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Analysis of the risk of corruption in public - private partnership rules

Transparency-Serbia

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The notion and purpose of public-private partnerships

Public - Private Partnerships (PPPs) represent a form of business of public sector institutions, where they, through a commercial contract arrangement, work with a selected private company in areas traditionally falling within the domain of the public sector. PPP can refer to project development, facility construction, project financing, infrastructure management, service provision to citizens and the economy and other areas. The PPP project can be implemented by a private partner or a joint venture that forms a public and private partner on an agreed scope.

These contracts are most often characterized by longevity, especially when it comes to very valuable investments, which can only be paid in the long run. Projects are financed in a mixed way, often with the participation of end users, citizens who use services. In most cases, the public partner is dedicated to overseeing the execution and creating the conditions for the contract to be implemented, while the private one undertakes the production of project documentation, the provision of funding and the management of the project. Each such partnership must contain rules on the sharing of responsibilities, risks and benefits of project implementation.

PPPs look attractive to decision-makers, or the public sector, because, on the one hand, an infrastructure object is obtained or the problem of providing services to citizens is solved, while costs that would otherwise arise through public procurements or the work of state authorities and public enterprises can "conceal" or delay. The need for borrowing and the credit burden of the state or local self-government is reduced, and instead of capital investment, an investment that has to be done at once, through the PPP, the authority gets the opportunity to allocate the costs, which are reflected in reduced or absent revenues, over a number of years. This reduction in income is less visible than the profits generated through PPPs. Public private partnership, however, does not mean that the authorities spend less public money - money is only paid later and in a different dynamics than in cases when the state itself purchases goods, services and works, and a private company carries out business *for the state, not with it.*

A good reason for using PPPs is the well-proven assumption that the private sector is more efficient than the public sector in business. It is considered that the participation of private sector partners reduces the costs of implementing the project. Competitive procedures in choosing a private partner and a good risk allocation should really ensure that the project costs are minimal. Also, when a private partner is entrusted with the long-term management of the PPP-related facility (e.g . motorway, factory, stadium), he has an interest in completing the construction as soon as possible, in accordance with the budget and that all maintenance and management costs are adequately accounted for, or smaller. All of this, however, falls apart when there is no competition in partner selection, where risks are not well distributed and when there is no control over the implementation of contractual obligations. This last risk is particularly high in situations where a private partner has the ability to reduce profits in a joint venture or in an object that is jointly managed by showing increased costs or lower incomes.

In the practice of other countries, there have been some shortcomings of the public-private partnerships, among which are the slow implementation, the inflexibility of a long-term

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arrangement, insufficient transparency regarding the commitments made by PPPs in future years and the lack of precise information on benefits that will a public partner have from investments, a risk distribution that favors a private partner, and more. On the other hand, there are cases where PPP has made better risk management, greater innovation, greater expertise, better maintenance of facilities, greater discipline related to the project budget, and more.

Main problems and possible solutions

Planning process

When deciding on the use of public funds, whether real estate, state-owned enterprises or budget funds, the underlying risk lies in the fact that this decision does not reflect public or predominant public interest, but it is made in accordance with the private one.

For example, the decision to build a water purification plant at first glance seems to be a matter of public interest. However, such a facility can be expensive, and the quality of water is relatively satisfactory, which leads to the conclusion that there are more priority issues from the angle of interest of citizens. Construction of roads is always useful for citizens and the economy, but some roads are more important than the others. Opening of sports grounds is important, but it may be more preferable for the authorities to devote themselves to the construction of preschool facilities, etc. **Choosing "wrong priorities" can be the result of ignorance, but also corruption** - when a decision-maker, a person who grants that decision, or a person who can influence them, has a private interest in carrying out a public project, to implement it in a certain way or with a particular partner.

