Chapter 3
Paving the Way for PPPs through Policy Reform and Institution Building

**Highlights**

- Of the Bank Group institutions, mainly the World Bank, supported by PPIAF and WBI, was active in creating an enabling environment in client countries, that is, in upstream work. Most of their support targeted LICs and Africa, using a wide range of instruments.

- World Bank upstream support to client countries’ PPP agendas was mostly delivered through sector reform. Few efforts aimed at improving fiscal management or at addressing issues of PPP awareness and commitment.

- Although sector reform plays such an important role in upstream work, it was difficult to achieve because of its complexity and the political nature of the reform process.

- More narrowly targeted upstream support—for example, building institutions for PPPs or installing a regulatory commission—worked the best.

- Key drivers of success were ensuring political commitment, raising public awareness, securing stakeholder support, and identifying PPP champions.

- The design of PPP component(s)—if and how they are embedded in a larger World Bank lending operation and if and how related knowledge products are conceived and delivered—matters, which suggests that PPIAF resources should be used more strategically.

- A lack of skills and resources for the preparation of a PPP pipeline and bankable PPP projects is a serious limitation across all World Bank-supported countries.

PPPs require their own infrastructure for development. Government authorities need to be capable of developing sector reform policies and assessing fiscal risks associated with PPPs; they should base their decisions about public procurement versus PPP on comprehensive value for money assessments and have impartial transaction advisory at hand to make PPP deals bankable and sustainable. In summary, PPPs require a fairly developed enabling environment or, as the G-20 High Level Panel put it: “PPPs require their own infrastructure” (High Level Panel on Infrastructure 2011; CEE Bankwatch Network 2008; Hammami, Ruhashyankiko, and Yehoue 2006; Irwin 2007; Sadka 2006; Ter Minassian 2004; World Bank 1998).

This chapter assesses how well the World Bank Group has assisted client countries in creating an enabling environment so that these countries can engage in PPPs. The chapter starts out describing the World Bank Group portfolio as deployed to prepare countries for PPPs, that is, “upstream work,” then assesses how far these
objectives were met and presents evidence on effects of this upstream work on subsequent PPP transactions.

Upstream work is defined as support activities that have as an objective the improvement of the country’s condition and enabling environment for PPPs. Box 2.1 in Chapter 2 summarized what constitutes an enabling environment, including more general factors, for example, sector reform progress but also PPP-specific factors related to institutions, processes, and capacity. Based on this, upstream work was categorized into (i) building consensus for PPPs, (ii) implementing sector reform (with PPP reference),36 (iii) introducing the needed regulatory regime and legal framework for PPPs, (iv) building up institutions to manage the PPPs’ process, (v) building capacity, (vi) improving fiscal management, (vii) improving governance and anti-corruption measures for PPPs, and (ix) increasing access to long-term finance through domestic financial markets.

World Bank Group Interventions to Improve the PPP Enabling Environment

Upstream support for PPPs is provided by three World Bank Group entities. The World Bank, PPIAF, and WBI were active upstream. IFC advisory, IFC investment,37 and MIGA focused on downstream support (with the exception of few IFC Advisory Services that did engage upstream—see Chapter 4). Table 1.1 summarized all PPP interventions, grouped by their up- and downstream focus. In total, 353 World Bank projects supported PPPs during FY02–12. Of these, a statistically significant sample of 254 projects was reviewed in detail. More than two-thirds of these (75 percent or 191 projects) had an upstream component. In about one-third of cases (26 percent), upstream components were found together with a downstream element (Figure 3.1).

PPIAF is a multidonor trust fund, managed by the World Bank and working in partnership with the World Bank Group, its donors and other development organizations. Of the total 683 PPIAF activities, 210 were reviewed in detail, 208 of which supported upstream interventions. PPIAF support to PPPs increased from $9 million in FY02 to $16 million in FY09 and since has slowed down significantly to $9 million in FY12. For more details on PPIAF, see Box 3.1.

In addition, WBI supported the upstream agenda in 112 projects; of these, 33 were reviewed. Most of the support was through building consensus (42 percent) and capacity building (39 percent) on a variety of issues (contract management, PPP procurement, value for money and project development among others). In addition, WBI worked on collaborative governance and issues of disclosure of information and transparency of PPPs. Of the 105 reviewed IFC advisory projects, 10 had only
upstream focus, whereas 20 had some upstream components contained in support of a specific PPP transaction.

**Figure 3.1. Share of World Bank Loans with Upstream and Downstream Components**

Most of the World Bank Group’s upstream work supported LICs, LMICs, and Africa. Of PPIAF’s 683 projects, most can be found in LICs (46 percent, by numbers) and LMICs (41 percent), with the relatively most important share concentrated in Sub-Saharan Africa, accounting for 36 percent of total portfolio volume. In contrast with other World Bank Group support, multisectoral projects dominate, accounting for 40 percent of total PPP funding (by total funding), followed by support to specific sectors, that is, energy and water, with each accounting for about 19 percent of total funding.

