fiscal constraints to new infrastructure investment

In many economies, demand for new infrastructure projects is growing. In addition, there is rising pressure for funds to renew, maintain and operate existing infrastructure. Competition for such funding is often intense, not just between infrastructure projects, but also with the many other demands on public sector finance.

The IMF Fiscal Monitor (May 2010) highlights the extent of the fiscal challenge facing a number of economies, both advanced and emerging, that has the potential to limit the amount of public funding available for needed investment in infrastructure. Particularly for advanced economies, the recent crisis has led to large deteriorations in balance sheets due to the combined impact of automatic stabilisers and large fiscal stimulus packages. A number of advanced economies are also faced with significant structural challenges to their fiscal positions, such as population aging. Although emerging economies have not experienced the same deterioration in balance sheets as advanced economies, the deterioration they have experienced has still been substantial, particularly in the context of the large infrastructure requirements they require to sustain growth. These economies will also remain exposed to interest rate and growth shocks as a result of negative fiscal spillovers from advanced economies.

The way forward

For the APEC region to remain a reliable engine of growth within the world economy, increased investment in infrastructure (particularly among emerging APEC economies) must be made. Such investment would strengthen development outcomes by eliminating bottlenecks and other supply side constraints that act as a drag on the region's growth.

In order to achieve this, infrastructure needs to be delivered as efficiently and as cost-effectively as possible. Increased involvement of the private sector in both the financing and delivery of infrastructure will be a key part of the solution to this challenge.



PPPs can contribute to filling APEC's infrastructure gap

One means through which governments can overcome funding challenges and meet quality improvements demanded by the public is through private sector involvement in the provision of infrastructure. The need to address funding gaps and the increased focus on service delivery has provided the catalyst for the development and implementation of public private partnerships (PPP) across the world.

Benefits of PPPs

PPPs, if implemented successfully, can provide an alternative and sustainable option for the financing of infrastructure development, taking pressure off already strained public sector balance sheets.

It is also recognised, however, that PPP delivery structures offer a number of wider economic benefits in addition to helping governments overcome financing gaps. These include:

Value for money: PPP projects can often deliver greater value for money compared with an equivalent asset being procured conventionally. Value for money is driven by:

- **Risk transfer:** Transferring to the private sector those risks that it is better able to manage, which typically include most risks associated with design, construction, operation, and finance;
- **Asset utilisation:** Transferring the design and management of an asset to the private sector can reduce cost to government through potential third-party utilisation and/or more efficient design by the private sector;
- **Innovation:** The requirement that services are specified in terms of payment for a specified output, on which performance can be measured, has been linked to improved quality and timing of delivery. This process allows a wider opportunity to develop innovative solutions and contrasts with the conventional approach to public procurement that is based on pre-determined funding of inputs;

- **Whole of life cost recovery:** The time profile of PPP projects provides scope to recover costs of the initial investment, develop alternative approaches to service delivery and focus on costing over the whole life of the project; and
- **Competition:** Effective price-led competition is a significant driver of value for money.

New facilities provided efficiently and effectively: Usually, the private sector will not receive any payment until the facility is available for use. The PPP contract structure fosters the use of construction and procurement methods that encourage efficient completion and minimise the risk of defects.

Innovation and spread of best practice: The expertise and experience of the private sector encourages innovation, resulting in reduced costs, shorter delivery times and improvements in functional design, construction and facility management processes. This can improve service standards in the provision of infrastructure.

Flexibility: PPPs have in-built flexibility and can be introduced successfully to most types of infrastructure. The principles that underpin PPPs can also be adapted to many situations.

Timeliness: PPPs have demonstrated that, when managed well, they can deliver projects sooner than other methods.

Despite the known benefits of PPPs, it is important to recognise that PPPs are not the only solution available to governments facing a shortage of funding for infrastructure. They involve a number of costs and are best used as one part of an overall infrastructure development strategy.

Potential costs of PPPs

It is important to ensure that potential PPP projects are analysed, selected, structured and procured thoughtfully to preserve public interests.

It can often be difficult to balance the need to preserve the public's interest while working hard to attract private participation. Governments should remain mindful of the possible costs of PPPs, including:

- PPPs are a new and developing form of procurement for many Governments within the region. The development of a functioning PPP market requires a significant upfront commitment to



policy and legislation as well as investment in building the necessary skills and capacity to implement projects;

- this investment is not only required on the public side of a PPP transaction. The private sector must also invest in understanding the delivery of infrastructure through PPPs as opposed to simply working as a contractor to government;
- there are large transaction costs in setting up and managing a PPP, so the project needs to be of a sufficient scale to justify these costs;
- if the release of tenders to the market in a particular jurisdiction is not co-ordinated, it can result in unreasonable demands (and additional costs) for bidders;
- if the private party makes a successful bid which proves not to be financially viable, there may be reputational and financial consequences for the government involved;
- reliance on PPPs to fill infrastructure gaps may distort a government's priorities — the projects that proceed may be those that have the highest returns, rather than those that offer the greatest wider economic (and social and environmental) benefits;
- for some projects, PPP delivery may be viable, but it may nevertheless offer worse value for money than traditional delivery. Of course, this is only a concern if traditional delivery could be funded by government, but nevertheless, it is an important consideration; and
- recruitment, development and retention of high quality government project team members are necessary.

Capacity building to achieve commonality of best practice in PPPs

Although PPPs are not the only policy solution to addressing APEC's infrastructure challenge and, in some cases, may not be the best answer, they do have the potential to make a significant contribution. A number of economies within the region (although predominately advanced) have successfully used the PPP model to deliver infrastructure projects. In the last year alone (2009-2010) there has, despite the impact of the global financial crisis, been over US\$8.5 billion of investment through PPPs across Australia, Japan, Singapore, the Republic of Korea, and Vietnam (one project approximately \$US1 billion). Projects are as varied as a major transport expressway in Vietnam, the Singapore Sports Hub, and a desalination plant in Victoria, Australia.

In addition, as PPPs are complex transactions for which much experience lies within advanced APEC economies, this is a policy area that is well suited for cooperation, knowledge transfer and capacity building. Such work could lead to a greater up-take of best practice processes and the achievement of improved outcomes in PPPs for a greater number of APEC economies.

It is with these considerations in mind that the APEC infrastructure pathfinder initiative was launched by Finance Ministers in Singapore in 2009.



2. Outline of the APEC infrastructure pathfinder initiative

Background

APEC Finance Ministers have been alert to the scale of the region's infrastructure challenge for some time and have responded to this challenge with an increasingly sharp focus.