At the first level, therefore, the risk of corruption in planning may exist when deciding to **enter a particular project at all**, whether it will be subsequently implemented as a public-private partnership or in some other way (e.g. through the public procurement of works) . Solving the problem to which the project relates will more often be the issue of choosing between a number of things that are really in the public interest, rather than situations in which the measures that are solely a matter of someone's private interest are taken. For example, it is unlikely that any political power man would have proposed to build a path exclusively leading to his private property. It is much more likely that such a private interest would be masked by suggesting that the road route would lead near to this property instead of a more favorable site, and that it would be justified by the greater possibilities for the development of tourism, industry, security reasons or solving the problem of unequal regional development.

Once the priorities have been determined, the method of their resolution should be chosen. **Public-private partnerships are never the only possible solution**. If a road should be built, there is a possibility to do so through direct government investment, through public procurement. If the problem of parking in the city center needs to be solved, there is a possibility to liberalize the market and to build private garages on its land. If the municipality should allow citizens to receive some services (such as placement of children in kindergartens), and there is not enough resources for that, they do not need to seek a

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private partner, nor to invest in building alone, but can also give vouchers or money to parents, so they would organize themselves.

The planning process should ensure that public-private partnerships are selected only when this is precisely the best solution - that is, in the long run, the most cost-effective when taking into account all relevant stakeholders. This implies recognizing these long-term goals, identifying possible ways to solve the problem, and then a properly performed analysis that will lead to the selection of the best solution. For example, the needs of citizens and the economy for electricity can be satisfied from various sources (savings or existing consumption, imports or production), from various energy sources (coal, water, solar, nuclear ...), plants may have a longer or shorter lifetime exploitation, the degree of environmental pollution that carries with it other costs (e.g. health fund) can be significantly different, the availability of credit and technology for individual solutions may be significantly different, the scope of engagement of domestic labor and businesses also. Only when all these factors are recognized and when the correct data on their significance is obtained there will be an opportunity to face arguments and to make the right decision.

The correct decision on PPP implies not only the selection of this type of contract, but also **the proper selection of the type of public-private partnership that is most favorable for a public partner** (e.g. a concession or a joint venture).

The role of citizens in planning

Since the goal of planning, when performed in the public interest, comes down to that it is necessary **to choose between several possible public interests**, which can not be realized at the same time, then it would be **precisely the citizens whose property it is all about, are supposed to be given the opportunity to declare themselves.**

Although the purpose of public-private partnerships is primarily to meet certain needs of citizens, **public-private partnership regulations do not contain rules that would ensure the voice of citizens being heard**. This applies equally to the time when the public-private partnership is planned, as well as for the period when it is realized (satisfaction with the use of services).

The precondition for declaring citizens would be the obligation of the authorities to draw up and publish a plan for public-private partnerships at an annual or perennial level. A similar obligation exists in the related Law on Public Procurement. There, the preparation of a public procurement plan for the current year is a condition for the public procurement to be implemented at all. In the current public procurement regime, these plans are published. As a consequence, interested bidders have more time to prepare for participation in procedures, and citizens and other interested persons are given the opportunity to become acquainted with the planned way of spending money in an even more detailed way than they could do by reading the program budget.

A public discussion of the planned PPP projects would have been possible even before it was included in the plan. This would enable citizens to declare their project priorities. When there is already an analysis that shows that public-private partnership is the best solution, a

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public debate could also make sense if new issues arise, for example, in relation to the price of services to be paid by end-users, in terms of the efficiency of technology that will to be sought from a potential private partner, etc. The obligation to conduct a public debate could be prescribed in the PPP Law or in the acts at the level of local self-government. The format of the public debate should be followed by the one that applies to laws, which is regulated by the Law on State Administration and the Rules of the Government of Serbia. Finally, a public debate could be conducted on the entire document - the PPP plan and the concession - or on the individual projects that were planned.

