

PPPS IN THE SOCIAL SECTORS: EDUCATION AND HEALTH

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Introduction

Public-Private Partnerships (PPPs) have been successfully applied in many countries to develop key infrastructure projects in key economic sectors such as transportation, telecommunications, energy and water and sewerage. In all of these cases, the impetus for PPPs has been the government's search for greater efficiencies and economies in the delivery of public services or value for money. In some countries, the PPP model has also been used to carry out infrastructure projects in the social sectors—notably education and health. In these sectors, the PPP procurement model has proven itself most useful in the construction of schools, hospitals and clinics. Additionally, the PPP model has been applied on a limited basis in the achievement of “soft” service outputs in the social sectors such as teacher performance and mentoring, human resource recruitment training and facilities management.

One of the leading questions on the minds of policymakers in developed and developing countries is how to structure financially sustainable PPP projects in the education and health sectors. This brief paper examines some of the international experience to date in these sectors and discusses some of the issues which should inform the policies being developed to promote the wider application of PPPs in the key social sectors. We will do this by describing the key features of the PPP models that are currently applied in each of these sectors and the key issues facing these projects in achieving sustainability.

The Social Sector Challenges for PPPs

It is widely understood that social sectors present a unique set of problems for PPPs that distinguish them from conventional PPPs in the economic sectors. Understanding and dealing with the special challenges facing policymakers in the social sectors is vital to developing and planning viable social sector PPP programs and projects. The main factors to be considered are the following:



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- *Segmentation of the beneficiary class.* Unlike economic infrastructure projects such as transportation and energy, education and health services are structurally segmented. That is to say, public sector services in the health and education sectors are relied upon more heavily by low and middle income groups than by the upper income and wealthy. As a result, political sensitivities and class tensions will be very high in social sector PPPs.



- *Bankability.* Segmentation of the market also imposes limitations on the ability of PPP social projects to cover all project costs with user fees and tuition payments. Consequently, government will need to provide budget support for most of these projects either through capital infusions and/or through annual budget appropriations.
- *Stakeholder involvement.* Most of the PPPs in social sectors are intended to provide services in municipalities and local communities. These projects require extensive stakeholder participation and consultation in the planning, implementation and project monitoring. Communicating with these groups is vital throughout the project life-cycle to ensure that the beneficiaries are receiving the level and quality of care required under the contracts.
- *Performance indicators.* In the social sectors, measuring the performance of the PPP against realistic performance indicators is more complicated and more important than the in the economic sectors. Auditing contract performance in these sectors is more complex because of the difficulty of establishing clear benchmarks and measuring the key performance indicators.
- *Operations and maintenance.* Operations and maintenance issues are more significant in social sector PPPs than in the economic sectors. More attention to project monitoring and the application of the performance indicators referred to in the previous paragraph is required to assess achievement of outputs and to determine when and how to apply penalties in the contract.
- *Regulatory risks.* Economic regulation in the infrastructure sectors is an integral part of the PPP process. The usual approach in PPPs is for the private sector to develop and operate facilities while the public sector focuses on supervision through regulatory agencies. No such comparable regulatory framework and institutions exist in the social sectors. In the absence of these regulatory institutions, alternative independent monitoring mechanisms need to be developed to fill that gap in the PPP framework.

EDUCATION

The key challenges facing educators and planners in developed and emerging market economies are well known:

- Inadequate physical infrastructure at the primary and secondary levels, overcrowded classrooms and insufficient and unsanitary supporting facilities;
- Teacher apathy, low salaries and absenteeism;
- Inadequate leadership and lack of managerial expertise at the school level;
- Inadequate teaching materials; and
- Lack of continuing education opportunities for teachers and administrators.

These problems have contributed to low levels of student achievement and higher dropout rates—especially in low-income communities throughout the world. Conventional procurement options are not the only options for dealing with these problems. PPP structures and private sector incentives can be effectively melded to target these problems and unlock hidden values in the value chain within the existing budgetary and resource constraints. As noted herein, worldwide experience with these innovative techniques is still relatively limited, but most state, federal and municipal governments will be moving to apply these techniques to address pressing social priorities.

In light of the extensive experience of the UK with social sector PPPs, we can identify the main categories of education PPPs as follows:

a) *Management Contracts*. These projects cover the following activities:

- Mentoring Programs
- School Management Schemes
- Teacher Recruitment and Training and
- Information and Communications Technology Training Centers.

Each of these programs in the education sector has distinct advantages and disadvantages from a PPP perspective. For instance, **management contracts** offer public access to the knowledge, expertise and management skills of private providers. These contracts are typically structured on the basis of performance incentives to attain positive outcomes. To be financially viable, these contracts often require bundling of schools into clusters to allow the private party to realize economies of scale which lower procurement costs and management fees, and yield higher levels of value for money. Management contracts also require significant stakeholder support.

Mentoring contracts involve teams of private specialists working directly with teachers and administrators focusing on various disciplines such as science, math and English. The team assumes responsibility for teacher training and monitoring.

