KEYNOTE ADDRESS TO

THE PRIVATE SECTOR LAUNCH OF THE STANDARDISED PPP PROVISIONS

PRETORIA : 6TH MAY 2003

TREVOR MANUEL, MINISTER OF FINANCE, SOUTH AFRICA

Ladies and gentlemen, distinguished guests.

It is most gratifying to see so many eminent people, so many lawyers, accountants, engineers, business executives, here tonight. Gratifying because I am delighted to welcome you to our modest celebration of four years of progress in our public-private partnership programme. But gratifying more particularly because such a formidable gathering of intellectual and financial capital, at a launch of some 300 folios of dense, frankly insufferably uninteresting text, which in itself represents not a single cent of business opportunity, signals that we must have got something right. There must be something in the evolution of Chapter 16 of the Treasury Regulations that has struck an alarm bell. There must be something in the interaction you have had with our PPP team that has elevated your interest above the ordinary. There must be something in the third derivative of the escalation algorithm in the fourteenth schedule of the annexure to the fifth codicil that has alerted you to the possibility of a performance bonus going astray. There must be something, something important, that has brought you here.

That thing is of course really just the fact that we are serious about making public private partnerships work in South Africa. Deeply, profoundly serious. The challenges we face – building and maintaining roads, rehabilitating our hospitals, streamlining the justice system, banking the unbanked, delivering water, preserving our biodiversity heritage, bringing computers and connectedness into schools and clinics – are deeply serious undertakings. And so when we seek to harness the resources, the project management capacity, the technology and knowledge, that resides in the business sector, in pursuit of these public purposes, we do so on the strength of legally secure, financially sound, forward-looking, affordable, cost-effective, transparent contracts.

That is why we are here. Too often, in too many countries, in too many projects, weakly specified contracts have led promising partnerships into conflict, contestation, failed services, unmet targets, unpaid bills and court proceedings. Hope has ended in disillusionment. Opportunity has ebbed away. The poor have ended up paying for services they don't receive. Business sector growth prospects have withered and died.

We will not go down that route. Those who think that service delivery contracts can be signed off on the basis of casual disregard for procurement procedures and a half-hearted flip through the pages do not belong on our government side negotiating teams. And those businesses who think that government contracts are a licence to overcharge for shoddy services or to offer system designs that meander from one mediocre consultant's report to the next incontinent permutation, should know that they also do not belong in this partnership. Our approach begins with a non-negotiable shared understanding. We are together here, custodians of our nation's well-being and our children's heritage. And these hundreds of pages of draft contract terms are about ensuring that we exercise that custodianship correctly. Nothing less. We have, over the past several months, put our best efforts into developing these drafts, and our invitation is that you share with us, over the month ahead, in refining the standard provisions of this custodianship. It is a serious undertaking, and I am deeply grateful that you are here to share it with me.

But I would also like to say that the progress we have made to date, represented in part by the text of these draft provisions, but also by the 50 contracts in progress, or under negotiation, or in feasibility stage, in terms of Chapter 16 of the Regulations, and the toll road concessions and prison projects that pre-date the establishment of the PPP Unit, and the various initiatives that have been supported by the Municipal Infrastructure Investment Unit – this evolution of a philosophy of risk sharing and far-sighted project management, owes its success in no small measure to your efforts as advisors, as investors, as project leaders and as participants in long hours of project development, refinement and negotiation.

We have learnt a great deal, and I am sure you have shared in this learning curve, both before and since our *Strategic Framework for Delivering Public Services through Public-Private Partnerships* was published three years ago. That learning is in itself a partnership of non-trivial dimensions, and I would like to pay tribute to the unsung efforts of all those who have joined in this process, both those whose efforts have been charged by the hour and those whose motivation has been more qualitatively calibrated.

This government's overwhelming priority is to meet the socio-economic needs of all South Africans, and in particular, to alleviate poverty.

In seeking to address these challenges, government has to balance short and long-term goals, and pursue its objectives in a sustainable manner. Economic policy and the use of resources must therefore be affordable. Government cannot impose undue risks or burdens on future budgets and future generations through the imprudent commitment of scarce resources to unaffordable projects.

Two key policy themes were recently emphasised in our Medium Term Budget Policy Statement:

- The focus of public spending on programmes that promote human development and broaden economic opportunities; and
- The targeting of additional expenditure on capital formation and maintenance of infrastructure assets.

The planned increase in capital and infrastructure spending takes into account a number of considerations:

- We have to arrest the deteriorating condition of parts of the public infrastructure estate – including buildings, roads, and rail rolling stock – and reverse the escalating cost of rehabilitating or replacing this asset base. The problem is particularly evident in the provincial and local spheres where budgetary and capacity constraints led to marked reductions in infrastructure spending in past years. Progress remains uneven, but the recently published *Intergovernmental Fiscal Review* illustrates clearly and in considerable detail how this tide has turned.

- We have to deal with the remaining institutional weaknesses and the resulting inefficiencies, underspending and slower than anticipated delivery in several priority area.

- In some localities, floods and other disasters have added to the urgency of rehabilitating the infrastructure and road network.

- We recognise the important role that infrastructure plays in improving quality of life in poor communities, often through relatively labour-intensive activities that contribute significantly to job creation and – as President Mbeki has emphasised – reliance on normal participation in income-earning occupations.

- Then there is also the impact of improved infrastructure on industrial development and tourism, which are of vital importance both to economic growth and job creation.