In 2008 at their meeting in Trujillo, Peru, Finance Ministers recognised PPPs as a means of meeting the infrastructure requirements of both emerging and advanced APEC economies. Ministers also welcomed a set of common principles that APEC economies could use as a reference when formulating guidelines to developing well-functioning PPP markets. These principles cover issues such as:

- developing robust quantitative and qualitative methods for identifying and assessing possible PPP projects;
- property rights frameworks;
- adequate allocation of risks;
- establishing dedicated PPP units with broad mandates;
- adopting flexible, streamlined and transparent tendering processes; and
- removing barriers to institutional investment in non-government debt and equity markets.

To elevate their response to the infrastructure challenge, Ministers agreed during their 2009 meeting in Singapore to work together to improve the policy settings that help infrastructure markets operate more effectively. In recognising the important role that PPP models could play in bridging the region's infrastructure gap, Ministers called on economies to develop greater commonality of best practices in the delivery of PPP projects. Effectively, this would provide a means of developing a harmonised road map for private infrastructure provision and would help decrease project bidding costs for contracts, reduce government transaction costs, increase competition, facilitate greater flows of finance across borders, and fast-track projects to a "bankable stage". These issues were outlined in more detail in the Australian Treasury commissioned report, *Meeting APEC's Post Crisis Infrastructure Challenge: Towards Commonality in PPP Infrastructure Markets*, which Ministers endorsed in Singapore.

APEC Finance Ministers also agreed to undertake the APEC infrastructure pathfinder initiative in 2010 to provide capacity building to assist emerging APEC economies.

Overview

The APEC infrastructure pathfinder initiative delivered targeted capacity building to a number of developing APEC economies. Representatives from international financial institutions as well as from relevant organisations from 16 of the 21 APEC member economies contributed to the initiative as participants, experts, resource people or observers.

This initiative was designed to identify established best practices in specific areas of PPP infrastructure project development and implementation, with the aim of assisting targeted economies to improve project implementation and financing arrangements.

The pathfinder was delivered in three phases covering a workshop held in Jakarta in May 2010, an intervening period where participants tested options and strategies with major stakeholders within their home economy, and a final workshop held in Melbourne in August 2010. A brief outline of the two workshops is provided below. The Appendix to this report provides a more detailed discussion of the elements and outcomes of the pathfinder.

Jakarta workshop

The Jakarta workshop provided the opportunity for economies to explore common best practices in PPPs and focussed on three key aspects:

- **PPP procurement:** Considering the elements of established best practice in the PPP procurement approach, including the establishment of centres of excellence to leverage experience and standardise procurement approaches, capacity building to ensure adequate resourcing during procurement, and measures to increase market awareness of PPP procurement processes;



- **PPP project development:** Analysing each of the key stages in developing a project and processes used internationally in project development, and covering the use of business cases, procurement options analysis, and standardising processes and frameworks; and
- **PPP project management:** Focusing on the procurement stages of a PPP, including detailed proposal development, evaluation, short-listing and negotiation, and contract management.

The Jakarta workshop also outlined critical success factors for PPPs. Economies considered a number of critical success factors, and coalesced around project selection and implementation, political commitment, legislative frameworks, risk allocation and transparency.

Project selection: Economies, particularly those in early-stage development, found it difficult to implement a suitable process for project selection. They expressed concern that projects that were unsuitable as PPPs were often procured without an adequate understanding of project feasibility, economic viability or sustainability. Governments need to identify those sectors and projects that should take priority in the PPP process. A review of the commercial deliverability of the scheme, conducted before procurement processes begin, could help to ensure this.

Political commitment: Participating economies highlighted the difficulty in obtaining the necessary level of support and continued commitment to PPP infrastructure projects, especially when the duration of some projects is between 20-30 years. Political commitment is an essential element both during implementation to provide confidence to the private sector and over the whole life of the project. Unless PPPs are seen to offer continuing business opportunities, firms will be reluctant to develop the necessary resources that are required to bid for contracts.

Legislative frameworks: There was also a need to recognise that it is not just PPP-enabling legislation that is required, but broader frameworks for PPP delivery. Participants highlighted the need for legislation that did more than just state “we will do PPPs”. Participants emphasised the need for broader legislative and regulatory frameworks to establish the rules for infrastructure. The frameworks and policies need to provide clear, transparent information and processes to underpin the relationship between the private and public sector and must be firmly embedded in the legal structure of the host country.

Risk allocation: Participants highlighted the difficulty in achieving the appropriate risk allocation in a PPP project as a key barrier to successful implementation. In some instances, projects have been implemented only to be followed by the private sector returning for government support due to inadequate risk profiling or failure to accurately evaluate and manage risk.

Transparency: Many economies felt that it was difficult to attract the private sector into a competitive process without ensuring transparency and accountability through clear definition of the process, and of the respective roles and responsibilities of the government and private sector parties. It is vital to any PPP transaction that there is a transparent, well understood and structured process to ensure all proponents are treated in a fair and equitable manner.

Melbourne workshop

The Melbourne workshop focused on the issues of project selection, risk in PPPs, and the perspective of different parties to the PPP transaction.

The discussion on project selection focused on the management of government objectives and private sector views to achieve outcomes. Key questions considered included: what the state's aims are for the project; how these aims are perceived and whether they can be facilitated by the private sector; and how the relative merits of a project compare to other competing projects.

The discussion on risk in PPPs aimed to establish and understand best practice risk management and allocation in PPPs. It also sought to identify tools for risk analysis and utilise case studies to demonstrate the use of risk analysis.

The discussion on the perspective of different parties to the PPP transaction looked at the typical structure of a project covering the use of special purpose vehicles, financing projects, and the use of project agreements. The workshop also addressed the key issues and motivations of investors, contractors, and operators.

The Melbourne workshop also incorporated expert panel sessions that shared insights into the successful delivery of PPP infrastructure projects and the prerequisites that were required to achieve greater commonality in PPP frameworks across APEC economies.

Key opinions offered by panellists included:

- the need to consider the use of guarantees (where the government agrees to pay the private sector a specified amount if demand does not reach a specified level) when financing some PPPs;
- the importance of adequate risk allocation in a guarantee funding arrangement, during the early stages of market development;
- the importance of political support and commitment to projects in giving the private sector confidence that projects will proceed and be supported for the life of the project;
- the need for initial projects or pathfinder PPPs to be sufficiently attractive to the private sector, as there are a significant number of unknown risks in a new market;
- that governments should not be concerned about letting PPP markets evolve. The first project will not always be perfect. As PPP markets evolve, the degree of risk transfer to the private sector can often be increased;
- the importance of frameworks to ensure well-defined processes and guidelines; and
- the importance of being able to access capital, risk management, anti-corruption and corporate governance support in the procurement of PPPs. The ability of the World Bank

and the ADB to support economies to ensure each of these are in place and/or considered throughout the procurement process was also stressed.