Implementation of the contract

The risks of corruption that may arise in the implementation of public-private partnership contracts are numerous. The natural **tendency of the private partner to reduce their obligations**, to overcome the risks of doing business to a public partner and to increase their own profits is not corruption for themselves. However, **the occurrence of such damage** to the public partner and public interest in general **may be related to corruption** with the public partner. This can be a matter of corruption that arises in the early stages of negotiation and contracting (some provisions favoring the interests of a private partner are entered into the contract or the provisions that protect the interests of the public partner in crisis situations are not included), but also those to which comes in during application. A typical example would be corruption related to overseeing the fulfillment of contractual obligations, which aims to ensure that the level of fulfillment of the obligations of the private partner, which is an essential element of the contract, does not undergo supervision at all or that the information is wronged.

Similarly, **there are risks when it comes to achieving benefits for the public partner**. A typical example would be managing a joint venture, where mainly the (private) partner dictates the dynamics of spending of funds and does business with related parties, benefiting when a joint venture spends assets or even operates in its entirety at a loss. The absence of supervision over contract implementation processes can significantly reduce the revenue generated by the public partner, and this lack of supervision can be the result of poor planning and negotiation, as well as corruption during the implementation of the contract.

Citizens and execution of the contract

In order for citizens and other interested parties to contribute to the suppression of corruption during the execution of the PPP contract, **there should be an obligation of a state body**, whether it is a public partner or an external supervisory authority, to monitor the implementation of the public-private partnership contract thus **collecting data from interested parties.**

Namely, as soon as there is an obligation to monitor the implementation of the contract, to keep a written record of it, the chances of corruption being detected will increase. Consequently, the chances of someone risking by entering into corrupt relationships will be decreased. Furthermore, the collected material on the implementation of the contract allows for subsequent insights and other irregularities, which may also be related to

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corruption, to be seen. However, **it must not all be left to the functioning of the supervisory authority itself**. It is not a rare situation when there is an obligation to carry out surveillance, but it is not defined how it must be conducted, at what time intervals, or how detailed, so the control itself is ineffective due to corruption. A frequent excuse in such situations is the lack of capacity (whether it is real or fingered), which explains that the supervisory authority could not determine that there was an irregularity.

Possible solutions for such disagreements are the inclusion of citizens. When the supervisory authority is obliged to collect and consider what the interested parties indicate to it, whether it is about service users, non-governmental organizations that monitor, political opponents of the government or about competing companies, their information and reports should be carefully examined and the results of this inquiries to inform the applicant. A corrupted supervisory authority will then not be able to say that the problem "has not been noticed", but will have to look back at it somehow.

Finally, **the implementation of a contract is not only a goal itself**, but it is also necessary to determine what the needs of the citizens are and to what extent they are satisfied. Therefore, a PPP or supervisory authority (e.g. a line ministry) should monitor the situation in the area and collect information on the effects of the implementation of the contract from the service user. This can be done through specially organized surveys among citizens or through constantly open channels of communication with them.

Supervision and other control measures

The supervision as a measure for reducing the risk of corruption functions as an element of ensuring (public) accountability, or putting invoices on performing a public business. In this regard, there is a significant area for improving control in the field of PPP, both at the legislative level and in practice.

In the current legal system, public-private partnerships are approved by the Government, apropos the Commission, as an "operational-independent" body. Such an approval may be inappropriate in some cases. As the budget, with all its items must be approved in the National Assembly, with only a small portion remaining for discretionary or hidden costs that the executive authority can do without prior approval, it would be logical for public-private partnerships to go through this the kind of parliamentary approval.

Parliamentary oversight is not always effective, but it is the basis of a separation of powers system. In this sense, there are already many cases where the Government or certain state administration bodies have to prepare reports for deputies on how they implement laws and strategic acts.

Even more significant is the role of the State Audit Institution. This body has the ability to evaluate the purposefulness of the public sector’s operations, so the subject of their interest could be the initial decision to enter this type of arrangement, as well as the reports on the implementation of the contract. Currently, the revision of expediency is very rare. The legal obligation does not exist, only the possibility. It would be appropriate to consider the introduction of an audit of the most valuable PPP contracts as a part of the mandatory audit

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program that is prescribed by the Law on the State Audit Institution.

