Key Issues in Managing Fiscal Risks from Public-Private Partnerships (PPPs)

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Outline

• PPPs and fiscal policy
• Main weaknesses in managing PPPs
• Why worry?
• Managing fiscal risks
• Concluding remarks
PPPs and Fiscal Policy

• Expectations of public services have risen steadily and governments are struggling to satisfy them within the constraints of annual public spending limits
• PPPs are generally identified as one way to address these concerns
  
• In the current international context, where budgets are tight and increasing debt levels are at the center of public concern, the political appeal of PPPs has increased
• Countries are moving in the right direction strengthening legal, institutional, budgetary, and reporting frameworks
• However, implementation of best practices is not uniform across countries and serious challenges remain
Main Weaknesses in Managing PPPs

• Weak role of the Ministry of Finance (i.e., budgetary authority) as the gate-keeper of public finances
  – Institutional and legal frameworks result in government’s excessive exposure to fiscal cost and fiscal risks

• Lack of integration of PPP projects within the budgetary process
  – Weak capital budgeting procedures
    • Competition for budgetary resources not clear
    • Budgeting procedures bias decision-making in favor of PPPs
  – Lack of medium-term budgetary framework
    • Annual appropriation mechanism not appropriate for PPPs
    • Inadequate long-term fiscal sustainability assessment
    • Poor information on contingent liabilities
Main Weaknesses in Managing PPPs

- Inconsistencies between budgetary, accounting, and reporting standards
  - Accounting/reporting procedures tend to move PPP spending off budget and can create contingent liabilities for the government
  - National accounting standards not in line with international standards
  - Lack of transparency in fiscal reporting
- PPP operations gradually pushed outside the general government coverage
  - Power/water purchase agreements signed by state-owned enterprises
- Weak monitoring capacity across the public sector
  - Ministry of Finance (i.e., budgetary authority) and/or PPP unit
  - Procuring ministries/agencies
  - Supreme audit institutions
Why worry?

Mistakes can be costly!

Governments can manage fiscal risks while obtaining efficiency gains by implementing:

• Good projects
• Good laws
• Good institutions
• Good fiscal accounting and reporting
Managing Fiscal Risks

• Good projects $\rightarrow$ Improve public investment planning, project selection, implementation, and evaluation

• Systematic two-step investment planning process
  
  1. Choose the right projects
     • Have a clear investment strategy
     • Prioritize investment projects
  
  2. Do PPPs for the right reasons
     • Choose only PPPs that provide VfM
     • Include PPPs in budget and medium-term budget framework
Managing Fiscal Risks

• **Good laws → Strengthen the legal framework**
  
  • Introduce a clear and consistent PPP law and/or harmonize existing laws to provide a consistent legal framework
  
  • Clarify roles and responsibilities (e.g., across different ministries and levels of government)
Managing Fiscal Risks

- **Good institutions** → Strengthen the management and oversight framework
  - Establish due-diligence/multi-stage gateway process with strong role of Finance Ministry
  - Make sure PPPs are done for the right reasons → check VfM and fiscal affordability
  - Clear separation of PPP promotion and PPP oversight functions
Managing Fiscal Risks

- Good fiscal accounting & reporting → Achieve full and transparent disclosure of all fiscal risks from PPPs

- Issues to be addressed:
  - Limit public sector contingent liabilities from investments that are not on the public sector’s books
  - Prevent creating budgetary rigidities from pre-committing spending for hidden liabilities

- Yet, accounting & reporting rules cannot ensure by themselves fiscal discipline nor efficiency in public spending
Managing Fiscal Risks

• Good fiscal accounting & reporting → Need to integrate accounting/reporting and good budgetary planning, selection, and approval procedures

• The issue
  – since the long-term costs of PPPs are not reflected in the budgetary approval process, there is a bias in favor of selecting PPPs instead of projects implemented with traditional public procurement

• Recommendation (Victoria State of Australia approach)
  – any agency interested in PPP project must first seek approval for the capital spending that would be needed as if the project were to be financed publicly
  – If a PPP is used, the approved spending is converted into spending on the PPP’s service payments during the operation phase of the project
Concluding Remarks

• PPPs can be more efficient than traditional public procurement...but also entail fiscal risks
• These risks are not “theoretical”
• Governments can take action to manage fiscal risks:
  – Strengthen the legal and institutional environment
  – Develop good investment projects and do only PPPs with VfM
  – Implement transparent fiscal accounting and reporting
  – Improve budgeting procedures putting PPPs on an equal footing with traditional procurement
• We welcome OECD’s initiative to develop a comprehensive set of general principles on PPPs
• **Bottom line:** Progress being made but significant challenges remain
Thank you!