Access to expertise: The panel sessions also brought into sharp relief the importance of access to expertise as a vital component of successful implementation of PPP programs. Access to resources and practical industry experience is necessary to get projects off the ground, achieve value for money for governments and understand private sector issues across the full procurement timeline.

Summary of outcomes

The Jakarta workshop and intervening period prior to the Melbourne workshop highlighted significant movement among APEC member economies toward commonality of best practice processes in private infrastructure provision. A number of economies are now in the process of establishing dedicated PPP units and PPP centres of excellence to act as platforms for developing, delivering and managing PPP projects in the APEC region.

Economies are also in agreement as to the benefits of implementing common best practice approaches to the various stages of the PPP project procurement, development and management processes.

The Melbourne workshop, however, revealed a deeper level of policy challenges to encouraging private infrastructure provision within the APEC region. These challenges included managing the complex issues around risk transfer, and taking the initial steps to actually implement a project and create a viable PPP market. Indeed, while infrastructure requirements in emerging APEC economies are vast, the number of true PPP projects completed in emerging APEC economies in Asia in recent years has been small.

The drought in actual delivery of PPP projects is a critical issue. Many APEC economies have ambitious and well-founded plans for large scale infrastructure investment. PPP delivery models play a key role in many of these plans. Unless more PPP projects can be delivered within the next few years, either public funding of infrastructure will need to be dramatically ramped up or plans will not be met.





3. Key findings

The APEC infrastructure pathfinder initiative was effective in drawing to the surface the central issues underpinning the successful implementation of PPP infrastructure projects. These issues are presented below for consideration by APEC Finance Ministers.

In considering these issues which are outlined below, Ministers are encouraged to support the key recommendation of the report — the establishment of an APEC ‘Pilot PPP Mentoring Scheme’ in 2011.

Successful PPP infrastructure projects are an evolutionary process

Successful PPP programmes grow and evolve; they do not just happen overnight. The benefits of PPPs in terms of realising efficient and well-maintained infrastructure that supports economic development takes time. Small steps are needed to progressively improve outcomes. It is apparent that economies in the region are at different stages in the development of their PPP programmes. As PPP programmes grow and mature, the value capture increases. Ultimately, success is about realising greater value capture from procuring essential infrastructure as PPPs.

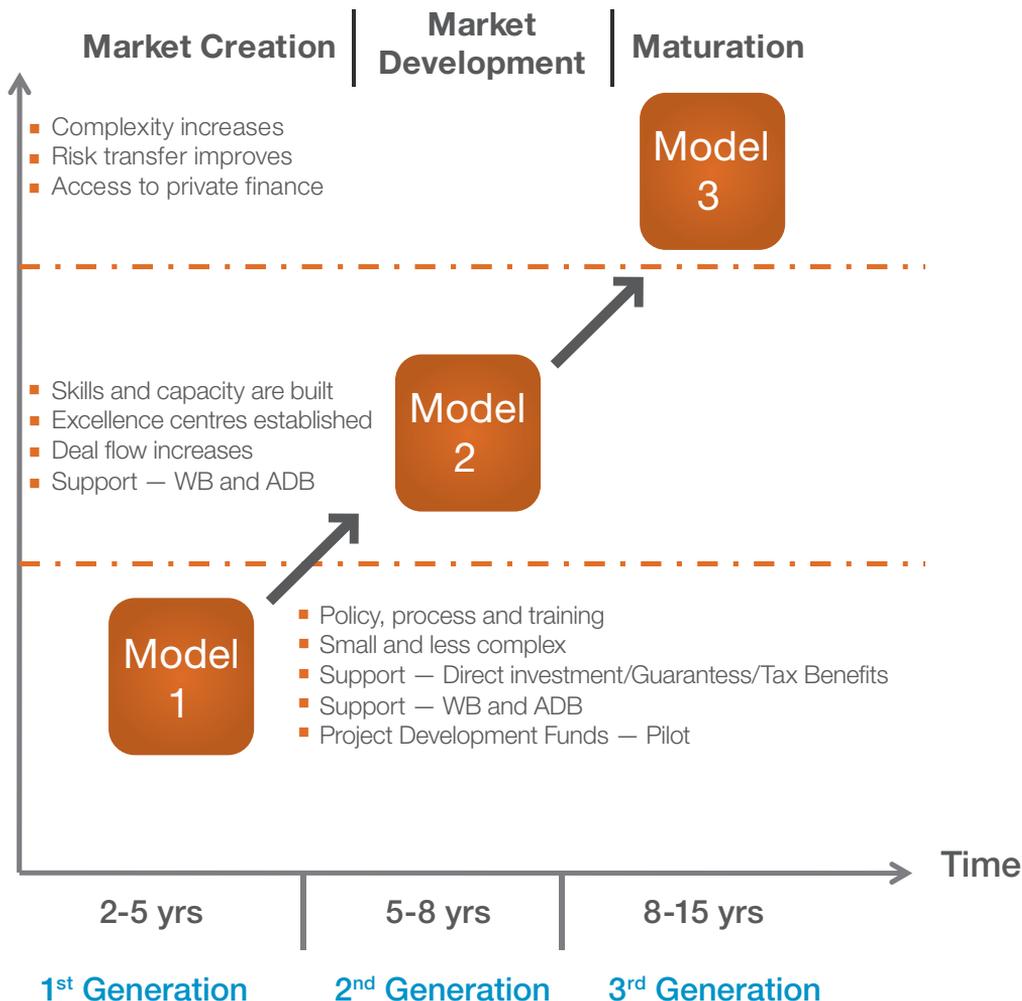
In the first generation of PPPs, greater onus is on the public sector to facilitate, innovate and create the market. Over time, this focus naturally shifts to the private sector as the market deepens and matures and the requisite skills are created, developed and honed by success (or otherwise) in the market. Naturally, the capacity of the market to generate value, innovate and accept risk transfer at the earlier stage is far less than in subsequent stages.

Common features of first generation PPP projects are that they tend to be small and less complex than the model is eventually able to deliver. The public sector is best advised to use this exploratory time to launch pilot projects that help it to develop policy, processes and training for both the public and private players. At this stage, APEC economies may need support for their PPP projects which could be in the form of direct investment, guarantees and tax benefits. The form and extent of support required will also vary from one economy to the other, depending upon the local risk environment. Consequently, multilateral agencies such as the World Bank and ADB have a critical role to play. The region would greatly benefit from common forms of support that can be readily used by individual economies. Examples are already starting to develop, such as the Indonesia Infrastructure Guarantee Fund (IIGF), where the World Bank has assisted in designing and structuring the fund to support infrastructure development in Indonesia.