In every state government operation, **the greatest risk is discretion**, the situation in which an authority or an individual can, based on its free assessment, to decide whether or not to enter a particular job. When the discretion is not accompanied by the protection mechanisms, such as fundamental analysis, oversight, transparency and review of the decision, then the risk is even greater. When it comes to the public-private partnerships, the greatest risks exist in situations where it deviates from the general rules for the application of some of the legally admitted exceptions.

A typical example may be the situation of deviation from the application of the regular rules on PPP on the basis of the circumstance that the business is concluded with an economic entity from a country with which Serbia has concluded an interstate agreement of a particular type. In general, such arrangements should be avoided, because the intergovernmental agreement may circumvent the application of any law, until the agreement violates any constitutional norm.

In order to minimize these risks, it is necessary to establish the rules, either in the Law on the Public Private partnership or in a separate law governing the conduct of negotiations preceding the conclusion of the international agreements. The current regulations do not pay attention to these issues. In order to solve this problem, an obligation should be prescribed for negotiators who act on behalf of the Government or other authorities in Serbia to ask the other contracting party before the conclusion of an interstate agreement that the international agreement contains a clause on the application of domestic law on PPPs and concessions. In this way, it would not be easy to involve into the application of exceptions to the general legal regime.

Penalties

The Law on Public-Private Partnerships does not contain penalties, which is one of its main disadvantages. Only when a legally regulated system contains penalties, as a threat in the case of prohibitions, restrictions and obligations, it can be said that the legal norms are complete. Of course, this does not mean that anything can be done with impunity within public-private partnerships. On the contrary, the most difficult and imaginary abuses are punishable by the criminal offenses, on the basis of a criminal case relating to public procurement procedures, or as abuse of office in general. In addition, pursuant to the Law on Public Procurement, some actions are punished by the misdemeanor penalties.

Recommendations

Having in mind the findings of the research on the current legal framework, the problems identified by other institutions and the analysis of the legal framework in the countries of the region, Transparency Serbia provides the following key recommendations for the amendment of the regulations related to public-private partnerships:

1. Enabling greater participation of the citizens in making decisions on planning public-private partnerships and in monitoring their implementation; to achieve this goal, it is necessary to have prescribed:

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a. the obligation to draft and publish an annual or multi-year plan of concessions and other public-private partnerships (such as a public procurement plan);

b. the obligation to organize a public discussion of the plan and / or individual PPP projects before the procedure for selecting a private partner begins, with the possibility to modify the plan based on the proposal and remarks from the public debate;

c. the obligation to monitor the implementation of the PPP contract and to gather information from the interested persons;

d. the extension of the notion of excitation, so that in addition to the users of services provided by the authorities, it includes the users of the services of the private partner who conducts the PPP project and the joint venture;

e. the obligation to collect information on the effects of the implementation of the PPP contract and the purpose for which the public-private partnership has been launched (e.g. user service surveys) as a part of the monitoring of the situation in the area.

2. Increasing transparency in public-private partnerships and concessions, **this includes:**

a. regulating public data standards and registries of the public contracts by the law;

b. the establishment of the Public Contracts Registry, in which all public private partnership contracts and reports on their implementation, will be published;

c. extension of the circle of information to be published on the public procurement procedure preceding the conclusion of the public-private partnership contract (in connection with the amendments to the Public Procurement Law);

d. the prohibition to be designated as secret contract provisions or parts of other documents in which the obligations of the public partner are prescribed or explained;

e. the conduction of joint enterprises formed within public-private partnership, under the term "authorities" in the sense of the Law on Free Access to Information of Public Importance (which allows control over the use of public resources, which does not affect the possibility of denying certain information as competitors in the market would not find business secrets of companies);

f. including information on planned public-private partnerships and the implementation of existing budget documents (primarily the Fiscal Strategy), in order to review the effects of these contracts on public revenues and public expenditures.

