

# The PPP bidding process

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# A Research Partnership<sup>1</sup>

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<sup>1</sup>Public-Private Partnerships: A Basic Guide, Cambridge University Press, 2013.



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# Project selection

- Since PPPs impact the intertemporal fiscal budget, project selection is important.
- Evaluate projects using social cost-benefit analysis tools.
- Determine shadow cost of public funds
- Approve only projects above that rate.
- Politicians can exercise discretion over the many projects that make the cut.

## Example (Social cost-benefit analysis in Chile.)

*For almost 40 years, all public sector projects must pass a social cost-benefit analysis. In the 80's the rate was 14%, nowadays it is 6%. The system has become outdated and is being modernized.*



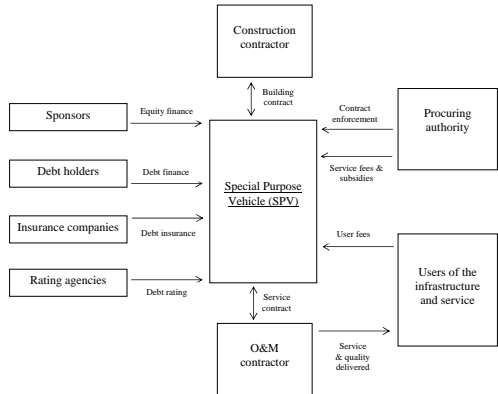
# Getting interest: Road show

- A successful PPP requires competition.
- A road show can get more than the usual companies involved.
- It can be expensive, but there are benefits from more competition.
- The project must be well defined.
- Having only one participant can be dangerous (a bilateral monopoly).
- Having none → loss of face.



# Project finance: An SPV for a PPP

- A dedicated firm, centre of a net of contracts.
- Funds cannot be diverted, facilitates refinancing
- High leverage, project contracts are security for lenders.
- Less risky for backers.



# Pre-qualification

- Pre-qualification is needed to weed out firms that do not have the financial nor technical resources to carry out the project.
- Responding to their questions distracts scarce qualified resources within government.
- If they win the project, it will be delayed for years, before they can be taken away from the project.
- Surety bonds can be used at different stages of the process, and they can exclude these serious firms, as they will not obtain bank backing.

## Example (An example from Chile)

*A well regarded PPP operator made an offer 25% below expectations for the Ruta 5 La Serena-Ovalle (US\$ 265 MM vs US\$ 345MM) Scotia Bank announced that they had made a mistake in their calculations and the cost would be in line with other firms. Scotia Bank decided not to finance the additional amount, and the government cashed a US\$10 MM surety bond. Six months later, the PPP was assigned to the runner-up.*



# The mistake of AZVI

REPÚBLICA DE CHILE  
MINISTERIO DE OBRAS PÚBLICAS  
DIRECCIÓN GENERAL DE OBRAS PÚBLICAS



## ACTA DE APERTURA DE OFERTAS ECONÓMICAS EN LA LICITACIÓN DE LA OBRA PÚBLICA FISCAL DENOMINADA "CONCESIÓN RUTA 5 NORTE. TRAMO LA SERENA - VALLENAR" A EJECUTAR POR EL SISTEMA DE CONCESIONES

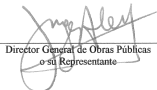
En la ciudad de La Serena, a 23 de noviembre de 2010, siendo las 12:00 horas, en el Salón Gabriel González Videla de la Intendencia Regional ubicado en calle Prat N° 350, de esta ciudad, se procede a efectuar la apertura de las Ofertas Económicas del Licitante y Grupos Licitantes que presentaron ofertas en la licitación de la obra pública fiscal denominada "Concesión Ruta 5 Norte. Tramo: La Serena – Vallenar" ante la Comisión de Apertura integrada en la forma indicada en las Bases de Licitación, cuyos integrantes firman al pie de la presente Acta, al igual que los representantes del Licitante y Grupos Licitantes.

1º) Se da lectura al Acta de Evaluación de las Ofertas Técnicas presentadas por el Licitante y Grupos Licitantes.