Well-supported first generation projects will over time lead to a developing market that will naturally change focus. Targeted hands-on assistance that develops and encourages skills and capacity are needed to support increasing deal flow. Upfront investment in this will accelerate the development of the market and enable it to attain maturity more quickly and achieve the

full value capture that PPPs are capable of. Complexity in terms of size, design and commercial arrangements defines a mature PPP market. It is at this stage that risk transfer is maximised and projects can be fully financed by the private sector, without the support of public agencies.

Figure 1: Evolution of a PPP program



Source: Ernst & Young.

The time periods outlined in the diagram above are indicative and not unreasonable when considered against the experiences in the mature PPP markets such as the UK, Korea and Australia.

CASE STUDY: AUSTRALIA

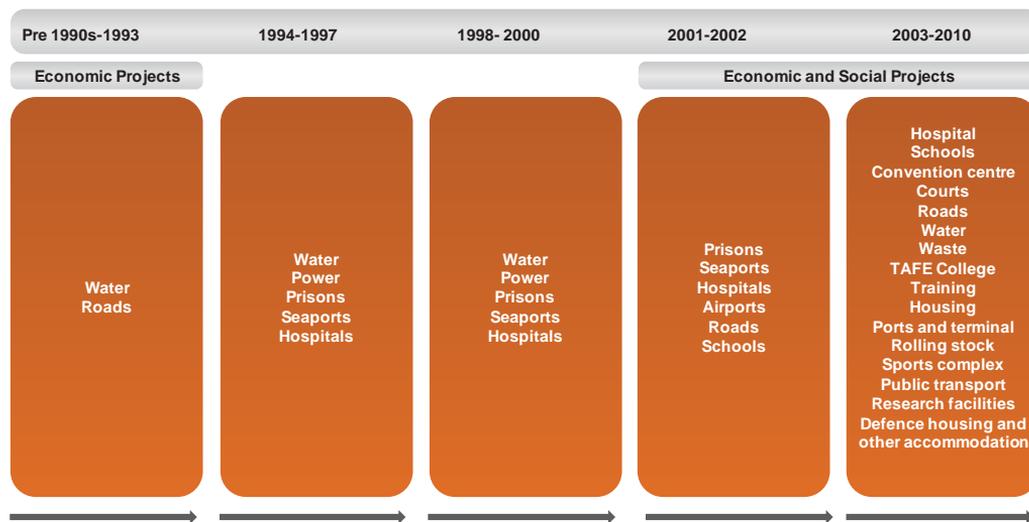
The private sector has been involved in Australian infrastructure for more than 20 years, beginning in the 1980s with projects such as the Sydney Harbour Tunnel.

The legislative regime in Australia prior to the 1990s, however, did not facilitate the utilisation of the private sector or the PPP approach across a full range of services. The government was constrained by specific legislation, which operated to prevent private involvement in certain projects.

As a result of deregulation and a move towards increased privatisation, Australia implemented legislation throughout the 1990s and beyond allowing greater private sector participation. This is not to say that legislation is always a prerequisite for undertaking PPPs. In Victoria, for example, legislation was required to allow private sector operation of prisons in the 1990s, and toll roads have needed specific legislation. But for most projects in Victoria, no legislative basis is needed for private sector participation through PPPs.

As the PPP market has developed over time the range of sectors where PPP approaches have been adopted has increased dramatically (see figure 2).

Figure 2: Evolution of the Australian PPP market



Source: Ernst & Young.

A more formal approach to PPPs by government began in Victoria with the introduction of the Partnerships Victoria policy framework in 2000. The policy aimed to provide the framework for a whole-of-government approach to the provision of public infrastructure and related ancillary services through PPPs. It was very successful in the delivery of major projects.

PPP policies or frameworks now span across nearly all Australian States and Territories. At the Federal level, the delivery of these projects is facilitated by the work of the Council of Australian Governments (COAG) and Infrastructure Australia (established 2008).

At the Federal level, there is a national Minister for Infrastructure supported by a Coordinator General. Similarly, the majority of States now have infrastructure policies, priorities and procedures administered by a dedicated Infrastructure Minister and supported by the Coordinator General, acting as a central point of contact.

Achieving optimal levels of risk transfer

Emerging economies in the region clearly feel significant pressure to deliver on infrastructure projects. In Melbourne, this pressure manifested in a strong focus on issues surrounding guarantees and risk transfer. It takes time to build a market and economies in the early stages of engagement with PPPs may need to reduce the extent of risk transfer in order to attract projects, build capacity and experience, and demonstrate a record of successful delivery of PPP infrastructure projects.

A strong focus on ensuring adequate guarantees and risk transfer may lead to more projects being completed, but it also carries significant costs for emerging economies. It can largely eliminate the benefits of risk transfer, and without vigilance from policy makers, it can see a situation where a PPP market emerges but risk transfer does not grow over time as the market develops. If a private sector partner does not carry any project risk, they will not face any incentive to innovate (and hence reduce cost) in the delivery of infrastructure. As PPP markets develop, the extent of risk transfer must increase if these benefits are to be realised.

Risk allocation is vital to any PPP transaction. Under traditional procurement practices, government generally takes responsibility for the majority of project risks (subject to contractual remedies for non-performance). Under a PPP arrangement, government can allocate specific risks to the private sector that they can best manage and price most competitively. It is important that risks that cannot be effectively managed by the private sector are not allocated to them, as the private sector will require significant compensation for accepting unmitigated risk. Risk allocation

starts with the identification and valuation of risks, which then need to be suitably allocated between the public and private sectors if a project is to be successfully structured.

In some instances projects have been implemented with the private sector then returning for government support due to inadequate risk profiling or failure to accurately evaluate and manage risk. Examples of poor risk management have even occurred in mature markets such as Australia, where the private sector has not on some occasions adequately managed risk in toll road PPPs, leading to insolvency of the private sector operators.

In other economies, inappropriate risk allocation has seen the private sector profit significantly at the expense of value for money to the public sector. Participants expressed their desire for a common and standardised approach to risk assessment.

Overcoming the deficit of knowledge and expertise on PPPs

The fact that only a small number of PPP projects in emerging APEC economies within Asia have been brought to completion in recent years highlights the scale of the implementation challenge that we face in meeting the region's infrastructure needs. These project bottlenecks are a key reason why emerging APEC economies are not moving through the evolutionary stages of building a successful PPP infrastructure market. Further capacity building and knowledge sharing can help in addressing this problem, but there have been a vast range of conferences and courses offered in the region in recent years.

Reflecting this capacity building effort, the level of conceptual understanding of the issues involved in delivering PPP projects within the region is quite high. Significant political will also exists within emerging economies to move forward in developing PPP markets. There are many political champions for PPPs (particularly Finance Ministers) supported by members of their public service and the private sector. There is also a relatively broad awareness of the benefits of PPPs, including lower operational costs, design innovation and capital market development.

