Private Sector Participation in Public Infrastructure (PSP-MST) MULTI-STAKEHOLDER TEAM

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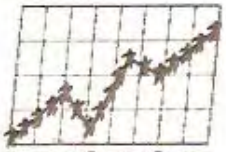

ACTION FOR ECONOMIC REFORMS

How to Ensure the Success of Private Sector Participation (PSP) in Public Infrastructure

(Results of Dialogues with the Business Sector)

On February 21 and 28, 2006, the EPRA PSP-MST conducted roundtable discussions among business sectors and investors involved in the power and water sectors; and, transport, port and road sectors, respectively. Around forty representatives in each event came from various companies engaged in privatization. Also present were representatives from the US Embassy and the Department of Trade and Industry's Board of Investments and Build-Operate-Transfer Center. The discussion evolved around the theme, *"How to Ensure the Success of Private Sector Participation in Public Infrastructure Development."*

These series of roundtable discussions were launched by the Economic Policy Reform and Advocacy (EPRA) Project of the Ateneo de Manila through its Private Sector Participation-Multi-Stakeholder Team (PSP-MST) largely because of the pressure to widely promote private sector participation (PSP) in the development of public infrastructure. The MST also hopes to advocate broader forms of PSP in infrastructure beyond the provisions of the BOT Law. Thus, even if House Bill 5002 has been filed by Congressman Joey Salceda amending the BOT Law and consequently its IRR, deliberations on the proposed amendments to the BOT Law are ongoing, especially because technical assistance for the advocacy to design a more responsive policy environment is made available thru the EMERGE and EPRA Projects with the USAID.

EPRA aims to promote wide ownership and support for economic reforms and to strengthen the capacity for reform among government and non-government stakeholders. PSP in public infrastructure is one of its sectors tasked to do the following: seek consensus among various stakeholders, widen public discussion on existing laws requiring amendments, assist line agencies in achieving

proper balance in streamlining of approval processes and safeguarding public interest; and form a strong consumer advocacy organization with the civil society organizations (CSOs) and the business sectors. EPRA, likewise, seeks to provide a venue for the general public and civil society to enrich the discussions toward policy reform. For this reason, the PSP-MST invited private sector representatives who are the direct and immediate stakeholders of PSP policies to the two aforementioned forums. It is expected that in these various forums different kinds of concerns from the various sectors—public, private, and civil society—will emerge. EPRA hopes that by drawing out these concerns, the proper balance among conflicting positions will be achieved.

One challenge confronting the stakeholders then is how to reconcile the inherent conflicts between promoting more Public-Private Partnerships on the one hand, and safeguarding public interests on the other, in the efforts to amend the BOT Law. An even greater challenge is insulating public (civil society) and private (business) interests from the challenges of politics and politicking attendant to private sector participation in public infrastructure.

The Private Sector's Expectations and Concerns

As mentioned earlier, amendments to the BOT Law, including a proposed BOT Authority have been drafted—undertakings that have rendered the field open for revisions in the policy environment. In line with such, EPRA hopes to play a role in effecting improvements on the said draft by consolidating the concerns raised by various stakeholders.

In the two roundtable discussions conducted, the general consensus was that private sector participation (PSP) must be promoted in the Philippines because unlike its neighbors in Asia, the Philippines does not have sufficient public resources from which to draw capital GDP. Still, the same stakeholders saw that throughout the execution of PSP contracts, there is a need to safeguard public interest at all times and for government to get a fair deal. In the past, some realized liabilities put a large burden on government and, consequently, on the taxpayers. Ideally, therefore, the relationship between the public and private sectors established must be one where everyone's best interest is served. Further, guarantees and subsidies ex ante should be justified ex-post by large social and economic returns and manageable fiscal exposure.

Those present in the discussions also articulated the following expectations:

- Government must be knowledgeable of the industry under consideration. If it needs more research support, then it should make moves to get it.
- Government must have a press office that can make information available to media such that the people do not blame PSP every time something goes wrong in a PSP initiative. To promote understanding of PSP among the general public, orientation and technical assistance must be extended to CSOs and media.
- PSP needs an actively functioning regulator that has sufficient funding support to allow it to operate efficiently.
- Engineers sent to inspect infrastructure should be capable and knowledgeable about world standards.
- Government should have lawyers working on PSP concerns.
- There ought to be transparency and accountability.

Participants and speakers in the two roundtable discussions likewise identified various issues which appear to hinder the success of private sector participation in public infrastructure as follows:

- Having just one BOT Authority to promote PSP and at the same time evaluate the soundness of proposals. The set-up whereby the same body serves as regulator and evaluator is deemed ill-advised, given the seemingly contradictory or conflicting interests/natures of the tasks involved. Also a concern is the lack of resources of the regulator.
- Lengthy project review and negotiation process which increases total project cost and creates mistrust of the government, especially from the point of view of foreign investors. Some proponents of BOT projects also claim they feel like college students defending their thesis when they are in the process of having a BOT project proposal approved.
- The sanctity of contracts' not being respected as in the case of PIATCO.
- The refusal of some LGUs to respect the provisions of contracts made with national entities (national government?)
- Unsolicited proposals' sometimes becoming the rule rather than the exception. This problem stems from the fact that government line agencies lack the in-house capacity to develop PSP projects themselves.
- Government's assuming too much risk. Two questions associated with infrastructure contracts are as follows: Are there ex-ante justifications for

providing subsidies to infrastructure projects with PSP? Can private developers reduce the probability that government contingent liabilities will be realized in the future?