Similarly, the WBI capacity building support mostly focused in LICs (38 percent) and LMICs (35 percent) by numbers and on Africa (32 percent). The 191 World Bank and 13 IFC advisory with upstream components focused mostly in LMICs (49 and 63 percent, respectively) and Sub-Saharan Africa (48 percent and 28 percent, respectively). Looking at the countries’ maturity to handle PPPs, upstream work strongly supports countries that need it the most, that is, those with a nascent enabling environment, as seen in Chapter 2.
Box 3.1. Public-Private Infrastructure Advisory Facility

PPIAF is a World Bank-managed multi-donor trust fund, aimed at helping governments in developing countries improve the quality of their infrastructure through private sector involvement. Most of PPIAF activities are carried out in support of World Bank Group projects, for example, technical advisory services during the preparation of or in support of the implementation of a World Bank loan for IFC advisory services. PPIAF funds country specific or multi-country advisory and related activities focusing on upstream work, including on building institutions to enable PPPs to take place; exceptionally, PPIAF gets involved in other parts of the PPP project cycle to support pioneering transactions. PPIAF can support upstream work by other World Bank Group institutions or can also be a stand-alone intervention.

PPIAF activities provide assistance mainly through capacity building (40 percent), consensus building (37 percent), and sector reform (36 percent), typically through workshops, seminars, advice or studies. PPIAF provides capacity at all stages of the PPP project cycle on contract management, pipeline development and support to those involved in oversight of PPPs (for example, audit agencies and PPP units). Consensus building activities are generally done through training activities to build PPP awareness, and stakeholder consultation to enhance political commitment.

Sources: IEG; www.ppiaf.org.

The World Bank’s upstream support to client countries’ PPP agendas was delivered through a broad range of lending instruments. By type of instrument used across upstream and downstream, about two thirds (67 percent) of the World Bank’s work was delivered through specific investment loans (SILs), followed by adaptable program loans (APLs) with 11 percent and development policy loans (DPLs) with only 6 percent. Looking more specifically at projects that have an upstream component (but may also have a downstream component), the picture is similar. SILs again dominant, followed by DPLs, APLs, and technical assistance loans (TALs). Although TALs and DPLs almost exclusively address upstream work, APLs and SILs typically address both upstream and downstream issues. The less common instruments such as guarantees (PRGs), emergency recovery loans (ERLs), and Financial Intermediary loans (FILs) were used mostly with downstream projects (Figure 3.2).

Except for SILs, country readiness drives the choice of instrument. SILs are used throughout all countries, regardless of their PPP readiness, that is, across nascent, emerging, and developed countries. For downstream work, SILs are more often used in developed than nascent or emerging countries, however. In developed countries, the basis for a PPP framework is better defined already and SILs seem to be used for specific interventions. APLs and DPLs are more often used in nascent and emerging countries to prepare the ground. The choice of instrument is therefore an essential factor in advancing the PPP agenda and need to be made contingent of the country’s readiness.
Focus and Results of World Bank Group Upstream Work

The World Bank Group’s upstream support to client countries’ PPP agendas was mostly delivered through sector reform. About half of the World Bank’s (47 percent) and about one-third of PPIAF’s (28 percent) upstream work focused on sector reform, often as a precursor to introducing PPPs. In addition to sector reform, capacity building and building consensus for PPPs were the next most frequently addressed enabling factors. The WBI’s focus was on consensus building for PPPs (42 percent), followed by PPP capacity building (see Figure 3.3). There has also been significant support to the legal and regulatory framework in which PPPs operate. Nevertheless, in Senegal, even though the Bank helped the government developing a PPP law that excluded such an approach, its applicability has been effectively limited to a single PPP, with a new law being developed for other sectors that allows consideration of negotiated contracts.38

Efforts aimed at improving fiscal management used to be rare. Across all World Bank Group institutions, systematic approaches to the client government’s capacity to assess the fiscal implications of PPPs were rarely found during FY02–12. Contingent liabilities associated with PPPs need to be dealt with at two levels: ensuring an appropriate level of risk sharing upstream and ensuring adequate budgeting of liabilities during project implementation.
IEG’s portfolio review indicates that although World Bank Group projects tend to give attention to ensuring adequate risk sharing, downstream contingent liabilities are rarely fully quantified at the project level. The nine country cases studies corroborate this and show that in selected cases the World Bank Group has actively been building the capacity of countries to assess PPP projects, and thus the ability to assess contingent liabilities. Recent efforts to systematize and introduce a framework for assessing fiscal implications of PPPs are a valuable contribution, with outcomes yet to be seen (Box 3.2).

**Figure 3.3. Objectives of World Bank Group Upstream Support**

Sector reform objectives were the most difficult to achieve because of their complexity and political nature. The World Bank is likely to have more leverage on client countries to advance sector reform than other institutions working on the upstream agenda—PPIAF or the WBI. Despite this, success on sector reform was only evident in about half of the cases (55 percent) for World Bank loans—an important finding, given that the country case studies indicate that proper sector reform was vital for successfully implementing a PPP agenda (see Figure 3.4). This
statistical evidence from the portfolio review is corroborated by the country case studies, which found that sector reform efforts take longer than anticipated and tend to be exposed to political economy factor (see below, Drivers of Success).

**Box 3.2. World Bank Operational Note on Managing Fiscal Commitments from PPPs**

There have been few cases of World Bank Group support to managing fiscal commitments. The importance of calibrating fiscal exposure in PPPs has been known for some time. Findings from IEG’s nine country cases studies indicate that assurance has only been provided if requested by the government. In Colombia, for example, in the mid ’90s, the Bank helped the government get a handle on contingent commitments (hidden exposure), which led to a rigorous, legally required procedure. In the Philippines the issue was flagged in a recent CAS, but no work was undertaken, partly because the government felt that it was not providing sufficient guarantees. Brazil has, on its own, established exposure limits for its state and local governments (both in aggregate and by project), and some states have already reached the limit, prompting calls for federal help.