What is often missing is staff in PPP units who have 'hands-on' experience at negotiating and delivering PPP projects. There is also an understandable concern among Ministers, and others with 'sign-off' responsibility on major PPP projects, about where they can go to receive impartial advice on complex PPP issues.

Participants recognised the importance of access to this expertise as a vital component of a successfully implemented PPP programme. They expressed the need to have access to expertise to:

- develop guidance material and standardised procedures;
- ensure a strong understanding of project costs against project benefits;

- improve the project approvals process through stronger understanding and relationships with key stakeholders;
- ensure the government is prepared and has a well-defined project prior to going to the market;
- develop, close and deliver transactions that are well structured and where risks are well known; and
- access tacit knowledge of experienced practitioners to help economies understand how they can respond to local infrastructure challenges.

Recommendation: Establishing a Pilot PPP Mentoring Scheme in 2011

Given that a key constraint on PPP markets in emerging economies is the lack of hands-on experience at conceptualising, negotiating and delivering PPPs, further initiatives are required to impart this expertise and advice to officials within the region.

Following on from the work undertaken in the APEC infrastructure pathfinder initiative, it is recommended that APEC Finance Ministers agree to a 'Pilot PPP Mentoring Scheme' in 2011.

The scheme will be a joint initiative of Australia, Singapore, and the World Bank and it will involve working with a group of targeted emerging APEC economies to identify and successfully implement prospective PPP projects.

Once projects have been selected for implementation, relevant experts will be sourced to provide hands-on technical assistance and advice on either removing the impediments to project implementation processes or developing strategies for the effective and timely delivery of these projects.

Progress on this initiative, once launched, will be discussed at an interim capacity building workshop, currently scheduled to take place in Phuket, Thailand, in July 2011. The focus of this workshop will be to review, assess and further progress the mentoring scheme and provide an opportunity for economies to share their experiences and the lessons they have learned throughout the different stages of project implementation. These experiences and lessons are expected to provide a valuable body of material to help guide other economies in their PPP project development and implementation processes.

Final progress is to be reported to the Honolulu Finance Ministers' Meeting at the end of 2011. The 'Pilot PPP Mentoring Scheme' would then be evaluated and further decisions taken on its future.

Appendix: Detailed report on the capacity building program

This appendix reports in more detail on the structure and outcomes of the capacity building activities that were undertaken as a part of the APEC infrastructure pathfinder initiative.

This capacity building program provided the foundation from which key issues were drawn for consideration by APEC Finance Ministers. It also served to highlight the important role that could be played by the APEC PPP Pilot Mentoring Scheme in 2011 in breaking the bottlenecks in PPP project implementation within the APEC region.

Objectives of the capacity building workshops

The key objectives of the capacity building workshops were to expand participation by each economy in PPPs, and to build capacity and knowledge across the key stakeholders responsible for development and implementation of infrastructure procurement policy and frameworks.

The workshops were also designed to reveal key challenges that are being faced by emerging APEC economies in this field, and to bring them to APEC Finance Ministers for attention and action.

Training needs assessment

Prior to the workshops, a training needs assessment was undertaken whereby the participants expressed a desire to share experiences and understand best practices in the following areas:

- legislation and legal frameworks;
- gaining political support for a PPP program;
- developing a PPP policy and framework;
- getting projects to a “bankable stage”; and
- planning and preparing PPP projects.

The workshops were framed to address the key issues identified by participants through a series of expert presentations, case studies, plenary sessions, participant presentations, expert panels and presentations by the public and private sector involved with live PPP projects.

Identifying common best practice approaches to PPPs — Workshop 1: Jakarta

This workshop was framed to address the findings of the training needs assessment by outlining best practice and using group sessions to allow participants to compare and contrast their own economies with the elements of best practice. Through doing this, the aim was to help economies to adopt or adapt existing best practice.

The workshop format aimed to meet the issues across four group sessions:

- critical success factors for PPPs;
- exploring best practice in the PPP procurement process;
- exploring best practice in PPP project development; and
- exploring best practice in PPP project management.

Critical success factors to PPPs

This session focused on critical success factors for PPPs, sharing global examples and case studies. It aimed to set the scene for the workshop by outlining the areas that underpin PPP implementation.

The critical success factors identified and discussed were:

■ Project selection	The government needs to identify sectors and projects that should take priority in the PPP process. A review of the commercial deliverability of the scheme, prior to the commencement of the procurement, can be a source of comfort to the private sector. It helps to reduce the incidence of unsuccessful procurements and avoid the associated bidding costs that would otherwise be incurred.
	At the first stage, the government needs to set standard criteria for screening initial PPP projects from a long list of candidates, then set specific criteria for screening PPP projects for each sector since the nature of projects vary from sector to sector.
■ Political commitment	Political commitment at the policy level is important for the private sector. Most fundamentally, there needs to be confidence that the PPP regime will remain in place and a recognition that the private sector needs to make a return out of PPP projects.
■ Unwavering focus on value for money	Value for money is the key driver and decision making criteria in the use of PPPs to deliver infrastructure.



<ul style="list-style-type: none"> ■ Enabling legislation 	<p>PPP projects often need to be supported by enabling legislation that is firmly embedded in the legal structure of the host country. A key aspect of this is the existence of a concession law that can be readily applied to PPPs.</p>
<ul style="list-style-type: none"> ■ Centre of excellence 	<p>The development of centres of excellence to provide a strong knowledge base can ensure project information is retained project-by-project. The centre of excellence can act as a source for the development of guidance material and the development of in-house expertise (financial, technical and legal).</p>
<ul style="list-style-type: none"> ■ Expertise (financial, technical, legal) 	<p>Both the public and private sectors must have the necessary expertise to deal with the PPP process. The public sector procurer, for example, needs to be able to negotiate individual project contracts and to access the appropriate financial, legal and technical expertise.</p>
<ul style="list-style-type: none"> ■ Deal flow and standardisation (reduces procurement costs) 	<p>A regular and predictable flow of deals, based on recognised risk allocation templates, nurtures the development of a successful PPP programme. Guidance on contract structure also helps to keep costs down.</p>
<ul style="list-style-type: none"> ■ Properly resourced and committed government team 	<p>It is vital that the procuring body (government) has the necessary expertise to ensure a strong understanding of the project costs against the project benefits, as well as the capability to develop and manage a suitable commercial framework.</p>
<ul style="list-style-type: none"> ■ Effective management & allocation of risk 	<p>Risk allocation is vital to any PPP transaction. The transfer to the private sector of those risks that it is best able to manage, which typically includes most risks associated with the design, construction, operation, and financing of a project is crucial to PPP success.</p>

