

PUBLIC PRIVATE PARTNERSHIP IN CONSTRUCTION INDUSTRY

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Abstract: PPP is an agreement between the government and the private sector for the purpose of provisioning of public services or infrastructure with a common vision, the enterprise of both the sector is blended in a platform for accomplishment of mutual benefits. It is one of the alternatives in the hands of Government to attract the investment when it cannot alone bear the burden infrastructure development. An attempt has been made in the study to examine its execution at different project level in real life situation in Indian context. Many states in India have resorted to PPPs for financing infrastructure and other public utility services.

Keywords: Public Private Partnership, Construction, Build-Own-Transfer, Build-Own-Lease-Transfer

I. INTRODUCTION

A public-private partnership (PPP) is a government service or private business venture which is funded and operated through a partnership of government and one or more private sector companies. These schemes are sometimes referred to as 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), 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 it more attractive to the private investors. 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.

There are usually 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 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.

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 bank lender(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.

In India, the Government of India defines a P3 as "a partnership between a public sector entity (sponsoring authority) and a private sector entity (a legal entity in which 51% or more of equity is with the private partner/s) for the creation and/or management of infrastructure for public purpose for a specified period of time (concession period) on commercial terms and in which the private partner has been procured through a transparent and open procurement system."

The union government has estimated an investment of \$320 billion in the infrastructure in the 10th plan. The major infrastructure development projects in the Indian state of Maharashtra (more than 50%) are based on the P3 model. In the 2000s, other states such Karnataka, Madhya Pradesh, Gujarat, Tamil Nadu also adopted this model. Sector-wise, the road projects account for about 53.4% of the total projects in numbers, and 46% in terms of value. Ports come in the second place and account for 8% of the total projects (21% of the total value). Other sectors including power, irrigation, telecommunication, water supply, and airports have gained momentum through the P3 model. As of 2011, these sectors are expected get an investment of Rs. 20, 27,169 crore (according to 2006–2007 WPI).

II. PUBLIC PRIVATE PARTNERSHIP

Public-Private-Partnership or PPP is a mode of implementing government programmes/schemes in partnership with the private sector. The term private in PPP encompasses all non-governmental agencies such as the corporate sector, voluntary organizations, self-help groups, partnership firms, individuals and community based organizations, PPP, moreover, subsumes all the objectives of the service being provided earlier by the government, and is not intended to compromise on them. Essentially, the shift

in emphasis is from delivering services directly, to service management and coordination. The roles and responsibilities of the partners may vary from sector to sector. While in some schemes/projects, the private provider may have significant involvement in regard to all aspects of implementation; in others s/he may have only a minor role.

PPPs have become attractive to governments as an off-budget mechanism for infrastructure development as:

- They can enhance the supply of much-needed infrastructure services.
- They may not require any immediate cash spending.
- They provide relief from the burden of the costs of design and construction.
- They allow transfer of many project risks to the private sector.
- They promise better project design, choice of technology, construction, operation and service delivery.

The flowchart below shows the various components of Public Private Partnership:

