E

Public-private partnerships

Introduction

To revitalise the economy and meet the goals of the National Development Plan, South Africa needs to establish a more competitive infrastructure base. However, government capital budgets have come under significant pressure in recent years due to weak economic growth and competing priorities, such as funding for higher education and compensation of employees. Greater use of well-managed public-private partnerships (PPPs) can improve planning and feasibility studies, resulting in more rigorous project assessment and accountability, and draw in private financing for public infrastructure projects.

The Infrastructure Fund, first announced in 2018, creates an opportunity for more partnerships between government and the private sector through the use of blended finance. A pipeline of economic and social projects, most of which are expected to be PPPs, is being developed with the private sector. The fund is discussed in more detail in Annexure D.

The difference between PPPs and traditional government infrastructure projects

A PPP is defined as a contract between a public-sector institution and a private party, where the private party performs a function that is usually provided by the public sector and/or uses state property in terms of the PPP agreement. Most of the project risk (technical, financial and operational) is transferred to the private party. The public sector pays for a full set of services, including new infrastructure, maintenance and facilities management, through monthly or annual payments. In a traditional government project, the public sector pays for the capital and operating costs, and carries the risks of cost overruns and late delivery.

Reviewing the regulatory framework for PPPs

To date, 34 PPP projects valued at R89.3 billion have been completed. PPPs have been successful in South Africa, although a number of challenges have arisen over the years. New PPP transactions have been declining, from an estimated R10.7 billion in 2011/12 to R5.6 billion in 2019/20, in part because these projects are perceived to involve high costs. In September 2019, the National Treasury initiated a review of the PPP regulatory framework to address these challenges and recommend changes to the framework to improve its effectiveness and encourage private-sector participation. With support from the World Bank, the National Treasury worked with experts on this review, which is nearing completion.

The regulatory framework includes PPPs regulated by the Public Finance Management Act (1999) and the Municipal Finance Management Act (2003). The public and private sectors have contributed important suggestions, which, alongside lessons learnt, have been incorporated into the draft final recommendations report. The National Treasury will present the recommendations at a validation workshop in March 2021 to stakeholders and PPP practitioners before formally adopting the recommendations. After the workshop, the approved recommendations will be published on the National Treasury website. These recommendations will be implemented in 2021/22.

The recommendations include:

- Integrating PPP policies into the infrastructure delivery management systems.
- Amending regulations and legislation to exempt smaller projects from onerous requirements, taking specific conditions into consideration.
- Centralising and improving the screening and assessment of projects and proposals.
- Establishing a PPP regulator, and country- and sector-specific benchmarks for cost and efficiency.
- Standardising project preparation requirements for certain smaller projects and contract templates across sectors.
- Building PPP capacity across government institutions including contract management practices.
- Setting out clear timeframes for different project phases to reduce the PPP project planning cycle.
- Building and retaining the skills required in the public sector to improve the planning and management of PPPs.
- Implementing measures that facilitate market consultation to obtain feedback on projects and inform the procurement strategy.
- Simplifying value-for-money assessments and introducing economic valuations of all projects above a certain threshold.
- Streamlining the procurement evaluation process for PPPs to reduce the time it takes to appoint a preferred bidder.
- Installing a system that monitors and evaluates projects to draw lessons for better project planning and implementation.

Most of these recommendations, focused on national and provincial PPPs, also apply to municipalities. In addition, the review of the municipal PPP framework specifically recommended reducing the number of public consultations, increasing the involvement of the Municipal Infrastructure Support Agency and simplifying the unsolicited proposal framework in line with municipal regulations.

Contingent liabilities

Most national and provincial PPPs are guaranteed by the Minister of Finance and create a contingent liability. Government incurs contingent liabilities only when a contract is terminated. PPP projects where a public-sector institution makes a unitary payment have contingent fiscal obligations to compensate the private sector if the contract is terminated before its expiry date. PPP agreements can also impose other fiscal obligations on government that are not defined as contingent liabilities. For example, where the private sector collects user charges from the public, government usually guarantees the minimum revenue, which imposes a fiscal obligation and requires budget allocations.

The National Treasury uses a four-stage approval process to ensure that contingent liabilities arising from contracts are acceptable and monitors these liabilities on an ongoing basis. There are various categories of contingent liabilities, depending on whether the termination is the result of private-sector default, government default or *force majeure* – an event beyond either party's control. Compensation depends on the reason the contract ended, but termination due to government default usually results in the greatest compensation. Table E.1 shows potential termination amounts per sphere of government.