A recent Finance and Private Sector Development Sector operational guidance note “Implementing a Framework for Managing Fiscal Commitments from Public Private Partnerships” (World Bank and WBI 2013) could provide a basis for a more systematic approach by the Bank Group in advising clients and assessing risk. This framework was developed jointly with the WBI, based on the World Bank’s experience in Ghana and Kenya, where it advised the government on roles and processes in assessing its commitments with regard to its—yet upcoming—PPP pipeline.

The note provided guidance to the formulation of specific components/subcomponents of the Ghana PPP APL and thus became an integral component of sector’s lending program work in Africa. However, it remains unclear how this operational guidance note will be implemented across the World Bank Group, as it was not integrated in an overall PPP operational plan, nor were accountabilities for its execution spelled out.

**Sources:** IEG country case studies; World Bank and WBI 2013.

Sector reform efforts were particularly prominent in the water and energy sector, indicating the heavy reliance on PPPs in reform in these areas. Of all projects where the PPP agenda was pursued through sector reform, about one-third (30 percent) were water and sanitation projects and one-fifth (20 percent) energy projects. Complex sector reform efforts—that is, those in energy, railways, and water—show overall relative low success, with 67, 63, and 50 percent of them achieving their objectives, respectively.

More narrowly focused efforts to build institutions for PPPs worked the best, with more than 81 percent of interventions achieving their objective. Through such support the World Bank effectively contributed to establishing processes and institutions—for example, dedicated PPP units—advised successfully on interministerial coordination, and built capacity within these institutions. Similarly, building up consensus or installing regulatory commissions succeeded in about 75 percent of cases, respectively. Compared to relatively broad-based sector reform efforts, these types of upstream efforts are relatively targeted—which may be one of
the reasons for their success. Interestingly, apart from complexity, neither income levels nor regions are good predictors for success in upstream work.41

Figure 3.4. World Bank Achievement of Upstream Objectives and Evidence for Outcomes

PPIAF and the WBI’s self-reported results indicate a high level of achievement throughout all areas. For WBI and PPIAF, this evaluation has to rely on self-reported results measures.42 The WBI regularly surveys participants of its capacity building seminars and workshops; PPIAF assess outputs, for example, preparation of PPP sector strategy, and their immediate outcomes, for example, adoption of such a strategy document by the client government.

For selected countries, IEG also assessed broader outcomes, albeit not validated independently (see Box 3.3). According to these data, PPIAF and the WBI have largely achieved their immediate objective, with 75–100 percent of their projects rated successful. These relatively good results do not vary greatly across sector or client country income levels. Their results were analyzed more in depth in the context of the nine country case studies. Case study evidence also indicates that PPIAF activities often complement the World Bank Group PPP agenda. For example, in the case of Brazil where PPIAF supported the development of a regulatory framework; or in the case of Ghana where PPIAF resources were used for a comprehensive country level diagnostic, which in turn allowed designing the PPP APL, currently under implementation.43

Looking at results across the various instruments used, DPLs and SILs tend to perform better. TALs and APLs were found to typically promote complex reforms in and were rated below average. By contrast DPLs often related to specific PPP
upstream components, for example introduction of a PPP unit or a PPP policy framework and tended to score better (Figure 3.5).

**Box 3.3. PPIAF’s Upstream Support to the Power Sector in Brazil**

PPIAF supported the implementation of regulatory reforms in the power sector in Brazil. Brazil’s power sector has changed from a model based on tariff-subsidized, government-owned utilities and a government-run grid to a hybrid competitive model with a mix of private and government-owned utilities, mandatory competitive auctions, and an independent regulator.

In 2002, PPIAF provided assistance to the Chamber of Power Sector Crisis Management (Câmara de Gestão da Crise de Energia Elétrica), which was organized by the Brazilian government to address urgent post-crisis issues regarding the sector’s market and regulatory framework. PPIAF’s team helped identify the critical issues and design a blueprint for the new energy auction model, through its technical assistance project. PPIAF’s recommendation led to the adoption of a competitive market model based on bilateral contracts and mandatory energy auctions as a primary vehicle to introduce competition. This happened despite the strong political support for the adoption of the single-buyer model, where one sole company would purchase electricity from generators and sell it to the distributors.

PPIAF refined many of its initial recommendations with follow-up activities to help develop a new market and regulatory model for the Brazilian power sector. It also supported strengthening independent regulatory agencies. PPIAF conducted an independent assessment of regulatory roles and responsibilities of the Federal Electricity Agency and came up with the report with 29 recommendations for strengthening the agency as the independent regulator.

Key success factors of PPIAF’s support in the power sector include the high level of knowledge work and international expertise the World Bank has provided to Brazilian counterparts. PPIAF’s knowledge work was also a demand-driven, where PPIAF has given the advice to the specific areas of regulatory reforms at the request of several ministries. Compared to other sectors, where PPIAF provided technical assistance such as irrigation projects, PPP projects in the power sector have a large pool of successful implementation.

Sources: IEG country case study; IEG 2013b.