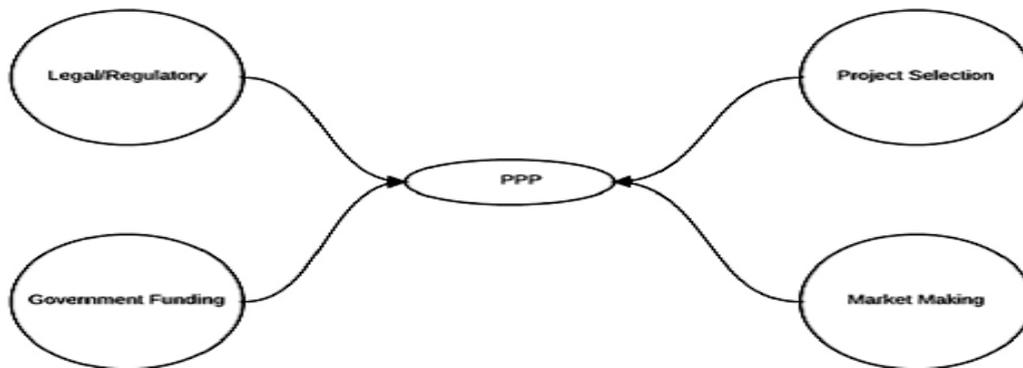


Figure 1 Components of PPP

III. TYPES OF PUBLIC PRIVATE PARTNERSHIP

PPPs broadly refer to long term, contractual partnerships between the public and private sector agencies, specially targeted towards financing, designing, implementing, and operating infrastructure facilities and services that were traditionally provided by the Government and/or its agencies. These collaborative ventures are built around the expertise and capacity of the project partners and are based on a contractual agreement, which ensures appropriate and mutually agreed allocation of resources, risks, and returns. This approach of developing and operating public utilities and infrastructure by the private sector under terms and conditions agreeable to both the government and the private sector is called PPP.

Types of PPP:

Service Contract:

Under a service contract, the Government (public authority) hires a private company or entity to carry out one or more specified tasks or services for a period, typically 1–3 years.

Management Contract:

A management contract expands the services to be contracted out to include some or all of the management and operation of the public service (i.e., utility, hospital, port authority, etc.).

Lease Contract

Under a lease contract, the private partner is responsible for the service in its entirety and undertakes obligations relating to quality and service standards.

Concessions

A concession makes the private sector operator (concessionaire) responsible for the full delivery of services in a specified area, including operation, maintenance, collection, management, and construction and rehabilitation of the system.

A. Build operate Transfer

Under BOTs, the private partner provides the capital required to Build the new facility, Operate & Maintain (O&M) for the contract period and then return the facility to Government as per agreed terms.

The main characteristic of BOT and similar arrangements are given below:-

- Design Build (DB)
- Build Transfer Operate (BTO)
- Build Own Operate (BOO)
- Build Own Operate Transfer (BOOT)
- Design Build Operate (DBO)
- Design Build Finance Operate (DBFO)
- Design Build Finance Operate and Maintain (DBFOM)
- Build Own Operate Remove (BOOR)

B. Build Own Lease Transfer

Under this type of PPPs, a facility which already exists and is under operation, is entrusted to the private sector partner for efficient operation, subject to the terms and conditions decided by mutual agreement. The contract will be for a given but sufficiently long period and the asset will be transferred back to the government at the end of the contract.

Leasing a school building or a hospital to the private sector along with the staff and all facilities by entrusting the management and control, subject to pre-determined conditions could come under this category.

IV. ADVANTAGES & DISADVANTAGES

Advantages:

- Mitigates and properly allocates risks
- Provide incentives for lowering costs
- Ensures value for money
- Attract the right skills and management expertise
- Promotes innovation
- Reduces corruption and waste
- Reduce burden on taxpayers
- Risk Transfer
- Long term nature of contract
- Private sector management skills

Disadvantages:

- Poor Value for money
- Higher Transaction cost
- Higher Capital Cost
- Insecurity
- Short term rigidities

- Culture Gap
- Public sector staff concern

V. CASE STUDY: VADODARA-HALOL TOLL ROAD

Project Description:

The Vadodara Halol Toll Road (VHTR) was one of the first State Highway widening projects developed on a Public Private Partnership basis in India and it has subsequently paved the way for a large number of projects to be undertaken on a similar format in Gujarat and the rest of India.

VHTR was an initiative commissioned as a part of the Vision 2010 - an infrastructure master plan developed by the Government of Gujarat (GoG). The underlying principle of the vision was to develop infrastructure projects in Gujarat by attracting private sector participation. The project involved widening and strengthening of 32 kilometres (km) of the existing two-lane State Highway (SH 87) connecting Vadodara to the industrial town of Halol into a four-lane tolled expressway.

The GoG commissioned the Infrastructure Leasing and Financial Services (IL&FS) to jointly develop two road projects in the State, i.e. Vadodara-Halol and Ahmedabad-Mahesana. The Roads and Buildings Department (R&B), GoG and IL&FS signed a Memorandum of Agreement (MoA) to this effect on 31st October 1995.

A special purpose vehicle (SPV) was constituted for this purpose named the Vadodara Halol Toll Road Company Limited (VHTRL)⁴. VHTRL in turn appointed a contractor, through international competitive bidding, for the construction, operation and maintenance of the project. The construction of VHTR commenced on 1st March 1999 and completed on 15th September 2000. The toll operations commenced on 24th October 2000. VHTRL manages, operates and maintains the road for 30 years starting from 2000.