Table E.1 Contingent liabilities by category

	Termination private party default		Termination force majeure		Termination government default	
R million	**2019/20**	**2020/21**	**2019/20**	**2020/21**	**2019/20**	**2020/21**
National departments' exposure	3 324.5	2 878.8	3 536.8	3 663.6	5 002.4	4 707.3
Provincial departments' exposure	3 159.3	2 649.3	1 889.1	1 263.4	4 514.0	4 151.2
Public entities' exposure	415.8	353.4	352.6	299.7	522.2	443.9
Total	**6 899.6**	**5 881.5**	**5 778.5**	**5 226.7**	**10 038.6**	**9 302.4**

Source: National Treasury

Estimated contingent liabilities for PPPs that are likely to accrue to government as a result of contracts terminating due to government default amount to R9.3 billion in 2020/21 – decreasing from R10 billion in 2019/20. This slight decrease was expected as government continues to pay off debt and equity owed to the private sector. Of the three spheres of government, national departments account for the greatest exposure, amounting to R4.7 billion in 2020/21. Head office accommodation projects and the Gautrain Rapid Rail Link project are the biggest contributors to government's exposure to contingent liabilities. Government manages the risk emanating from PPP contingent liabilities by closely monitoring each party's performance against their contractual obligations and enforcing regulatory requirements.

Impact of COVID-19 on PPPs

In late March 2020, government imposed strict restrictions on activities to contain the COVID-19 pandemic. These restrictions significantly affected revenues for several PPP projects. In April 2020, the National Treasury – supported by the World Bank – engaged with key stakeholders to assess potential PPP risks and contingent liabilities, and identify solutions to mitigate the effects of restrictions. The stakeholders included the Gautrain Management Agency, the Western Cape Department of Transport and Public Works, the Independent Power Producers (IPP) Office, the South African National Roads Agency Limited (SANRAL) and the PPP Unit in the Government Technical Advisory Centre.

At the moment, the effects on risks to the fiscus and contingent liabilities are considered manageable. Operational PPPs such as the Gautrain Rapid Rail Link project, SANRAL toll roads and Chapman's Peak have lost revenue. Other operational concessions such as the Renewable Energy IPP Programme[1] have not been affected by the pandemic and there is no risk that they may affect the fiscus. The project terms of IPPs that are in the construction stage have been extended, while PPPs in the planning stage may face delays in reaching financial closure as a result of the pandemic.

Gautrain

In November 2020, passenger demand was 30 per cent of pre-COVID-19 levels after a slow recovery from the shutdown of all rail transport during the strict lockdown. The Gautrain has a patronage guarantee[2] as part of the PPP agreement signed with the private operator, Bombela Concession Company. The private operator is partly liable for losses if revenue drops below a certain amount. In 2020/21, the private operator is expected to lose about R700 million and the provincial government's patronage guarantee is expected to exceed its current budget by R400 million. The Gauteng Department of Roads and Transport is expected to absorb this amount. The number of people using public transport is projected to remain below pre-COVID-19 levels for some time as a result of slow economic growth and the probability that more people will continue to work from home. The overall impact of COVID-19 on projects such as the Gautrain is unknown and will need to be assessed and quantified in future.

[1] Renewable energy independent power producers are not strictly PPPs. They are guaranteed by the fiscus and may pose a contingent liability if not managed.

[2] A patronage guarantee is a subsidy provided when the private operator's total revenue is below a contractually agreed amount.

Chapman's Peak toll road

Traffic volumes along Chapman's Peak toll road in Cape Town declined by 99 per cent in April 2020 compared to April 2019, recovering to 70 per cent of December 2019 levels by December 2020. The Western Cape Department of Roads and Transport, which guaranteed the private-sector debt payment, has had to pay about R14 million more to the private sector than budgeted for in 2020 as lower traffic volumes affected revenue collection.

Moreover, the department estimates that it will pay about R10 million more in 2021 due to reduced traffic. The decrease in tourism and increase in remote working will continue to affect traffic volumes and revenue. This is likely to increase the Western Cape's debt payments to the private sector. However, loans are expected to be fully repaid by 2023, after which the provincial government is expected to earn revenues from this road.