Little is known regarding how far the upstream efforts also delivered the intended long-term outcomes. Although the reaching of objectives is usually well assessed at project closure (for World Bank) or completion of the activity (for PPIAF and WBI), less is known about reaching longer-term outcomes. For about one quarter of cases there is evidence that PPP institutions and regulatory regimes are functioning and that consensus also led to action. Less is evident regarding to what extent PPP-related capacity was actually applied and sector reform led to the wanted market structure and private sector participation (about one-third of cases). As World Bank Implementation Completion and Results Reports (ICRs) are usually prepared at the time of project closure, many of these outcomes have not yet had time to materialize—or simply were not recorded.
Governments may also choose to benefit from Bank Group upstream assistance and subsequently go outside for their financing and developing. A government may take advantage of Bank Group assistance in preparing the enabling environment and a specific project, but is then approached by a group that wishes to avoid competition entry. As observed in IEG’s country case studies, lost opportunities for a PPP may also result from cases where PPP projects were given the go-ahead but subsequently were reversed when a foreign government came in with attractive terms and conditions that eventually turned the PPP back into a public investment.

**Drivers of Success of Upstream Work**

The most frequently found factors that influenced how far policy reform was successful were strong government commitment to sector reform and the availability of a capable and sustainable government champion to promote the PPP agenda. Frequent stakeholder consultation and active involvement of local staff contributed likewise to success of policy reform. By contrast, failure was generally associated with political uncertainty, power shifts during the project cycle, shift of government priorities caused by unforeseen exogenous events (for example, the Asian crisis), lack of stakeholder consultation, and project design factors. The country case studies corroborated these drivers of success and failure, which allowed gaining insights into the mechanics of these factors.
PPPs are basically about embracing market economy principles—ensuring political commitment, raising public awareness, securing stakeholder support, and identifying champions in a country are key to a PPP agenda. Upstream work was more successful when governments had clear objectives and demonstrated strong leadership and continuity. Lack of political commitment and domination of government-close enterprises and state-owned enterprises was one of the leading causes for the low success of World Bank sector reform efforts, particularly in the energy and water sectors, according to the portfolio review and corroborated by the findings of the country cases studies. Invariably, understanding of the strengths and shortcomings of PPPs, political acceptance, and ability to foster sound transactions were the result of experience with private sector involvement that spanned decades (Brazil, Colombia, and the Philippines), and even then progress was hardly steady, with periods of reform often followed by regressive phases (Guatemala and the Philippines). Box 3.4 depicts several examples of successful and less successful working with governments that lack commitment and outlines lessons to be learned from this experience.

Box 3.4. Drivers of Success and Failure in Creating and Maintaining Political Commitment and Awareness—Guatemala and the Philippines

Guatemala—Changing Priorities Stalling Transport Sector Reform Progress

The World Bank supported Guatemala as of 1998 through a TAL to structure, among other things, the transport sector, eventually introducing private sector participation. The component of this loan targeting the transport sectors was not successful. After the successful implementation of the energy (and telecom) reforms, the government ran out of time. The following government changed priorities and did not have a majority in Congress. As a result, the transport sector reform was delayed until 2010 with the enactment of the new PPP Law. The transport sector is still dominated by public works, with emphasis on construction and entrenched sector interests. Furthermore, the country has very limited fiscal capacity because of low tax revenues. The regulatory and institutional framework is not ready to carry out PPPs. The following impediments prevented PPPs in the transport sectors: (i) lack of political ownership and complex institutional setting; (ii) the small-scale limits attractiveness to private sector participation; and (iii) cumbersome bureaucratic processes to obtain environmental licenses and land access permits.

The following lessons can be drawn from the World Bank’s participation. The design of the World Bank TAL was too ambitious and complex and focused on too many sectors, given the country’s political structure (four-year mandates without reelection) and long project life cycles (six to eight years). Second, although the World Bank’s advice was still relevant to the country’s objectives (developing transport infrastructure), the implementation cycle was not in line with the government’s priorities.

The Philippines – Working Around Changing Priorities Successfully

The Bank Group faced challenges in implementing its PPP agenda during 2003–09, as a result of poor governance. There were some notable successes in the early part of the period, such as completion of the Second Subic Bay Project, but IFC’s support of Manila Airport was cancelled without disbursement. Overall,
Political commitment need not be taken as a given, but can be influenced. Evidence from country case studies indicate that World Bank Group can address lack of or inconsistent political commitment. Factors that influenced political commitment were project life cycle that were synchronized with political realities on the ground and congruence of objectives, that is, project objectives should be in line with current government priorities, as in the case of Guatemala (Box 3.4).

Upstream work in the form of sector studies showed to be helpful in the case of the Philippines as they focused the political attention on the right issues—and the public thinking which may even be more important. Building institutions, albeit not directly focused on creating political commitment, can have as side effect that the institutional roles and responsibilities become clearer and get codified which can improve the authorities’ readiness to take important decisions and deal with a complex PPP agenda, as it was the case in Colombia (Box 3.7).
Privatization of state-owned enterprises has been a strong precursor to encouraging the PPP process, as it enhances competition and usually is accompanied by regulatory reform (Brazil, Colombia, and the Philippines). Indeed, it is observed that in economies (or sectors) dominated by state-owned enterprises, PPPs are not embraced (Ghana, Guatemala, and Vietnam), as there is less competition, and regulation/oversight is unbalanced. Finally, even within the same country, PPPs could be successful in one sector and fail to gain a foothold in another because of uneven government commitment and consequent inattention to proper regulation and oversight—for example, water (Box 3.5) but not electricity in Senegal, or power but not transport in Guatemala. In China, PPPs have mainly worked in water, as other infrastructure sectors are dominated by state-owned enterprises.