PPP Structure of the Project:

The VHTR project is developed under the Built, Own, Operate and Transfer (BOOT) basis. For the purpose of effectively executing the project, an SPV – VHTRL was created. VHTRL was promoted by the GoG and IL&FS. It entered into a concession agreement with GoG to design, finance, build, operate, maintain, and transfer the facility after recovery of a predetermined return. VHTRL in turn appointed a consortium of Punj Lloyd Limited and IRCON International Limited as contractors to construct, operate and maintain the project. The contractors also have an equity stake in VHTRL.

The scope of work for VHTRL included the following activities:

Construction:

This included the design and completion of the road, including the pavement, cross drainage system, bridges, toll facilities, medians, separators, road furniture, and horticultural aspects.

Management, operation and maintenance:

This includes toll collection, operating the toll plaza, traffic regulation and maintenance of the facility. It also includes special maintenance activities such as eliminating potholes in the pavements, replacing drainage structures, road markings and signage, cleaning lanes, shoulders, right-of-way strips, structures, maintaining operational installations and drainage facilities. Rehabilitation works include preliminary works, slurry seals, surface treatments, resurfacing and emergency works.

In consideration for performing its obligations, VHTRL has a right to charge toll directly to the users of VHTR and is permitted to earn from advertisements, hoardings and other commercial activities at the project site.

The concession period is for a period of 30 years. In case VHTRL is unable to recover the total cost of the project, including a 20% return, within 30 years from the date of operation, the concession period shall, at the request of VHTRL, without qualification be extended by GoG for a period of two years at a time until the total project cost and returns have been recovered by VHTRL. Any request for an extension needs to be supported by a certificate from an 'Independent Auditor' confirming the same.

Further, the GoG may also grant certain development rights to VHTRL. The terms and conditions governing the utilization of development rights shall be specified in a separate agreement entered into between the parties. All the development income generated by VHTRL shall be applied towards the recovery of the total cost of project and the returns.

The land for the project is leased to VHTRL by GoG through a lease agreement between the parties.

On the termination of the Concession Period, the Concessionaire has to transfer and assign to the GoG all the Concessionaire's rights, title deeds, and interest in the facility for a nominal consideration of Rupee 1. The Concessionaire also has to deliver to GoG operating manuals, plans, design drawings and other information to enable it to continue operating the facility.

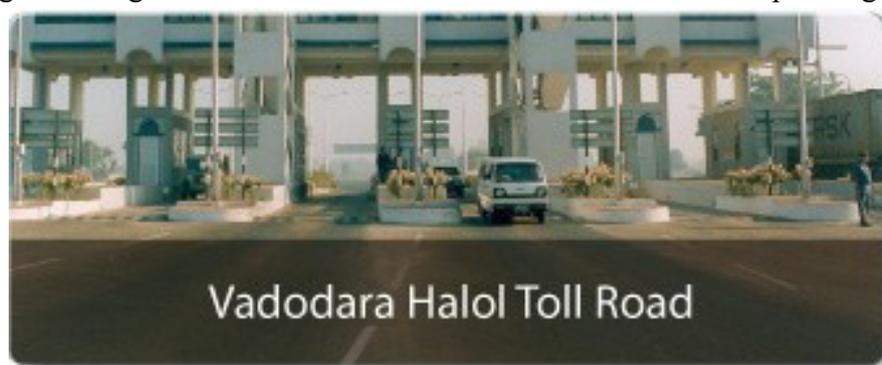


Figure 2 Vadodara Halol Toll Road
(Source: <http://www.ilfsindia.com>)

CONCLUSIONS

The current scenario of PPP suggests that it is limited only in transportation sector incorporating BOT and BOT Annuity models in most of the developing countries. But the use of PPP models in other sectors is also very handful.

One of the persuasive arguments in favour of PPP is the promise of better quality of service through clear customer focus. It is also argued that introduction of PPP would reverse the years of chronic under-investment through mobilizing public and private capital. Although experience, in this regard, shows that it did not open the floodgates to private sector participation. Perhaps, there is a need for greater public participation in PPP projects through 'risk sharing' to assure the private sector of the necessary 'comfort' they may look for. PPP agreements also provide room for (ex-post) evaluation.

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