Public Private Partnership - PPP

Wikipedia

A public–private partnership (PPP or 3P or P3) is a government service or private business venture that is funded and operated through a partnership of government and one or more private sector companies.

PPP

PPP involves a contract between a public sector authority and a private party, in which the private party provides a public service or project and assumes substantial financial, technical and operational risk in the project.

- In some types of PPP, the cost of using the service is borne exclusively by the users of the service and not by the taxpayer.
- In other types (notably the **Private Finance Initiative - PFI**), capital investment is made by the private sector on the basis of a contract with government to provide agreed services and the cost of providing the service is borne wholly or in part by the government.
- Government contributions to a PPP may also be in kind (notably the transfer of existing assets).
- In projects that are aimed at creating public goods like in the infrastructure sector, the government may provide a capital subsidy in the form of a one-time grant, so as to make the project economically viable.
- In some other cases, the government may support the project by providing revenue subsidies, including tax breaks or by removing guaranteed annual revenues for a fixed time period.
- In all cases, the partnerships include a transfer of significant risks to the private sector, generally in an integrated and holistic way, minimizing interfaces for the public entity.
- An optimal risk allocation is the main value generator for this model of delivering public service.

Two fundamental drivers for PPPs

- Firstly, PPPs are claimed to enable the public sector to harness the expertise and efficiencies that the private sector can bring to the delivery of certain facilities and services traditionally procured and delivered by the public sector.
- Secondly, a PPP is structured so that the public sector body seeking to make a capital investment **does not incur any borrowing**. Rather, the PPP borrowing is incurred by the private sector vehicle implementing the project.

On balance sheet and off balance sheet

- On PPP projects where the cost of using the service is intended to be borne exclusively by the end user, the PPP is, from the public sector's perspective, an **off-balance sheet** method of financing the delivery of new or refurbished public sector assets.
- On PPP projects where the public sector intends to compensate the private sector through availability payments once the facility is established or renewed, the financing is, from the public sector's perspective, **on-balance sheet**, however, the public sector will regularly benefit from significantly deferred cash flows.

Cost and efficiency

Generally, financing costs will be higher for a PPP than for a traditional public financing, because of the private sector higher cost of capital. However extra financing costs can be offset by private sector efficiency, savings resulting from a holistic approach to delivering the project or service, and from the better risk allocation in the long run.

SPV

Typically, a private sector consortium forms a special company called a **special purpose vehicle** (SPV) to develop, build, maintain and operate the asset for the contracted period. In cases where the government has invested in the project, it is typically (but not always) allotted an equity share in the SPV.

The consortium is usually made up of a building contractor, a maintenance company and equity investor(s).

It is the SPV that signs the contract with the government and with subcontractors to build the facility and then maintain it. In the infrastructure sector, complex arrangements and contracts that guarantee and secure the cash flows make PPP projects prime candidates for project financing. A typical PPP example would be a hospital building financed and constructed by a private developer and then leased to the hospital authority. The private developer then acts as landlord, providing housekeeping and other non-medical services while the hospital itself provides medical services.