In addressing these challenges, we seek several objectives through the design and structure of public private partnerships.

- PPPs require outputs and service level standards to be specified clearly and transparently, together with a comprehensive identification of costs and risks;
- Efficiencies arise from the integration of the design, building, financing and operation of assets that is intrinsic to a well-structured PPP;
- The private sector tends to bring higher levels of innovation to planning and project delivery, and has a sharper and more timely engagement with technology, with significant spin-offs for skill transfer in the public sector;
- The introduction of enhanced management skill into public service delivery is of considerable benefit in service quality and effectiveness;
- The contractual assurances of specified service standards and affordability also bring stricter and more effective management of risk.

Of course, these objectives also require that government departments or agencies embrace new approaches and develop greater depth of project negotiation and management capacity. This is both about meeting and engaging with the strategic issues that arise on equal terms, but is also about the greater challenge of representing the wider interests of citizens and taxpayers, and ensuring that democratic accountability is not undermined by the dispassionate decentralisation of contract negotiation.

There are three critical requirements of PPPs which, as you know, have been elevated to the status of doctrine in the current Treasury Regulations.

- A project must be affordable;
- It must provide value for money; and
- It must transfer appropriate technical, operational and financial risk to the private party.

Let me take the liberty of suggesting a few aspects of these criteria that you might want to bear in mind as you examine the draft Standard Provisions in the weeks ahead. Think of these, perhaps, as Ministerial concerns.

Affordability. This means, of course, that we will not commit budget expenditure that is not available. This sounds obvious, but it is astonishing how often the initial design or project specification falls into the trap of aiming for higher levels of service than the country can readily afford. But affordability is also about much more difficult, socially nuanced considerations. A sensitive issue in toll road project design, for example, is the structure of tariff-setting, including discounts for regular local traffic users, and appropriate differential costs on distinct categories of road users. Affordability is both about budgetary considerations and about wider human, social or environmental considerations. Analogous issues arise in water concessions or projects involving access to land and ecological assets. Our toll road concessions involve a considerable shift of these responsibilities to concessionaires. Needless to say, the issues remain in the public domain and so remain “Ministerial concerns” – but notice that there is now an implicit partnership, or shared custodianship between Government and the concessionaire in this unavoidably contested terrain of public service tariff-setting. And affordability, in this public terrain, is not just about a capacity to pay and a fair balance between outlay and reward, but it is also about avoiding the unnecessary exclusion from public goods or services of those who could be accommodated without cost or inconvenience to others, but who lack the means to pay. It is, in other words, about familiar problems of public utility tariff-setting in the presence of excess capacity and declining marginal costs.

Value for money. We have borrowed from international experience, and we look for an intelligently structured “public sector comparator” against which we can assess the case for bringing profit-seeking capital into the delivery of public services. But of course we are also stretching the demands on our projects to new lengths, and we are placing high demands on bidders to respond with imagination and innovation. We want our PPPs to produce high standards at affordable cost; we want to see impetus given to black economic empowerment; we want to see local economic development spin-offs for small and medium businesses; we want to see skills transfer; and we want to see job creation. All of these “add value” in increasingly complex and qualitative ways. But they make the public sector comparator increasingly irrelevant or artificial as an evaluative benchmark. They also bring additional performance criteria and distinct risks, often in the absence of appropriate data and agreed indicators. I said I would mention my Ministerial concerns, I leave it to you to prepare the appropriate solutions.

The transfer of risk to the private party. The doctrine of original sin: private interests collude to undermine the public good; pass on the game-keeper’s role to the poacher. In the perfect PPP, all risks are fully covered by offsetting profit-seeking interests, the public good is assured by a lump-sum unitary charge, uncertainty is disposed of through complete contract specification. And if we happen to have missed some critical future event, like the invention of perpetual motion, we can re-contract because time moves backward just as easily as it progresses forward. Unfortunately, life isn’t quite like that. Information is unavoidably incomplete; the possibilities for collusion are unlimited; there is the practical inconvenience of complying with awkward features of the tax laws. So the risk-transfer objective is really about a sensibly structured set of compromises. The concern here is that it is so much easier to specify the elements of the risk matrix that are financial, quantifiable, businesslike, auditable and well-behaved. These are the risks that can for the most part be disposed of through assignment and pricing. But there are other aspects of the world we inhabit that are best addressed through collective decision-making, through the exercise of voice, through consultation and democratic processes. Some risks can be assigned and then managed; others are better managed and then assigned. Again, I merely articulate a concern; I look forward to further engagement.

As many of you know, the PPP Unit has already published several guideline documents to assist national and provincial departments and government agencies in preparing and overseeing PPP transactions. The development of these Standardised Provisions, however, represents a step-change in our PPP programme.

This has been a complex and exhaustive project, drawing extensively on external expertise. It has been a monumental learning project for the National Treasury, and indeed I believe that the influence and ramifications of this undertaking will extend beyond our borders in the evolution of PPP practice and procedures internationally.

I know that – once you have had the opportunity to work through these pages – you will want to join me in congratulating Aijaz Ahmad, who leads our PPP Unit, and Uven Bunsee, who has so ably steered this initiative, Della Levinsohn and Alice Rennie who served as coordinators, those who have served on the Steering Committee and Review Group and so many others who have contributed to the project. But the job is not yet done, and so let me urge you to work through the details, reflect and share your reflections, and assist us in completing this particular public-private partnership.

I thank you.