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CONTRACTING THROUGH THE APPLICATION OF THE PUBLIC-PRIVATE PARTNERSHIP MODEL

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Abstract: *The model of public-private partnership (hereinafter: PPP) model is being increasingly used in contracting international affairs. The public sector has until recently predominantlz relied on project funding from the limited budget resources, loans of international financial institutions and development assistance funds primarily from the European Union.*

Contracting of international business affairs through the PPP model requires legal, financial and technical expertise, and the success of the project depends on the negotiating skills of the involved parties during the contracting process. The most difficult challenges in the conclusion of international affairs through the PPP model are uncertainty and risk.

Negotiations are invariablz exposed to a variety of challenges, such as: the environment, culture, ideology, bureaucracy, regulations, possible sudden change in circumstances. If the conditions for the application of the PPP model are created, the model should enable the public partner to realize as much "value for money" as possible.

Keywords: *public-private partnerships, negotiation, risk, contract models, international financial institutions.*

1. INTRODUCTION

In the last three decades the PPP model has been increasingly used in contracting international affairs. This was once the exclusive role of the state – to meet public needs financed exclusively from the budget; today this is largely achieved through the implementation of the PPP model. This way, the satisfaction of public needs is provided by engaging means of the private partner.

Private companies have previously been involved in public sector projects as subcontractors and thus provided services of design, construction and others, but through the PPP model, private partner assumes the role of financing.

Most of the PPP projects involve the transfer of a substantial part of the risk and investments from public to private sector which is more efficient in the management of certain risks. PPP projects bring significant benefits in terms of efficiency and lower costs for the public sector (Yescombe, Public-Private Partnerships Principles of Policy and Finance, Oxford: Elsevier Ltd.; 2007, p 15).

PPP model has reached a significant volume and value of total transactions. Over the past two decades, in the European Union more than 1,300 PPP contracts were signed, bringing the total value close to 250 billion euros. The European Investment Bank (EIB) has so far supported the development of around 100 PPP projects in most European countries through approved loans of over 15 billion euros (Kapeller, Nemoz, Public-Private Partnerships in Europe - Before And During The Recent Financial Crisis, the European Investment Bank 2010, p 28).

Unfortunately, the financial crisis has affected the number of concluded contracts under the PPP model in Europe which fell by more than 40%. These difficulties represent pressure on governments that rely on PPP projects during the construction of infrastructure projects and the provision of public services.

The European Project Expertise Centre was established in 2011 with the mission to support the public sector in the implementation of PPP projects and to promptly respond to problems arising in the implementation of projects. EPEC was established at the joint initiative of the European Investment Bank, European Commission, Member States and candidate countries of the European Union.

2. PPP PROJECTS

PPP represents all forms of cooperation between the public and private sectors in the field of use of resources, knowledge and experience, design, financing, construction, operation and maintenance of local infrastructure and the performance of the original functions of the public sector.

PPP brings together public and private sector in order to achieve the interests of both sides. Good management of these projects leads to the achievement of synergies and the utilization of the best aspects of both sectors, which leads to a balance between innovative ideas and discipline of the private sector on the one hand and good public services on the other.

PPP is a type of commercial cooperation in the framework of which the partners pool resources and knowledge to the appropriate allocation of resources and risks, all in order to meet the public need. A private partner can use his resources and skills in the provision of goods and services traditionally provided by the public sector (Dare, Public Private Partnerships, Practical Analysis, London: Globe Business Publishing Ltd., 2006, p. 7).

Within the PPP as a form of commercial cooperation, the private partner receives assets of the public sector to commercial use, takes significant risks related to the performance of public office and / or using public sector assets, benefits from performing public service and / or use of public sector assets; all this should maximize financial-economic benefits for the public sector.

PPP projects are long-term arrangements (generally over 25 years) that require a large initial capital for activities that are necessary for the company for many years and which is returned during the duration of the project.

The private partner provides the financial resources for the project using both his own funds and borrowed sources of financing; the public sector, as the end user, pays for the service provided. Risk allocation is such that the sides take upon themselves the risks that they best manage, which they agree upon through a long-term contract. The long duration of these contracts is the result of a complex project and the financial structure which includes a large amount of investments (by private sector) with long term returns.

PPPs enable public institutions to provide new infrastructure and services with smaller initial investment as well as to control the quality of the works. For the public sector the advantage of financing large projects through PPP model is that the public sector is not required to provide all the funds all at once, but is able to allocate project costs evenly throughout the project.

Depending on whether the private partner's fee ispaid by the end users, the public partner or in combination, there are three different types of PPP projects:

- projects based on demand - fee paid by the end-user;
- projects based on availability - compensation is paid in full by public partner;
- projects with a combined model of payment - fee paid by the end user and the public partner.

Without financial support from international financial institutions the success of PPP projects is very difficult to achieve, therefore it is necessary that the legislative act is mutually coordinated and harmonized with the rules of the procurement process for projects funded by international financial institutions.

Efficient allocation of risk is an essential precondition for the successful implementation of PPP projects. Project risks should be allocated between the public and private sectors so that specific risk should take over the party which it will manage in the best way. When the public partner delivers the Tender Documentation it is desirable that he provide a matrix of risk allocation and thus demonstrate to the private partner exactly what risks he plans to transfer to his side. Defined risk matrix is the starting point for further negotiations with the private partners.

For the success of the PPP project it is necessary that the project is commercially attractive to the private sector and that it offers a satisfactory return on investment. For the success of the project it is of great importance that the private sector is able to deliver the project within the stipulated standards and norms, that the project is financially sustainable and structured so that the international financial institutions and banks have an interest to finance it.