Box 3.5. Paving the Way for PPPs through Effective Water Sector Reform—Senegal

Through lending and analytical work, including the Water Sector Project (closed FY04) and the Long-Term Water Sector Project (closed FY09), the World Bank supported comprehensive policy and institutional reform in Senegal in the water sector, commencing in the mid-1990s. The existing state-owned water utility was dismantled and replaced with a public asset-holding company that owns assets in the water sector, sets tariffs, and functions as the sector regulator. A framework engaging a commercial operator in water distribution was developed and a dedicated program was subsequently established to develop and implement an overall sector development strategy and coordinate interventions in the sector. These reforms were sustained and consolidated over the last 15 years.

Factors that drove the Bank’s success in Senegal’s water sector reflected several good practices: (i) guidance and support on the need to build consensus around reforms among stakeholders, including the government, unions, civil society, and donors; (ii) close support on the specific institutional, regulatory, and contractual framework of the PPP; (iii) effective adaptation of lessons of the experience from other parts of the regions; (iv) “permanent” Bank interaction with the client through field-based location of task team leaders and sector specialists and frequent headquarters missions; and (v) an effective Bank role as impartial “facilitator” as the new water company and SDE adjusted to their roles and contractual obligations.

Sources: IEG country case study; World Bank 2004c.

Addressing regulatory failure has been key to the World Bank Group’s upstream support so PPPs could gain a foothold, in particular in the energy and water sectors. As a general rule, a strong regulatory framework is a required for successful PPPs, as evidenced by IEG’s portfolio analysis and the country cases. Particularly for electricity and water, a well-functioning authority appears to be needed to ensure tariffs that are fair and that recover costs and to ensure access; not surprisingly, most World Bank projects that aimed at advancing PPPs through sector reform were found in these two sectors.

In the Philippines water PPPs have been successful in metro Manila but have not taken a hold in other cities. There is a strong regulatory framework in place in
Manila but not outside the city. In contrast, toll highways have been established both around Manila and elsewhere without awaiting the highway master plan (which has only recently been developed). In Ghana, initial progress on the regulatory front was reversed as the independent regulatory commission turned into a stakeholder commission. In Senegal, a toll highway project has been supported as a stand-alone project. In contrast, its water sector performance has been based on meaningful regulatory reforms, and the electricity sector has suffered from the failure to establish an adequate framework.

The existence of at least some basic regulations is a necessary, but not a sufficient condition for PPP success; the framework must balance market requirements with technical principles and public policy objectives, such as pro poor access, as well as optimal public sector risk exposure. Early reform efforts sometimes erred on the side of excessive public sector guarantees (Colombia, now corrected), high tariffs (electricity in the Philippines and Guatemala, subsequently reduced by subsidies), or unsustainable tariffs (Ghana (Box 3.6) and Senegal). These examples, however, showed also that launching a PPP agenda need not wait for perfect regulation in place, but can also take the approach of incremental improvement, that is, where the implementation of PPP transactions help identify changes needed.

In any case, a PPP agenda that emerges from a National Infrastructure Plan and or public investment management system will reduce uncertainty and should spur more competition in the process. The lack of such a framework has hampered transactions in Guatemala and Ghana is still coming to grip with integrating the various PPP opportunities and its national public investment priorities. And even in transport, PPPs can only be successful if there are enabling laws (such as BOT laws) and workable guidelines and policies on safeguards—where World Bank Group involvement has been beneficial (as in the Philippines).

In addition to sector reform, a PPP-specific enabling environment that included a minimum of an institutional framework, processes, and roles helped the PPP agenda take off. At the minimum, an institutional framework needs to be in place for approval of PPP projects, particularly when the public sector underwrites risk and (as in Brazil) to limit the amount of exposure underwritten by states and municipalities, as well as to ensure adherence to public policy objectives. Such a system includes transparent processes and institutional responsibilities for (i) implementing the PPP process from identifying PPP projects to the closure of the transaction and contract management; (ii) approving the most significant milestones, including fiduciary control functions; and (iii) instilling program oversight to ensure the right processes are followed. Such an institutional framework for PPPs needs to build on sound public financial management principle to ensure that fiscal exposure
emerging from PPPs is adequately assessed, controlled, budgeted and disclosed. Adequate knowledge and capacity is a prerequisite for all entities involved.

**Box 3.6. Private Energy Generation Facing Regulatory Failure—Ghana**

The World Bank has entered into a sector reform dialogue as of 1998 through the Ghana Thermal Power Project and several analytical work elements, including one on energy tariffs and their poverty and social impacts. By project closure, a relatively robust regulatory framework was instituted, including the Public Utility Regulatory Commission and the Energy Commission. The Thermal Power Project also provided extensive capacity building to these regulatory commissions. During 1998–2004 tariffs actually increased by 350 and 250 percent. However, subsequent decisions by the government to absorb the tariff increases awarded by the PURC undermined the financial viability of the sector.