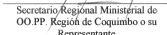
2º) La Comisión procede a abrir los sobres de la Oferta Económica del Licitante y Grupos Licitantes cuyas Ofertas Técnicas han sido declaradas técnicamente aceptables, da a conocer su contenido y deja constancia de los valores propuestos en la presente Acta:

NOMBRE LICITANTE / GRUPO LICITANTE	TRAMO AL QUE POSTULA (A o B)	TRAMO A INGRESOS TOTALES DE LA CONCESIÓN (ITC)	TRAMO B FACTOR DE SUBSIDIO (S)	TASA DE DESCUENTO ELEGIDA	
		Valor de ITC (U.F.)	Factor de Subsidio	Fija	Variable
RUTA ELQUI – HUASCO	A	7.980.000	-	X	
OHL CONCESIONES	B	9.300.000	0,055	X	
CONSORCIO VIAL CHILE	A	8.480.000	-	X	
SACYR CONCESIONES CHILE S.A.	A	7.969.696	-	X	
CONSORCIO AZVI COPASA	A	5.973.001	-	X	

Firma Miembros de la Comisión de Apertura:

  
Director General de Obras Públicas  
o su Representante

  
Intendente de la Región de Atacama  
o su Representante  
  
Secretaria Regional Ministerial de  
OO.PP. Región de Atacama o su  
Representante

  
Intendente de la Región de Coquimbo  
o su Representante  
  
Secretario Regional Ministerial de  
OO.PP. Región de Coquimbo o su  
Representante

  
Director Nacional de Vialidad  
o su Representante





# The Mistakes of Colombia: 1st generation PPPs – 13 projects for US\$ 1 billion

- No international road shows, projects went to Colombian firms.
- Seven projects awarded directly, after no interest in auction (two others had only one interested party).
- By 1999, one project awarded in 1995 and one in 1996 had not obtained financing.
- INVIAS did not define the projects in detail (only feasibility studies). INVIAS unable to use eminent domain.
- No conflict resolution mechanisms, no step-in procedures for possession of franchise by lenders.

Traffic was 40% below predictions, delays, renegotiations, compensation for cost and traffic guarantees, cost overruns in land expropriation, project modifications.



# A two stage procedure

Many countries (including Uganda) use a procedure that is easy to corrupt (mixes quantitative and qualitative variables). Alternatively:

- After pre-qualification, a technical first stage in which firms propose alternatives (if any) to the reference project. Firms can comment beforehand on the design of reference project.
- Firms bind themselves to build the reference project or their alternate.
- Firms post a large (US\$6-10 MM) surety bond of offer seriousness, payable on demand.
- Firms are evaluated and if they pass a threshold, go to the economic stage.
- In this stage, economic offers opened. This has just one value, what the firm asks for: lowest toll, smallest subsidy, PVR, payment to Treasury.
- PPP assigned to firm with the best offer (in one dimension!).



# Contract type: Present Value of Revenue (PVR)

- PPP assigned to firm that asks for lowest present value of user fee revenues.
- Appropriate when demand is unresponsive to the actions of firms and user fees are charged.
- Reduces demand risk for firms; assigns it to public. This can lower cost by up to 30%.
- In case of expensive renegotiation (for example, to expand road size) provides a fair standard for repurchase of concession.
- PPP with modifications can awarded competitively again with repurchase value as part of new contract.
- Thus reduces inflexibility of contracts.
- PPP contracts need to allow repurchase, at fair price.



# Institutional design and conflict resolution mechanisms

- Usually promotion and regulation of PPPs is part of the same government department.
- These are two different objectives: better to have independent departments for each.
- Conflicts between private party and public sector are common.
- Contract or legislation should include mechanisms for conflict resolution, according to fair rules.
- One possibility: creation of a permanent, specialized adjudicatory panel.



# Unsolicited proposals

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- Standard approach is to analyse and reward in auction, if idea is acceptable.
- Important: How long does intellectual protection last? Take it or lose!



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- It can interfere with other programs (Tunel El Salto-Kennedy in Santiago).
- **An alternative:** biannual competition for projects.
- Winning project(s) receive large award(s), and public sector owns the idea.
- The government recovers award when making a PPP of the project (if).



# Conclusions

- A good PPP program requires much forethought, otherwise, results are disappointing.
- Requires appropriate institutional and contract design.
- Fully developed projects before adjudication.
- Correct risk assignment: to those who can act on it (cost → private party) or who can bear it best (demand risk in highways → public).
- The two stage procedure is cleaner than ones where project and technical variables are mixed with economic variables,
- Creative use of surety bonds is helpful.