<ul style="list-style-type: none"> ■ Clear specification of outputs 	<p>The requirement that services are specified in terms of payment for a specified output, on which performance can be measured, has been linked to quality and timing of delivery. This contrasts with the conventional approach to public procurement that is based on predetermined funding of inputs.</p> <p>It is crucial that the outputs that will be required for delivery of a particular service are clearly defined at the outset.</p>
<ul style="list-style-type: none"> ■ Project affordability 	<p>All PPP projects have to be affordable to the host economy. The test for economic infrastructure is whether the users can afford to pay the charges (tolls or tariffs) that would support the financial viability of the project. The test for social infrastructure is whether the procuring public sector authority can afford the cost of the ongoing liability over the lifetime of the contract. If a project is judged not to be affordable, the scope of the project may have to be reduced.</p>
<ul style="list-style-type: none"> ■ Understanding that the private sector needs to make an appropriate level of return 	<p>While governments have a monopoly in dispensing PPP projects, they need to demonstrate a sure touch in assessing the return that is required by the private sector in return for taking responsibility for the risk. If expected returns from a project are too low, bidders will divert their skills and resources to other more attractive projects in different countries and jurisdictions.</p>
<ul style="list-style-type: none"> ■ Contract structure and payment mechanisms 	<p>One of the critical elements of any PPP project is the payment mechanism and contract structure. For the private sector, the payment mechanisms and the contract structure are important for their key role in distributing funds and in determining return on investment. The payment mechanism and contract structure are also important to the public sector as a tool for managing performance.</p>
<ul style="list-style-type: none"> ■ Effective procurement process 	<p>An effective procurement process is crucial to successful PPPs as it allows Government to engage with bidders, test the project, structure the project to their needs and differentiate bidders to select the most appropriate short-list. The procurement process must also aim to keep competitive tension and provide the market with sufficient confidence in the ability of the process to deliver.</p>

One of the key elements of this session on critical success factors for PPPs was the use of the resource people in the workshops, including experts from countries that have successfully delivered PPPs. Comments from some of these resource people in relation to their institutions have been summarised below.

P3 Canada

In Canada, a Federal body (PPP Canada) has been established to provide financial support and advice to projects procured by other levels of government, and to support Federal Government departments to utilize the P3 approach. The national experience is being guided by lessons learned from existing practice, much of which originated within projects procured by provincial governments. Successful use of P3 methods for smaller jurisdictions will be enhanced if ways can be found to reduce planning and transaction costs through methods such as standardised procedures and documents. Careful planning and an understanding of the risks and rewards of alternate approaches have contributed to the success of P3 projects.

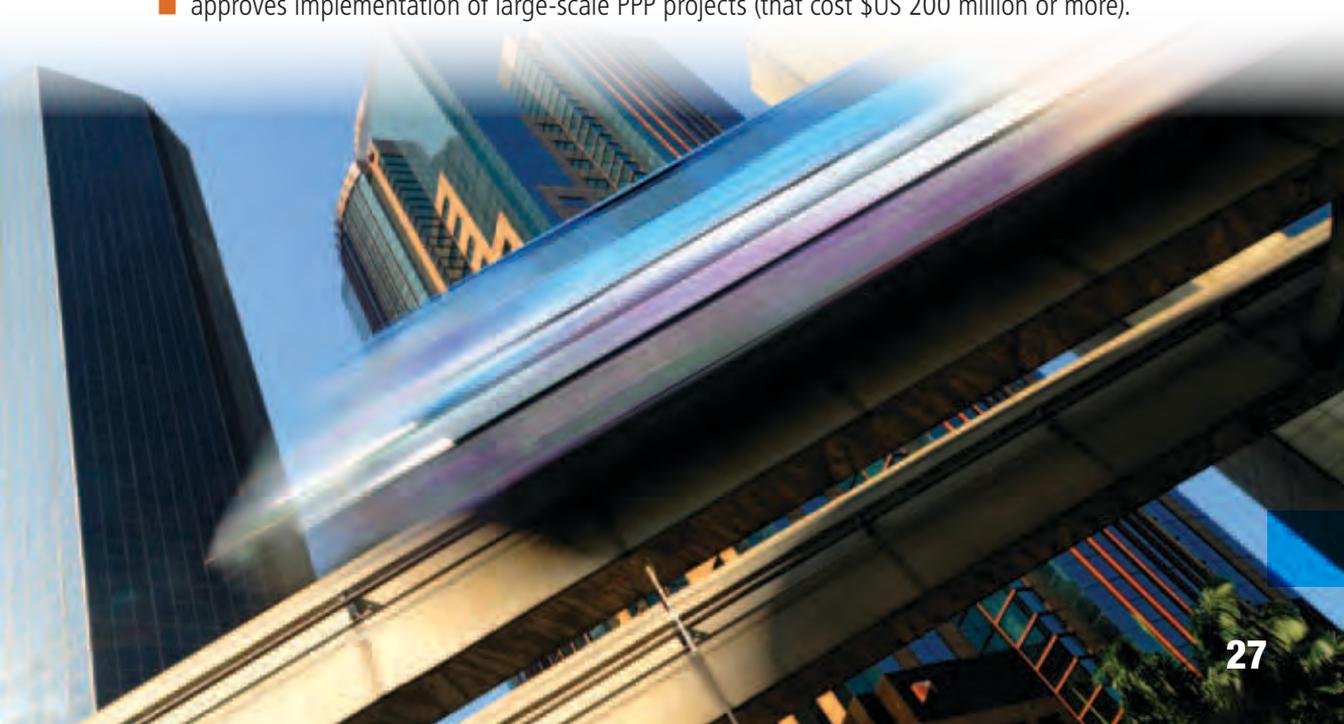
Infrastructure Australia

In Australia a national body, Infrastructure Australia, has been established to provide guidelines and advise infrastructure planning and investment, including on the procurement of Government infrastructure. Infrastructure Australia's mandate encourages a more consistent approach between projects. This encourages greater rigour, lower bid costs and more certainty for the private sector and investors.

Korea

The Korean Ministry of Strategy and Finance is responsible for establishing PPP policy. The three important roles of the Ministry of Strategy and Finance in the national PPP program are as follows:

- develops PPP policy (law, regulations, and implementation guidelines);
- establishes comprehensive investment plans for PPP projects; and
- approves implementation of large-scale PPP projects (that cost \$US 200 million or more).



The Public Private Investment Management Centre provides technical research assistance and capabilities for PPP projects. This dual layer system with a standardised policy approach and a support centre to drive projects, has been very successful in delivering projects in Korea.

Japan

Responsibility for PPPs within Japan rests primarily with the Ministry of Land, Infrastructure, and Transportation.