3. THE PROCEDURES OF PUBLIC PROCUREMENT FOR SELECTION OF THE PRIVATE PARTNER

When it comes to the systematization of legislation and creating a single legal framework, PPP models in the European Union are still in the initial stage. The European Commission has not defined a policy of establishing and development of PPP, neither has it developed a clear concept of implementation in the Member States of the European Union

The basic principles of public procurement rules of the European Union are as follows: procurement must be transparent and all participants must be treated equally. At the beginning of the process the notice of procurement has to be filled in standard form and published in the Official Journal of the EU.

When awarding PPP, one of the following tender procedures must be observed:

- Open procedure;

- Restricted procedure;
- Negotiated procedure;
- The competitive dialogue.

The selected public procurement procedure must be specified in the notification. In an open procedure, the contracting authority invites potential partners to directly submit bids for the contract, in response to a public call. In the restricted procedure we shall invite potential partners to participate in a process that takes place in two stages:

- prequalification and forming a narrow list of potential partners;
- submission of final bids from potential partners who are on the narrowed list.

In the open procedure and in the restricted procedure negotiations are not allowed.

In the negotiation process, we negotiate with potential partners. This procedure is carried out through the following stages:

- Pre-qualification phase and the formation of narrowed the list of potential partners;
- Potential partners are invited to negotiate;
- Selection of one or more partners for negotiations;
- Negotiations;
- Closing a deal.

In the competitive dialogue prequalification process is conducted, and then a narrowed list of potential partners is formed. Potential partners are then invited to participate in the dialogue process during which they will discuss and develop the best solutions. Dialogue is kept until parties achieve solutions that meet the requirements of the project, after which potential partners are invited to submit their final offer. The public partner needs to structure the procurement process so as to ensure that his objectives are met more effectively. In practice, the competitive dialogue is most often conducted through the following phases:

- Preparing for the dialogue;
- Dialogue;
- Post-dialogue.

Salakjuz states that business people should resist the temptation to sweep through pre-negotiations and start talking about the job as soon as possible. “Instead, we need to use the pre-negotiation phase to learn as much as possible about the background, interests and management structure of the other side, and to notify the other party of our own origins, interests and organization. This phase is essential if the parties are serious in their wish to get to know one another well. Adequeate knowledge is an essential condition for establishing trust and good business relationship. In projects that require significant investment and a close working relationship, the parties can engage advisors or a well informed third party to facilitate the whole process of parties getting to know one another. Managers often tend to resist spending enough time on pre-negotiations relying on the famous saying: “time is money”.

“Indeed, time is money in terms that certain assets must be invested in order for a particular project to become profitable. To invest less time than is required in the design of the work is the same as to invest less money than you need. Insufficient investment increases the possibility of failure.”

After the successful completion of the first phase of the negotiations, participants are entering a phase of dialogue when they determine the interests of the parties to the negotiations, present proposals and counter-proposals, develop the way to achieve an agreement and agree on essential elements of the contract. This phase ends with an invitation to a private partner to deliver home offer which should contain the agreed contract draft, proposed financial plan outlined in detail together with the technical solutions related to the project. The last phase is the delivery of the final offer and - if everything is already agreed upon – there remains nothing but the conclusion of the contract.

4. PPP MODELS

The contractual model is based on the contractual relations between private and public partners. The contractual model is, almost as a rule, concluded in writing, for a limited time not less than five years and no more than forty years, with the possibility that after the expiry of the contractual period parties conclude a new contract with the selection of private partners through the re-procurement. The most important model is the concession contract.

The institutional model involves cooperation between private and public partners which can be realized through the establishment and management of a joint company and by taking over the control of the existing public institutions by the private partner, in proportion to the percentage of financial participation. Further, the contract governs the allocation of risk, responsibility of the parties, the financial role, managing the company. The institutional model is recommended in areas that are vital for the public sector and where it is necessary for the state to retain some control and supervision over the provision of public services to end-users, as well as services in the field of water supply, air transport, energy, etc.

5. CONCLUSION

In practice PPP projects have brought a new way of structuring the relationship between the public and private sectors in projects that aim to meet the public needs. Instead of the public sector self-financing and building facilities and infrastructure, which then fruther be managed and maintained to provide service to end-users, this way public sector concludes long-term contract with the private sector that undertakes to finish either part of the job or the whole project in its entirety. The public sector retains regulatory and supervisory function by prescribing standards for services rendered and supervision of their implementation. Private partner makes his profit either from end users or by collecting from the public sector in the form of rents.

One of the basic principles of public-private partnerships is that risk should be transferred to the party that can best manage it. PPP projects aim at transferring risk thus providing the reduction of long-term costs, increasing quality of service and bringing increased revenue through effective use.

Key challenges in contracting business through the PPP model are risk and uncertainty. The public sector needs to understand the basics of common and fair distribution of risk and not to attempt to insist on the transfer of risks which can not be managed. The procurement process has to abide by the rules, must be transparent and all participants must be treated equally. This should enable us not only to gain the best partner who is able to implement the project in the most efficient way, but also to create the possibility that the project is financed by the international financial institutions.

One of the most important features of PPP projects is the introduction of leadership skills and innovation of the private sector to the public sector. These features can reduce costs, increase efficiency and quality of design, construction and management of a facility or service. Thanks to the introduction of the PPP model, public sector project expenditures during are lower than traditional procurement; still further, the application of the PPP model provides other significant benefits: new knowledge, easier access to markets, favorable risk distribution.

In Serbia, it is necessary to provide new sources of financing which will not immediately hit the budget already, but will allow steady, long-term financing.

Although the PPP is just one of the models that is available to the public sector, its importance should not be underestimated, especially if viewed as a means of relieving borrowing by the public sector. Cooperation with the private sector provides the possibilities for introduction of management skills and innovation of the private sector to the public sector, thus reducing costs, increasing efficiency and quality of design, construction and management of a facility or service.

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