Although one private company had invested in the power sector since 1995, PPPs in the generation sector still face significant challenges because of, among other things, the ineffective regulatory regime. Despite World Bank capacity building efforts, the Regulatory Commission currently faces capacity constraints, as very little practical experience among staff exists, and consequently the regulatory process has lacked the requisite industry knowledge and confidence to meet the public and private sector needs and boost investor confidence; it operates a decision-making process that is not transparent (for example, not revealing the rate-setting guidelines in deriving tariffs) and suffers “stakeholder representation,” rather than nomination based on qualification and experience. As a result, the sector suffers from electricity tariffs that are too low, as the automatic quarterly tariff adjustment mechanism was suspended.

The uneven application of tariff as a result of public outcry—as happened in 1998 and subsequent years and led to the government mandating the Regulatory Commission to withdraw increases or the government itself offering to subsidize end users—can be partly attributed to a low level of public awareness. When the government liberalized price setting in the petroleum sector, it undertook a professional campaign to explain the policy. This has not been the case on a sustained basis in the power sector.

The lesson to be learned for future regulatory reform efforts is that it is imperative that sustained public awareness campaigns become a key part of any World Bank program of sector reforms and that they engage competent professionals to institute and oversee these campaigns. In addition to the partly ineffective regulatory regime, the World Bank gave less and less attention to ensuring cost recovery tariffs, as other issues such as privatization and radical sector reform came to the fore. Moreover, at the level of the Bank team there was a dilution of responsibilities as the number of the players was enlarged. This lack of consistent and strong dialogue may have contributed to an erosion of electricity tariffs between 2004 and 2007.


Whether a dedicated “PPP unit” at the country level is needed remains to be seen; identifying a sustainable “PPP champion,” however, may facilitate inter-ministerial coordination. Dedicated PPP units may serve well as the engine of PPP development; however, their existence and proactive engagement may easily imply implicit approval of PPPs as opposed to other procurement options.
Box 3.7. The Institutional Framework for Managing PPPs—Colombia versus Guatemala

Colombia—Successful Institutional Set-Up

The World Bank Group helped Colombia twice (with 2003 and 2011 PPIAFs) with institutional reform, with full support from the government. The Bank Group and country learned mutually and improved the institutional design and the execution capability for PPPs. Colombia today has an institutional set-up that, although still evolving, is capable of undertaking PPPs.

The primary driver for success was the early and comprehensive support from the World Bank Group. World Bank support started in 2003 through the PPIAF with transport sector reform, the transition from public works to private concessions, and the establishment of the predecessor entity the National Concession Agency. Support included provisions of advice to the draft PPP law that was enacted in 2012 and subsequently used to process the fourth generation of road PPPs; it also included IFC Advisory Services support. The World Bank also advised on the organizational set-up of the PPP unit to ensure institutional and functional autonomy, condition necessary for ensuring that pipeline development was carried out without interference and that actual transactions were handled in a transparent and neutral fashion.

The World Bank supported the government in the design of the agency and its coordination with other key agencies. In addition, the WBI strengthened the capacity of the National Infrastructure Agency and the National Planning Department staff. IFC also had a significant contribution in the regulatory and institutional reform process. The experience during the structuring of the IFC Ruta del Sol Project became the model for the new PPP law.

After the development of the PPP institutional framework, the government was committed to its PPP program. The National Infrastructure Agency had staff with strong technical capacity, using public-private comparator models for assessing PPPs, a stable budget allocation, and a sound approach toward managing contingent liabilities. The unit has thus far handled a significant portfolio of infrastructure projects, including 25 road concessions covering 6,035 km, of which 875 km are already built; two railway concessions covering 625 km; two port dredging concessions (Cartagena, Buenaventura); and the airport concession in Barranquilla. It has an ambitious transportation investment plan estimated at $18 billion.

Guatemala – Insufficient Institutional Capacity with Focus on Immediate Quick Wins

The World Bank provided support in 1997–2002 through the TAL on transport sector reform, but the government did not follow up until 2010 with the enactment of the new PPP law. Although the World Bank provided regulatory advice on a concession law (2003 and 2006 PPIAFs), the concession law was never approved.

The PPP law lacks specifics. The institutional framework is also weak. There is a perceived lack of PPP operative capacity in the relevant agencies, that is, the Ministries of Finance and of Transport and the National Infrastructure Agency. The project selection process is not transparent, and there is no clear coordination with other government agencies. There is no agency with sufficient control and supervision. The transport sector is dominated by public stakeholders and there is no tariff control. The weak regulatory framework and institutional limitations severely constrain the country’s capacity to carry out PPPs in the transport sector. The weak PPP unit was created without expertise from the World Bank. The objective of the government was not to achieve institutional reform, which it thought would come later, but to achieve quickly a “few success PPP projects” to demonstrate a “new way of doing business.”

Source: IEG country case studies.
Table 3.1 summarizes several more advantages and disadvantages of a dedicated PPP unit. In any case, it is likely to remain a balancing act of exploiting the advantages while containing the disadvantages. Vested interest can play a role in a country’s PPP agenda as well—in both dedicated PPP units as well as other arrangements. These can delay the PPP process or be the root cause for lack of government commitment. Regardless of which set up is chosen, the PPP champion seems to be an essential factors in advancing a PPP agenda and should be a neutral advocate for the public interest while creating a level playing field for the private investors.