- Competitive bidding and windfall gains. The public perception is that PSP in infrastructure has high private returns and is therefore capable of addressing social equity and redistributive concerns, but this is not necessarily so. Further, the lowest priced rule might limit the flexibility of the players in terms of addressing shocks to the system, like the major currency devaluation in 1997.
- Non-requirement of GOCCs in the utilities sector's to pay real estate taxes: hence, the burden of paying these taxes falls on the private sector.
- CSOs have certain criteria which are not normally business criteria such as welfare and poverty, but business is slowly becoming interested in them given the growing attention given to corporate social responsibility.
- Political risks. Politicking and politics should be managed. The law should be adhered to rather than revised to accommodate political interests.
- Weak appetite of foreign financial institutions to finance PSP projects in the Philippines.
- Inadequacy of government resources for the acquisition of right of way for certain projects
- Restive labor unions and the dislocation of the urban poor.
- Unsolicited projects have been creating a naturally strong constituency over the years. They also have a greater tendency to seek market guarantees.
- Preparation of Swiss challenges has also been problematic.
- Large fiscal losses because of the projects

Action/Reform Proposals

Participants to the roundtable discussions gave the following recommendations to improve PSP in public infrastructure development:

- Streamline the evaluation process. Advise government agencies to cut red tape and promote efficiency. Private investors complain about delays in securing approvals, and about policies that are good but are poorly implemented, if at all. They point out that delays increase capital costs in the long run.
- Improve the business environment. Ensure balanced risk sharing between the private and public sector. Respect the sanctity of contracts at all times.
- Create one office each for the promotion of PSP and the evaluation of BOT proposals.
- Fast track privatization. PSP must be promoted because without private sector participation, the cost of basic services becomes higher for the consumers. Recall what Malaysia's former Prime Minister Mahathir said: government has no business to be in business; government is there to help the private sector.
- Improve transparency. Increase access to information on project outcomes especially among academics and government which are the operators of the infrastructure project. Doing so should also reduce opportunities for corruption in any part of infrastructure development and enhance and improve the public's systemic perception of PSP projects.
- Impose reasonable tariffs. Guarantees should be made clearer and tax incentives should be extended. The cost of capital increases while the rate of return decreases in the absence of government guarantees and when debt and rate of return are bundled in the tariff.
- The scenario created must provide for adequate competition in the selection of BOT projects to undertake and of who shall undertake them.
- There must be a good mix of solicited and unsolicited proposals.
- Have the winner in the Swiss challenge pay the original proponent so that the original proponent will seriously prepare

Mr. Jurgen Lorenz (left), Managing Director of JL Business and Technology Consultancy and Mr. Mel Robles (right), Administrator of Light Railway Transit Authority are dicussing the proposed LRTA Line 6 Project.

its proposal to ensure its victory in the Swiss challenge.

- Develop the capital market. Infrastructure is the way to go where investments are concerned especially for power, water, roads and other infrastructure. A strong vibrant capital market will be very important.
- Promote political will and commitment on the part of government and the political leadership.
- Send delegates to China and Singapore to observe their political and economic environment. Implement similar models in the Philippines instead of creating completely new ones.
- Enhance social returns to unsolicited projects through improved and more thorough consultations between the private sector and government and affected stakeholders.
- Private project developers should ensure that the social objectives (including fiscal solvency) of their infrastructure project are not compromised by the manner in which these projects are structured and implemented.

Recommendations/ Observations on Proposed Amendments to the BOT Law

- Expand the BOT concept or model; provide for more innovative ways to attract investments in the country.
- Produce a flow chart on the existing law indicating required documents or listing PSP requirements for BOT projects.
- Provide for the creation of separate an implementation and evaluation body and a regulatory body. Study the possibility of privatizing or outsourcing the evaluation process. Decide on whether this should be provided for in the law.
- Amendment E on unsolicited contracts' being awarded to the winning challenger. This proposed amendment penalizes a bidder for winning the contract. Thus, it will serve as a disincentive.
- Amendment G provides for an executive warranty to uphold the validity of the BOT/PSP contract: Will the judiciary uphold the validity of the contracts? This amendment may not be advisable and may even prove dangerous for the executive body as it will be held liable by the judiciary as a result.
- Amendment M does not clearly state whether the BOT Authority will be authorized to stop the project in the event of violations to the concession.
- Amendment O is already covered by the penal code's provisions on swindling and fraud. If carried, related laws should also be amended.
- The new BOT law should clarify how it intends to deal with LGU projects. It should set the parameters regarding which projects are within the jurisdiction of LGUs and which have to be referred to the National Economic Development Authority (NEDA). Some investors claim there are LGUs that make investors their milking cows. When this goes on for a long time, consumers end up being penalized via higher fees.
- Most BOT projects are long term. Investors want to be protected over that span of time. As people they deal with in government initially may no longer be around in the long haul, it is important that policy itself be firmly in place and adhered to over the years, regardless of who is in charge.
- The law should set specific deadlines for the processing of proposals. It should indicate the imposition of penalties in case of failure to meet the said deadlines.
- The law should stipulate that investment promotion is the BOT's primary task.
- The BOT Law be amended to do away with unsolicited bids. If the law is not amended, fiscal risks associated with such projects will remain. In such an event, developers should ensure that projects submitted for approval do not burden the national government with undue fiscal risk at any time during implementation.

This article is written by Mary An Gonzalez for the Research Advocacy and Advisory Group (RAAG) as requested by the PSP-MST sector of the Ateneo-EPRA Project.

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