3. Strengthening the effectiveness of oversight of public-private partnerships planning and the performance of contractual obligations of a private partner;

a. prescribing the National Assembly's competence in the approval of PPPs and concessions with very long lifetime or those involving a high value public property;

b. imposing the obligation of the Government and / or the Commission to periodically report to the National Assembly on the implementation of the public-private partnership contract and the National Assembly's obligation to consider these reports within a certain time-limit and to make conclusions in this regard;

c. prescribing the authority that will be in charge of overseeing the implementation of the contract (PPP Commission or other body);

d. precising the rules on conflict of interest in relation to public-private partnerships, since the general rules relating to public officials and civil servants do not include all relevant actors (e.g. hired advisors), and, on the other hand, the rules of the Public procurement are not fully adequate for public-private partnerships;

e. prescribing the minimal control elements so as to include not only legal and financial indicators, but also other data that refer to the achievement of project objectives (e.g. the number of service users);

f. prescribing the obligation to conduct a competitive procedure with the application of the norms or at least the principles of the Public Procurement Law, for procurement by a joint venture formed within the framework of a public-private partnership project;

g. introducing the rules that would ensure that the Fiscal Council, from the point of view of its competencies (for example, the impact of implementing projects on the budget in the coming years), be expressed in the plans of public-private partnerships and / or individual projects;

h. specifying the possibility that the State Audit Institution, as a part of the revision of expediency, will consider the implementation of the public-private partnership contract, as well as the initial decision on the conclusion of this legal transaction.

4. The provision of special control measures in cases where the anti-corruption mechanisms of the Public Private Partnership Act do not apply due to the existence of a permitted exception to the application of that law (e.g. interstate agreements) and the avoidance of such arrangements, which includes:

a. prescribing the obligation of the negotiator on behalf of the Government before concluding an interstate agreement to require that the international agreement contains a clause on the application of domestic law on PPPs and concessions;

b. the obligation of the public partner to publish all the documents which also apply to such PPP and for which reasons for secrecy are not determined by a special decision;

c. obligation of the public partner to draft and publish a feasibility study;

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d. obligation of the public partner to provide competition to the extent possible, or to inform the supervisory authority and the public about what he has done to prevent the occurrence of adverse effects due to lack of competition.

5. Provision of the penalties for violations of the rules on public-private partnerships, which, inter alia, includes:
a. specifying the criminal act relating to abuses in public procurement and unauthorized arrangements by the bidders so as to include all cases of the most serious misconduct in public-private partnerships;

b. criminal or misdemeanor penalties in case of concluding a contract without a prior procedure;

c. misdemeanor penalties for failing to provide mandatory or specially requested documents to the PPP Commission;

d. misdemeanor penalties for failure to publish mandatory documents on the website of the public partner / joint venture;

Improving the legal position of the Commission for Public Private Partnerships in the direction of strengthening independence, which preserves:

a. a clear definition of the legal nature of this body, which now does not correspond to the classification of organs and organizations that make up the public sector of Serbia. In view of the competencies currently in place, and especially if those competencies are expanded as necessary, the Commission could be formed and as an independent state body. At the very least, the Commission could be formed as a separate administrative-professional organization (such as the Public Procurement Directorate). The Commission could also perform other related tasks;

b. the professionalization of the management by the Commission, the reduction of the number of members and the abandonment of the current concept that forms the Commission as a set of representatives of ministries and other bodies that may also be stakeholders in individual PPP projects;

c. enabling the work of the Commission in continuity by the fact that the mandate of the members of the Commission would not be related to the mandate of the Government or the National Assembly (prescribing a five-year mandate if it is a matter of election in the Assembly, appointing an officer on the basis of a conducted competition, if the Government does so, specifying reasons and procedures for eventual dismissal of a member of the Commission),

d. forming a Commission expert service that would provide it with all the necessary assistance in the work and enable greater independence in regard to the Ministry (to the economy at this point).