World Bank Group–supported countries that have larger PPP programs generally have at least a PPP champion (or focal point), which have evolved over time and was instrumental in interministerial coordination. Both Colombia and the Philippines have stand-alone units but have had to restructure them to address corruption and make them more transparent and effective. In Guatemala, PPPs were hampered by a lack of an adequate institutional set up to manage PPPs until 2012. Line ministries also often have units to evaluate and process transactions, and sometimes the boundaries are unclear. In contrast, a lack of capacity (as in Guatemala and Ghana) leads to paralysis (Box 3.7).

For the location of PPP champions or units, there are generally three options: (i) within the regular departmental structure of the Ministry of Finance; (ii) in an individual line ministry that is predisposed in its functions to use PPPs, such as an infrastructure ministry; and (iii) as an independent government agency that collaborates with a secretariat in the finance ministry (or equivalent) (OECD 2010), including offices attached to a Ministry of Planning or the Prime Minister’s office. Except for the last option, the solution need not include necessarily a dedicated PPP unit, as, for example, charging the Public Investment Unit with the role of a PPP champion, as is currently done in Ghana, may also work.

World Bank Group–supported PPP programs have been influenced by subregional market trends, making countries scramble to prepare for them. In Latin America, as public investment became more constrained in the aftermath of the debt crisis, private sector involvement in infrastructure grew rapidly, with the rising tide lifting individual countries whether they were ready or not. Colombia’s early PPPs were done in response to this trend, and mechanisms were not in place to properly regulate government support; this led to excessive guarantees—which in turn led to well-conceived policies to measure and limit public exposure. In a similar vein, more recently the large infrastructure gap and limited public resources in Africa have prompted an interest in PPPs as a means to raise finance for what were traditionally public sector investments.
## Table 3.1. Advantages and Disadvantages of a Dedicated PPP Unit

<table>
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<th>Advantages</th>
<th>Disadvantages</th>
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| • A dedicated PPP unit can act as a knowledge center on PPP project preparation, negotiation and execution.  
• Centralization of knowledge can provide cost savings for government | • Knowledge can be supplied by internal and external project advisors appointed directly by individual ministries/agencies with specific expertise in the relevant sectoral area and/or project issues. |
| • A dedicated PPP unit can help regulate the creation of PPPs by government organizations to ensure that they fulfill all requirements regarding affordability, value for money etc. | • Line ministries/agencies together with the finance/planning ministry have expertise in assessing cost-benefits of projects and political prioritization of projects. |
| • A dedicated PPP unit can ensure that appropriate budgetary considerations are taken for PPP projects and that contingent liabilities are also evaluated. | • The closer a dedicated unit is to the relevant political leadership, the more susceptible it is to the political influence in deciding which PPP project should be initiated. |
| • A dedicated PPP unit can give a fillip to a country’s PPP program, soliciting projects, attracting potential partners/investors, building trust and good will with private partners. | • Establishing a dedicated unit may imply an implicit approval of PPP and weaken the case for other viable procurement methods. |
| • A dedicated PPP unit can separate PPP policy formulation and implementation. | • PPP policy can be formulated by the same authority that does so for traditional procurement.  
• A dedicated unit may not separate policy formulation and implementation if it can directly fund PPP projects. |

Source: Adapted from OECD 2008.

The design of PPP component(s) and how related knowledge products are delivered matters—suggesting that the PPIAF resources should be used more strategically. At times, the PPP agenda did not advance because of complexity, as in Guatemala, where PPP upstream work was cobbled together in several sectors under one loan. However, a public sector development loan worked in Colombia, and in Ghana a PPP APL has been recently been put in place to advance such operations. In both these cases, however, the project design was not only adopted to local conditions through in-depth diagnostic work but also built carefully on existing structures, including on a strong series of sector reform efforts and the lessons that had been learned. At other times, PPP activities were embedded in somewhat disconnected operations—in the sense of having different counterparts and objectives than the partnership itself—such as a PPP program in a public management reform program (see Box 3.8).
Box 3.8. Lessons on How to Embed PPP Components—Ghana

Early attempts by the World Bank to advise on a PPP program in Ghana failed. The Public Sector Management Reform Project, approved 2004, was the first comprehensive attempt to build a PPP program in Ghana. The development of a strategy for enhanced public-private cooperation was seen as a first step to operationalize this objective. Eventually, a PPP strategy was developed. The outcomes were rated unsatisfactory for the following reasons: (i) too complex a project design embedded in an inappropriate framework, that is, sector-specific reform efforts in a public sector management framework, (ii) insufficient evidence of sustained government commitment, and (iii) unrealistic time frame and elections.

Currently the World Bank and the government of Ghana are working on a comprehensive PPP program. As of the financial crisis in 2008 the government showed increased interest in expanding the role of the private sector in the economy, including in financing infrastructure. To promote this approach, the government recognized that it would first have to create an appropriate policy, legal, regulatory, and institutional environment. The World Bank and PPIAF responded by launching a series of comprehensive studies, including a systematic readiness diagnostic and benchmarking with Ghana’s peer countries, which eventually led up to the approval of a World Bank APL PPP Project. This latest PPP APL builds on a systematic effort on sector reform in energy, water, and transport and takes a comprehensive approach with specific milestones, integrating institutional and legal issues as well as emphasizing capacity. As it was only approved in 2012, outcomes have yet to materialize.

Sources: World Bank 2004a; IEG country case study.