Japan has empowered local prefectures to provide infrastructure projects, which has created numerous opportunities for delivery. Japan has successfully delivered a number of projects, although to date they have been smaller projects (<\$US100 million). Presently, Japan is working to enable legislation to allow large infrastructure projects in the roads and ports sector to be fast tracked.

Best practice in PPP procurement process

Successful PPP delivery requires strong policy, legislative and procurement frameworks. With these in place, the private sector can bid confidently on projects, maximising competition, and consequently, value for money. However, this cannot be put in place without adequate capacity, in the form of resources and sector expertise.

This session aimed to work through implementation of a procurement process covering policy and procurement frameworks, capacity building and centres of excellence.

Policy and procurement frameworks

The key issues identified by participants in the workshop sessions were:

- many economies have frameworks and policy in place and/or under development;
- political will and enabling legislation were commonly recognised as critical to implementation;
- competing legislation/approaches were common across national and regional governments. There was a need to coordinate across all government levels; and
- there are difficulties in bridging the gap between written policy and guidelines, and implementation.

Capacity building on procurement processes

The key needs identified across the workshop session were:

- ability to learn from other procurement processes, globally and locally;
- the current level of skill and resources in the sector was seen as a challenge by many economies;



- capacity was often split across different jurisdictions. Getting a coordinated approach was a challenge;
- project selection and business case development were key areas of capacity concern;
- capacity building was seen as needing to focus on the unique elements of PPPs over and above other procurement and infrastructure delivery approaches;
- there was a need to build both public and private sector capacity — joint training may be one way of addressing this challenge; and
- exchange programs and advisors were seen as a useful way to build capacity, but there was a need to keep focussing on tailoring to local conditions.

Centres of Excellence

The key issues identified by participants were:

- there were often difficulties in developing a single centre as the nature of projects required different skills;
- in building a centre of excellence, it was important that the capacity was developed from a top-down as well as bottom-up approach;
- any centre of excellence must work across national and local jurisdictions and consider the interests of both parties to a PPP transaction; and
- it was not enough just having an information portal. There was a need to have direct access to people with transaction, procurement and legislative experience.

Best practice in PPP project development

This session aimed to consider the elements of established best practice in PPP project development. The key issues identified by participants were:

- the range of different processes currently used across and within economies;

- the need for a tool for early rejection/selection of projects and to develop a more detailed business case development process to manage costs.
- the importance of preparing a business case is still important for economic infrastructure projects, despite the government not making a direct contribution. This was to ensure value for money by testing a variety of procurement models;
- where project feasibility is flawed and not tested thoroughly through a business case or economic analysis, there is a risk that private parties have recourse to government for risks that they should bear;
- a need to undertake feasibility analysis to choose projects where the risk of private sector seeking additional compensation is lowest;
- the importance of economies developing robust standard model contracts and having the political will to stand behind risk transfer; and
- the need for the business case process to identify early any key issues that could lead to project failure and derailment.

Best practice in PPP project management

Project management focuses on developing and delivering projects that will generate value for money and be delivered within budget and agreed deadlines.

Project management is important to ensure that there is sufficient understanding of the risks that may jeopardise project delivery and market interest. It is a key part of a sustainable PPP market.



This session focused on how projects are selected, how risks are shared and ensuring that projects are acceptable to the market and sustainable over the project-life.

The key findings were:

- standardised commercial principles were inscribed in some legislative frameworks but were often very general. Sector-specific standardised contracts could be useful;
- finding the optimal risk transfer point (where risk is distributed adequately to the party best able to manage it) was difficult, but important in the project management framework;
- despite risk transfer to the private sector, government has ended up making additional payments to private parties on a number of projects. This highlights the value of a robust business case, robust contract and contract management; and
- a central guarantee fund could be used as a mechanism for improving management of public sector risks and ensuring an adequate level of market interest in the early stages of procurement.

Areas of commonality of interest

Following the first workshop, it was evident that there were five key areas of commonality of interest. The key issues were:

Project selection: Economies, particularly those in early-stage development, found it difficult to implement a suitable process for project selection. They expressed concern that projects that were unsuitable as PPPs were often procured without an adequate understanding of project feasibility, economic viability or sustainability. Governments need to identify those sectors and projects that should take priority in the PPP process. A review of the commercial deliverability of the scheme, conducted before the procurement processes begin, could help to ensure this.

Political commitment: Participating economies highlighted the difficulty in obtaining the necessary level of support and continued commitment to PPP infrastructure projects, especially when the duration of some projects is between 20-30 years. Political commitment is an essential element during implementation to provide confidence to the private sector and over the whole life of the project. Unless PPPs were seen to offer continuing business opportunities, firms would be reluctant to develop the necessary resources that are required to bid for contracts.

Legislative frameworks: There was also a need to recognise that it is not just PPP-enabling legislation that is required, but broader frameworks for PPP delivery. Participants highlighted the need for legislation that did more than just state “we will do PPPs”. They also emphasised the need for broader legislative and regulatory frameworks to establish the rules for infrastructure development. The frameworks and policies need to provide clear, transparent information and

processes to underpin the relationship between the private and public sector and must be firmly embedded in the legal structure of the host economy.

Risk allocation: Participants highlighted the difficulty in achieving the appropriate risk allocation in a PPP project as a key barrier to successful implementation. In some instances, after projects have been implemented, the private sector has returned for government support due to inadequate risk profiling or failure to accurately evaluate and manage risk.

Transparency: Many economies felt that it was difficult to attract the private sector into a competitive process, without transparency and accountability through clear definition of the process, and of the respective roles and responsibilities of the government and private sector parties. It is vital to any PPP transaction that there is a transparent, well understood and well structured process to ensure all proponents are treated in a fair and equitable manner.

Homework period

One of the key elements of the workshops was the “homework” period. In between the workshops, participants were asked to take the issues they identified in the first workshop in Jakarta to stakeholders in their own economy.

The stakeholders consulted were varied between economies and included:

- government Ministries;
- key staff of government entities;
- agencies responsible for inclusion of the private sector;
- PPP departments or agencies;
- state owned enterprises;
- key private sector enterprises;
- academic institutes; and
- financing agencies including both domestic banks and the multilateral development banks.

These stakeholders identified a number of challenges to implementation and overcoming the issues within each of the economies. The comments from the stakeholder group were presented by each participating economy as part of Workshop 2.

This homework period allowed each of the participants to present their own concerns and listen to others to further the understanding of common issues in the region.



Best practice in implementation of PPPs — Workshop 2: Melbourne

The second workshop commenced with a group session to address the key issues identified in the first workshop across three areas:

- project selection;
- risk in PPPs; and
- perspectives of different parties to the PPP transaction.

The workshop also provided participants with the opportunity to present key issues for their home economy as identified through the stakeholder consultation process. In this process, participants raised three key issues identified from the list of five (project selection, political commitment, legislative frameworks, risk allocation and transparency) in the first workshop, and asked stakeholders in their home economies what potential barriers and enablers they faced to overcoming these issues.