SANRAL toll roads

SANRAL is currently operating three PPPs: the N3 toll road, the N4 East toll road and the N4 West toll road. The effect of lower traffic volumes and revenue due to restrictions varies; however, all the PPP agreements specify that any loss emanating from traffic volumes is borne by the private operator.

Revenue collection on the N3 toll road (between Cedara interchange in KwaZulu-Natal and Heidelberg South interchange in Gauteng) has been affected by restrictions on interprovincial travel and the hospitality industry. Revenue losses have not yet been quantified. The private operator will claim these losses from its insurer.

Traffic volumes at N4 East toll plazas (between Pretoria and Maputo) dropped to 18 per cent of pre-COVID-19 levels during the strict lockdown imposed in March 2020 compared to the same period in 2019. Between March 2020 and January 2021, total traffic volumes were about 80 per cent compared to March 2019 and January 2020 levels, showing a gradual resumption of activity. Additional COVID-19 regulations imposed at borders caused delays and a reduction in traffic movement between South Africa and Mozambique during 2020, and the December 2020 closure of border posts is significantly affecting toll revenue collections. Between August 2019 and July 2020, the private operator estimated a revenue loss of R298.7 million.

Revenue for the N4 West Bakwena toll road (between Pretoria and Rustenburg) is estimated to have dropped to 20 per cent of pre-COVID-19 estimates in March and April 2020 compared to the same period in 2019. Between March and September 2020, revenue losses amounted to R371.3 million. The private operator is pursuing this claim from its insurer.

Improving the quantification of contingent liabilities

The 34 PPPs in operation account for 2 per cent of the total public-sector infrastructure expenditure budget, and therefore do not pose significant risks to the fiscus. Over the medium term, it is anticipated that this share will increase as projects are developed in partnership with the private sector through the Infrastructure Fund.

In anticipation of this increase, the National Treasury has partnered with the World Bank to improve the methodology used to quantify contingent liabilities. At present, institutions submit their contingent liabilities report as part of the process of obtaining approval before a PPP can be implemented. The National Treasury monitors these liabilities annually. Improvements that are being explored during 2021 include designing a guideline and template to help public-sector institutions report on contingent liabilities, as well as formulating measures to evaluate the private sector's ability to deliver on its contractual obligations and debt repayments.

PPP projects completed

Table E.2 shows a list of 34 concluded PPP projects undertaken since this type of partnership was first introduced in South Africa in 1998. The total value of all projects amounts to R89.3 billion. These projects are in the health, transport and roads, and tourism sectors, as well as for head office accommodation. They have been funded through a combination of equity, debt and, in some instances, government capital contributions. Most of these projects are operational, with a few having reached the end of their project term. In some instances, project durations have been extended.