Careful thought needs to be given to how best to design PPP interventions to ensure dialogue with the right government counterparts, and where knowledge and capacity exists or can be developed quickly. In Vietnam, for example, knowledge products aimed at the government were fragmented and have not made much of a dent in the catalyzing transaction level activities. In this regard, although PPIAF’s work was useful, timely, and of good quality (especially with very relevant just in time studies and project preparation activities), it is unclear if deployment of resources is adequately strategic. Being flexible and responsive to requests for studies certainly is a good thing, but it may miss the opportunity to fully exploit carefully designed approaches fitting strategically into the PPP agenda. A more strategically oriented approach to utilize PPIAF resources, with filters to evaluate the strategic thrust of PPIAF interventions and a more systematic linkage to CAS undertakings, may be able to achieve a broader and richer set of results than the current approach, which is driven mainly by project-level preferences.

Capacity, regulations, and incentives tend to make PPPs at the subnational level successful. World Bank Group–supported PPP programs exhibited differences between PPPs managed at the national government level and those managed by local units. PPPs at the national level depend on the success of national laws and regulations, national ownership and capacity, and credibility of undertakings. Similar factors play a role in success at the local government level, but in addition local politics also plays a role.
Where decentralization is accepted and states and municipalities have strong capacity, clear regulations, implicit or explicit incentives tied into an accountability structure, and sizable markets, PPPs at the subnational level tend to work well (Brazil and China). However, in countries where markets may be fragmented (such as the water market in Colombia, Guatemala, and the Philippines), local government units do not have adequate capacity (Guatemala) or the regulatory frameworks do not cover local government units, so performance of PPPs is generally weaker. In the Philippines the Bank is currently working on consolidating water districts and establishing a water regulator for a more conducive climate for meaningful private sector participation. Conversely, the broad approach of the World Bank Group has allowed IFC to support PPPs at the local government level, even when upstream reform efforts at the national level have had mixed results (China).

A lack of skills and resources for the preparation of a PPP pipeline and bankable PPP projects is a serious limitation across all World Bank-supported countries. PPPs are more complex than public sector operations and to the extent that they employ project financing, they can also be more challenging than simple corporate finance. Countries with adequate capacity have gradually undertaken them and in some cases have developed institutions that evaluate projects and develop a pipeline (Colombia and the Philippines). In other countries, even where assistance with upstream issues such as regulations and laws has been supported by the Bank, PPPs have been slow to take off, because of a lack of capacity (China, Ghana, Guatemala, and Vietnam). More engagement in capacity building appears needed, and the World Bank Group (the World Bank or IFC Advisory Services) could play a role in develop oversight and competition processes and institutions to develop and execute a PPP pipeline.

Conclusion

Upstream support to client countries’ PPP agenda was mostly delivered through sector reform efforts. Capacity building for PPPs, creating consensus, and building the legal and institutional framework for PPPs were the next most frequently addressed enabling factors across World Bank, PPIAF, and the WBI. Although World Bank Group projects tend to give attention to ensuring adequate risk sharing, downstream contingent liabilities are rarely fully quantified at the project level. Recent efforts to systematize and introduce a framework are valuable contributions, with outcomes yet to be seen.

Sector reform, although the most important type of upstream support, was the most difficult to achieve. Despite the World Bank’s leverage and country presence,
success on sector reform was only evident in 55 percent of World Bank loans—an important finding, given that proper sector reform is necessary to implement a PPP agenda successfully. Sector reform efforts were particularly prominent in the water and energy sectors, indicating the heavy reliance of PPPs in reform in these areas. Sector reform failed often because of the complexity and political implications of projects; project design and unrealistic timing on the side of the World Bank were factors contributing to failure as well. The choice of lending instrument is another essential factor in advancing the PPP agenda and needs to be made contingent of the country’s readiness.

Relatively narrow interventions, for example, the efforts to build institutions for PPPs, worked the best. Similarly, building up consensus or regulatory commissions succeeded more often. Compared to relatively broad-based sector reform efforts, these types of upstream efforts are relatively targeted—which may be one of the reasons for their success. Also PPIAF and the WBI’s self-reported results indicate a high level of achievement throughout all areas, and PPIAF was found complementing the work of its Bank Group partner institutions.

The most frequent factors influencing how far policy reforms were successful were strong government commitment to sector reform and the availability of a capable government champion to promote the PPP agenda. Active involvement of local staff contributed likewise to success of policy reform. Privatization of state-owned enterprises has been a strong precursor to encouraging the PPP process, as it enhances competition and usually is accompanied by regulatory reform. Technical assistance upstream had a positive role in creating government commitment as did institution building efforts, because they clarified roles and processes for taking important PPP-related decisions.

Addressing regulatory failure has been key to the World Bank Group’s upstream support so PPPs could gain a foothold, in particular in the energy and water sectors. In addition to sector reform, a PPP-specific enabling environment including a minimum of an institutional framework, processes, and roles helped the PPP agenda take off. Whether a dedicated “PPP unit” at the country level is needed remains to be seen; identifying a “PPP champion,” however, may facilitate inter-ministerial coordination in any case. The design of PPP component(s), if and how they are embedded in a World Bank lending operation with complementary knowledge products, matters and suggests that PPIAF resources should be used more strategically.

On the side of the countries’ governments, a lack of skills and resources for the preparation of a PPP pipeline and bankable PPP projects is a serious limitation
across all World Bank-supported countries. For subnational PPPs to be successful, capacity, regulations and incentives need to be in place and embedded in a clear accountability system.