PPP in India

What is the issue?

\n\n

The promise of time and cost efficiency through access to specialized skills has had governments increasingly reaching out to the private sector for large infrastructure projects.

\n\n

What is PPP?

\n\n

\n
- A public-private partnership (P3) is a contractual arrangement between a public agency and a private sector entity, typically of a long term nature.
\n
- Through this agreement, the skills and assets of each sector (public and private) are shared in delivering a service or facility for the use of the general public.
\n
- In addition to the sharing of resources, each party shares in the risks and rewards potential in the delivery of the service and/or facility.
\n

\n\n

Why PPP?

\n\n

\n
- The partnership helps in providing better public services through improved operational efficiency.
\n
- It provides incentives for the private sector to deliver projects on time and within budget. Thus it has the promise of both time and cost efficiency in completing the long infrastructure projects.
\n
- It makes the country more competitive in facilitating its infrastructure base

and boosting associated construction, equipment, support services and other businesses.
\n
- The private sector has the access to specialized skills and thus innovation is promoted in the project.
\n

\n\n

PPP in India:

\n\n

\n
- India has systematically rolled out a PPP program for the delivery of high-priority public utilities and infrastructure.
\n
- According to the World Bank, India is one of the leading countries in terms of readiness for PPPs.
\n

\n\n

What are the risks associated with PPP in India?

\n\n

\n
- **Rigid design of PPP** - It inhibits the balance between contracts and adequate flexibility to accommodate unforeseen scenarios resulting in contract disputes.
\n
- **Mismanaging of risk** - Multiple stakeholders in large infrastructure projects, collaborating over long periods requires the risk to be managed properly.
\n
- **Response to unplanned situation** - A prior identification of all risks associated with the project is not feasible. Thus responding to technical defects and financial difficulties is uncertain.
\n

\n\n

What is the solution?

\n\n

\n
- **Chile model of PPP -** Chile has adopted the model of changing the mode of

contract from Built Operate Transfer (BOT) to **Least Present Value of Revenue (LPVR) mechanism.**
\n

- In BOT mode, Concession is offered to highest bidder whereas in LPVR, the concession is auctioned to the private partner that offers the best design/construction efficiency and minimum cost of capital.
\n
- Advantage of LPVR - The concession period is adjusted to account for unexpected events to ensure that the private partner generates the expected discounted revenues.
\n
- **Road Ministry Model -** Currently, Road ministry used Hybrid Annuity Model.
\n
- In Hybrid Annuity Model, the public and private sectors partly fund project construction cost.
\n
- The unpredictable commercial risk is shared in such a way that financial returns to the private sector are predetermined and toll revenues go the government.
\n
- **Principle of early contractor involvement** - It is a collaborative approach to tender a large, complex project. In a two-stage process, based on quality and cost pre-qualification, two-three contractors are shortlisted who compete in developing the best 'solution' i.e. detailed project plan, design and price.
\n
- Association of the contractor with project development reduces the information asymmetry with the asset owner, infuses ownership and can achieve higher cost effectiveness and expedite delivery.
\n
- Identification of project scope and risk and value drivers upfront induces collaboration and reduces the risk premium demanded by the private contractor.
\n
- **Facilitating structured negotiation** - There must be provision in a PPP contract that clearly articulates dispute-resolution mechanism that provides flexibility to restructure within the commercial and financial boundaries of the project. India is taking steps in this direction.
\n
- For instance, last year, finance minister Arun Jaitley announced setting up a **Public Utility Bill for resolution of PPP contract disputes** based on the Kelkar committee recommendations.
\n

\n\n

What is the way forward?

\n\n

\n

- With the Government's target of $375 billion in investment in infrastructure by 2019 and a hope of PPPs bridging 50% of this deficit, the need of the hour is to **employ institutional mechanisms while designing PPP contracts.**
\n
- The time is now for asset owners to think through new ways of de-risking key stakeholders, sharing supernormal profits and negotiating unforeseen conditions.
\n

\n\n

\n\n

Source: Business Line

\n