Table E.2 List of PPP projects concluded in South Africa

Project name	Government institution	Type	Date of close[1]	Duration	Financing structure	Project value R million	Form of payment
Transport							
SANRAL N4 East Toll Road	SANRAL	DFBOT[2]	Feb 1998	30 years	Debt: 80% Equity: 20%	3 200	User charges
SANRAL N3 Toll Road	SANRAL	DFBOT	Nov 1999	30 years	Debt: 80% Equity: 20%	3 000	User charges
SANRAL N4 West Toll Road	SANRAL	DFBOT	Aug 2001	30 years	Debt: 80% Equity: 20%	3 200	User charges
Northern Cape fleet	Northern Cape Department of Transport, Roads and Public Works	DFO[3]	Nov 2001	5 years	Equity: 100%	181	Unitary payment
Chapman's Peak Drive Toll Road	Western Cape Department of Transport	DFBOT	May 2003	30 years	Debt: 44% Equity: 10% Govt: 46%	450	User charges and guarantee
Fleet management	Eastern Cape Department of Transport	DFO	Aug 2003	5 years	Debt: 100%	553	Unitary payment
National fleet management	Department of Transport	DFO	Sep 2006	5 years	Equity: 100%	919	Service fee
Tshwane fleet management	City of Tshwane	DFO	Nov 2015	5 years	Equity: 100%	1 612	Service fee
Gautrain Rapid Rail Link	Gauteng Department of Public Transport, Roads and Works	DFBOT	Sep 2006	20 years	Debt 11% Equity: 2% Govt: 87%	31 800	User charges and patronage guarantee
SANRAL Gauteng Freeway Improvement Plan Toll Road	SANRAL	DFBOT	Oct 2007	20 years	Debt: 100%	20 000	User charges
Water and sanitation							
Dolphin Coast water and sanitation concession	KwaDukuza Local Municipality	DFBOT	Jan 1999	30 years	Debt: 21% Equity: 18% Govt: 61%	130	User charges
Mbombela water and sanitation concession	Mbombela Local Municipality	DFBOT	Dec 1999	30 years	Debt: 40% Equity: 31% Govt: 29%	189	User charges
Correctional services							
Mangaung and Makhado maximum security prisons	Department of Correctional Services	DFBOT	Aug 2000	30 years	Debt: 88% Equity: 12%	3 600	Unitary payment
Information technology							
Information systems	Department of Labour	DFBOT	Dec 2002	10 years	Equity: 100%	1 500	Unitary payment
Social grant payment system	Free State Department of Social Development	DFO	Apr 2004	3 years	Equity: 100%	260	Unitary payment
Office accommodation							
Head office accommodation	Department of Trade and Industry	DFBOT	Aug 2003	25 years	Debt: 80% Equity: 8% Govt: 12%	870	Unitary payment
Head office accommodation	Department of International Relations and Cooperation	DFBOT	Jan 2005	25 years	Debt: 81% Equity: 19%	1 959	Unitary payment
Head office accommodation	Department of Education	DFBOT	Aug 2009	27 years	Debt: 90% Equity: 10%	512	Unitary payment
Head office accommodation	Department of Environmental Affairs	DFBOT	May 2012	25 years	Debt 49% Equity: 15% Govt: 36%	2 731	Unitary payment
Head office accommodation	Statistics South Africa	DFBOT	Mar 2014	24 years	Debt 54% Equity: 9% Govt: 37%	2 533	Unitary payment
Head office accommodation	City of Tshwane	DFBOT	Mar 2015	25 years	Debt: 86% Equity: 14%	2 005	Unitary payment
Head office accommodation	Department of Rural Development	DFBOT	May 2017	27 years	Debt: 54% Equity: 10% Govt: 36%	3 991	Unitary payment

Table E.2 List of PPP projects concluded in South Africa *(continued)*

Project name	Government institution	Type	Date of close[1]	Duration	Financing structure	Project value R million	Form of payment
Health							
Inkosi Albert Luthuli Hospital	KwaZulu-Natal Department of Health	DFBOT	Dec 2001	15 years	Debt: 70% Equity: 20% Govt: 10%	4 500	Unitary payment
Universitas and Pelonomi Hospitals co-location	Free State Department of Health	DFBOT	Nov 2002	16.5 years	Equity: 100%	81	User charges
State Vaccine Institute	Department of Health	Equity partnership	Apr 2003	4 years	Equity: 100%	75	Once-off equity contribution
Humansdorp District Hospital	Eastern Cape Department of Health	DFBOT	Jun 2003	20 years	Equity: 90% Govt: 10%	49	Unitary payment
Phalaborwa Hospital	Limpopo Department of Health and Social Development	DFBOT	Jul 2005	15 years	Equity: 100%	90	User charges
Western Cape Rehabilitation Centre and Lentegeur Hospital	Western Cape Department of Health	Facilities management	Nov 2006	12 years	Equity: 100%	334	Unitary payment
Polokwane Hospital renal dialysis	Limpopo Department of Health and Social Development	DBOT[4]	Dec 2006	10 years	Equity: 100%	88	Unitary payment
Port Alfred and Settlers Hospital	Eastern Cape Department of Health	DFBOT	May 2007	17 years	Debt: 90% Equity: 10%	169	Unitary payment
Tourism							
SANParks tourism projects	SANParks	DFBOT	Apr 2000	Various years	Equity: 100%	270	User charges
Eco-tourism Manyeleti three sites	Limpopo Department of Finance, Economic Affairs and Tourism	DFBOT	Dec 2001	30 years	Equity: 100%	25	User charges
Cradle of Humankind Interpretation Centre Complex	Gauteng Department of Agriculture, Conservation, Environment and Land Affairs	DBOT	Oct 2003	10 years	Equity: 100% opex Govt: 100% capex	39	User charges
Western Cape Nature Conservation Board	Western Cape Provincial Government	DFBOT	Jul 2005	30 years	Equity: 100%	40	User charges

1. Refers to a phase in which all contract conditions of the financing established between government, private party and lenders are closed
2. Design, finance, build, operate and transfer
3. Design, finance and operate
4. Design, build, operate and transfer
Source: National Treasury