The workshop then proceeded with an action planning session to allow participants to develop a plan for addressing the key barriers to development of PPPs in their home economy.

Finally, the workshop aimed to provide some first-hand insights into PPPs through an expert panel and public and private sector presentations of “live PPP Projects” or “PPPs in action”.

Group sessions

The group session on day one covered risk in PPPs, and different parties’ perspectives to a PPP transaction to highlight some common areas of concern or capability gaps from Workshop 1. These two sessions highlighted approaches to identifying, allocating and managing risk in PPPs, and some key issues for all parties to PPP projects, including the importance of project selection, legal frameworks and policy. Key points from the discussion included:

- the importance of developing a thorough business case in selecting projects, with consideration of the private sector view, possibly through market sounding exercises;

- what a typical PPP structure looks like, the key documents and agreements and how projects have been financed by the market globally; and
- establishing and understanding best practice examples of risk management and allocation in PPPs.

Participant presentations

Each economy, by making a series of group presentations, then had the opportunity to highlight and share the key barriers to the implementation of PPPs within their own economy. This session was an important part of the capacity building program as it enabled economies to share local challenges and to learn directly from each other's own experiences. Economies were encouraged to ask questions of each presenter and make constructive suggestions as to how barriers to the implementation of PPPs may be overcome.

Action planning

The action planning session allowed participants to identify the barriers and enablers to PPPs as well as the relevant stakeholders that influenced successful implementation in their own economy.

The participants proposed activities that would help key stakeholders move along a commitment chart to achieve greater buy-in and focus their efforts in delivering PPPs. These activities were set-out along a specified timetable for participants to implement on their return.

Expert panel: Session 1 — Greater commonality achieved in Australian PPP frameworks

The aim of this session was for panel members to share their insights into the critical success factors and prerequisites that were required to achieve greater commonality in PPP frameworks across Australia. Panel members reviewed the roles played by the public and private sectors in achieving greater commonality and shared with the group some of the key lessons learned.

The main views expressed included:

- the need to consider the use of guarantees (where the government agrees to pay the private sector a specified amount if demand does not reach a specified level) when financing some PPPs;
- the importance of adequate risk allocation in a guarantee funding arrangement, especially in the early stages of market development;
- the importance of political support and commitment to projects in giving the private sector confidence that projects will proceed and be supported for the life of the project;
- the importance of broader support from the public sector for a PPP transaction. There are many intangible ways government can support a project. For example, the way they interact with the market and proceed with approvals can signal to the market confident intentions;
- the important role of governments in interacting with the private sector post-financial close to assist in achieving approvals, final design and development and commissioning;
- the importance to the private sector of a consistent pipeline of projects as it allows for effective and efficient resourcing and maximises competition; and
- the need for initial projects or pathfinder PPPs to be sufficiently attractive to the private sector as there are a significant number of unknown risks in a new market;

Expert Panel: Session 2 — Developing PPP markets in emerging APEC economies

Expanding from the first panel session, panel members discussed the key challenges and potential solutions in developing PPP markets in emerging APEC economies.

Introductory remarks were provided by Kamran Khan from the World Bank who made the following points:

- the importance of being able to access capital, risk management, anti-corruption and corporate governance support in the procurement of PPPs. The ability of the World Bank and the ADB to support economies to ensure each of these are in place and/or considered throughout the procurement process, was also stressed.

- government individuals that are responsible for the preparation of projects need to have strong technical skills. The World Bank plays an advisory role in this sense and can assist in preparing options on procurement for government;
- the need for government to put up capital, to be prepared and have a well-defined project prior to going to market. Sufficient amounts of project preparation funds need to be available to allow project development and procurement;
- viability gap funding (financial support provided by the government to make projects commercially viable) is crucial as many projects in emerging markets are not economically viable on their own. The government needs to be aware of this and be prepared to make a well-prepared project financially viable;
- governments should not be concerned about letting PPP markets evolve. The first project will not always be perfect. As PPP markets evolve, the degree of risk transfer to the private sector can often be increased; and
- credit worthiness and credit quality in new PPP markets are difficult to assess due to the upfront investment required and the uncertainty over future income. The ability to access forms of guarantees or multilateral support over the life of the project can be an important contributor to increasing private sector interest.

In the subsequent discussions the expert panel expressed the following views:

- the importance of having a well structured transaction where risks are well known. Guarantee funds must not be used as a blanket and cover all risk. The private sector has an appetite for risk and contracting must reflect transfer of risk from the public sector;
- the importance of leveraging knowledge sharing from existing PPP processes. This can lead to a number of regulatory, policy and legal changes to facilitate investment in each country;
- the importance of including an affordability target for projects where the government will be making a viability gap contribution or service payment. An affordability target recognises the budget constraint of the government and helps to constrain projects' costs; and
- the need to recognise wider economic benefits in project development and feasibility. Investment in infrastructure can have significant network effects and subsidiary benefits across an economy.



PPPs in action

The final session concluded with presentations by the public and private sector on two live PPP projects, the Linking Melbourne Authority and the Melbourne Convention Centre.

Political will

Political commitment was continually raised as a critical success factor for economies. Specific issues that were seen by participants as requiring political commitment included:

- the importance of the public sector message in a PPP transaction. There are many intangible ways governments can support a project. The way they interact with the market and proceed with approvals can give confidence to the market and increase the level of interest and competition, thereby improving value for money;
- the importance of a consistent pipeline of projects. A continuum of projects assists the private sector in effectively and efficiently resourcing their bids and maximises competition;
- the need for government to be prepared and have a well-defined project prior to going to market. Sufficient project preparation funds need to be available to allow project development and procurement; and
- the importance of political commitment to both the government and the private sector. Sometimes, a project is considered as a suitable PPP project, but the procurement process can take time. Therefore, the political level may want the project to be implemented immediately through the government budget. If this occurs the private sector will lose faith in the project and may be reluctant to prepare the necessary bidding documents since it costs them time and money. In these circumstances implementing agencies will also be reluctant to prepare any transactions or activities.

Resourcing and expertise

While not raised as a key issue in the first workshop, it became clear in the second workshop that access to expertise was a vital component to a successful implementation of PPP programs. Among other benefits, such processes could assist in:

- improving the knowledge and resource base to develop guidance material and standardised procedures;
- developing in-house expertise (financial, technical, legal);
- ensuring a strong understanding of project costs against project benefits as well as developing a commercial framework;
- improving the approvals process through stronger understanding and relationships with key stakeholders; and
- structuring transactions where risks are well known and that are more likely to be closed and to ultimately deliver efficient, successful PPPs.



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