The main difficulties encountered in these programs are measuring performance with relevant key performance indicators and baseline data, and the lack of sufficient numbers of qualified mentors and trainers and teachers. These programs also can be relatively expensive and labor intensive which limits their use on a broad scale throughout the school system. For these reasons, mentoring solutions may be of limited value in many emerging market economies.

b) *Build, lease and maintain programs* focus on new school construction and maintenance. These contracts involve performance-based availability payments executed with limited recourse project financing model. In these transactions, whole life costing and efficient allocation of risks between the public sector and the private sector are expected to yield achieve value for money. Build, lease and maintain programs for facilities are similar in many respects to core design, build, finance and

operate (DBFO) infrastructure projects and are not usually linked to discrete educational outcomes.

Results Achieved

Case studies and evaluation reports of PPP education projects confirm that positive results can be achieved in well-structured PPP education projects with the most notable gains in the construction of school buildings. Some of the results are well documented and correlate school construction with educational achievement.¹ It is too early to come up with hard data on the results achieved under management contracts and teacher mentoring programs. However, the results so far are encouraging.

HEALTH

In Great Britain, for example, the health sector has attracted significant private sector participation in the financing and construction of hospitals and provision of support services. PPPs have delivered more than 50 hospitals with a capital value in excess of £3.5 billion. The typical structure of these projects involves a Special Purpose Company operating under a PPP project agreement with the National Health Service Trust. The procurement is conducted on the basis of a DBFO model wherein the NHS Trust pays a unitary charge to the private party to cover initial construction costs and ancillary nonclinical cleaning, catering and laundry. The payment of the charge is dependent upon the private party providing the required services and begins only with the completion of the hospital.

While hospitals have received the most attention from the private sector, the UK has also experimented with PPPs provide primary healthcare and mobile clinics. They have also been used to build develop and operate Diagnostic Centers. This approach has been followed in some developing countries and is now receiving more attention by the multilateral development banks.

There are many factors which make health sector PPPs challenging to execute. First, the financial contributions received from the patients are relatively low and insufficient to cover costs and overhead. These projects therefore require a large and ongoing payment from the government. Secondly, the ongoing operating expenses of a hospital or medical facility represent the vast majority of project costs as opposed to a typical infrastructure project where the capital expenditures typically are the main cost element. It is therefore critical in any PPP health project to conform the size the project to the ability of the government to pay for the ongoing operating expenses. The worst case scenario in a health project is to develop the proverbial white elephant hospital with gleaming facilities which the government cannot afford to operate.¹

In light of the characteristics of most hospital PPPs, more attention must be devoted to the contract management and supervision of healthcare delivery outcomes. As noted in one recent article in an IFC publication, the greatest shortage facing the healthcare field is the dearth of qualified contract managers within the public sector who understand the workings of a modern health facility. The contract managers will be needed to monitor and audit the performance of the health PPPs.

Because of the fiscal constraints facing healthcare, it is legitimate to ask whether PPP health projects succeed in low income countries. The answer seems to be affirmative (see text box).

¹ Financial models can assist in determining the optimal size of the hospital based on the government's ability to pay.

The Lesotho project provided a model for tertiary care delivery in a developing country which can be replicated, provided the government is willing and able to make the political and financial commitment to a sustainable financing scheme. Other PPP schemes in health can be found in clinics, and primary care facilities, voucher systems to encourage prenatal care, and government-assisted insurance schemes. In all instances the PPP scheme is designed based on local political and economic realities.

Recently in Lesotho, for instance, the government implemented an innovative PPP scheme with a private company to build a state-of-the-art 425-bed National Referral Hospital. In addition to construction and operation of the hospital, the private company was responsible for critical services including the recruitment of doctors, nurses and other care professionals and the provision of all medical equipment and pharmaceuticals needed for the delivery of patient care. As well as running the hospital, the private company is responsible for the refurbishment, re-equipping and operation of three primary health clinics.

Conclusions and Lessons Learned

PPPs in the health and education sectors will grow in importance as governments seek to apply the lessons learned from conventional PPP schemes to the social sectors. A review of recent experience in these sectors underscores certain key factors to bear in mind in moving toward social sector PPPs:

- 1) Implementing PPPs in the social sectors require substantial attention in the first instance to affordability and financial sustainability because of the important role governments will continue to play in these fields.
- 2) Since most of these projects will be funded with government availability payments, performance indicators will be critical to measuring and monitoring performance and establishing benchmarks for penalties and bonuses.
- 3) Outside monitoring and project auditing must be rigorously enforced.
- 4) Dispute resolution should be addressed through proactive measures such as joint consultative meetings which allow the parties to review on a regular basis the operational problems as they arise in the project.
- 5) The upfront construction component of the project is likely to be the lower cost and easier risk to manage. Operational issues and costs will be far more important and complex.
- 6) Financial modeling should be developed to size the project to the government's affordability cap.
- 7) Governments will need to develop internal capabilities to manage not only the appraisal of these projects but also their implementation. As we have seen, resource constraints at the operational level are likely to be more significant than the construction risks.

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