3rd INTOSAI Working Group on Audit of Extractive Industries Annual meeting:

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“The role of Supreme Audit Institutions in ensuring sustainable growth from extractive industries”

Extractives and Public Private Partnerships (PPP) in the East African Region, opportunities, Risks and the role of SAIs.

Passionate professionalism in PPPs

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PPP definition

- A legally enforceable contract between a government or public sector entity and a private sector firm;
- Transfers some meaningful risks onto the private partner;
- The private partner receives its payments in accordance with its actual performance;
- For the provision of some service that has traditionally been provided by the public sector.

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The key underlying rationale for a PPP is that it offers better value for the public’s money throughout the entire life of the project.
Main Sector in Oil and Gas Industry

- **Upstream**
  - Exploration & Production

- **Midstream**
  - Transportation & Refining/Processing

- **Downstream**
  - Distribution & Retail Sale
PPP Principles

- Government purchases services not just assets
- Government specifies the service outputs required
- The private sector selects and provides the inputs
- Risks are comprehensively identified and placed with the party best able to manage.
- The private sector is paid according to the actual performance it delivers.
- The objective is to achieve better value for public’s money (VfM).
Caution for Governments on PPPs

PPPs require governments

- to think and behave in **new ways** that require **new skills**.

- PPPs are more than a one-off financial transaction with the private sector. They need to be based on **firm policy foundations** and **long-term political commitment**.

- Private sector partners look for these factors when deciding **whether or not to bid** for a project.

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Caution for Governments on PPPs

‘maximum cooperation for all on Board … that we may all land safely’

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Check list on whether to do a PPP

Public agencies must typically evaluate the following:

- whether the proposed project will provide a service or benefit that is best provided by the government.
- The capital investment required to develop, operate and maintain the project.
- The technical and technological requirements of the project.
- conduct a value for money (VfM) analysis
Value for money - VfM

...a comparison of the costs and benefits of traditional government contracting versus the costs and expenses of a PPP structure over the life of the project.

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PPP structures

PPP structures for any particular project depends.

- the functions the private sector party will perform and the risks it will assume;
- The degree of operational control the public agency wants to have over any aspect of the project;
- Whether the private sector party will own the project assets at any time during the term of the agreement;
- The terms of any PPP enabling legislation.

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## Review of PPP Structures:

<table>
<thead>
<tr>
<th>Type of Contract</th>
<th>Duration (years)</th>
<th>What the Private Contractor Receives</th>
<th>Nature of Private Contractor Performance</th>
<th>Examples</th>
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<tbody>
<tr>
<td>Service Contract (outsourcing)</td>
<td>1-3</td>
<td>Fee from government for performing a non-core service</td>
<td>Definitive, often technical type of service</td>
<td>Website design and management, ICT Capacity Building</td>
</tr>
<tr>
<td>Management Contract</td>
<td>3-8</td>
<td>Fee from government for the service and a performance-based incentive</td>
<td>Manage the operation of a government service</td>
<td>Call center staffing; Seat Management; Parking enforcement, regional water supply management</td>
</tr>
<tr>
<td>Lease</td>
<td>8-15</td>
<td>All revenues, fees or charges from consumers for the provision of the service; the service provider rents the facility from government</td>
<td>Manage, operate, repair, and maintain (and maybe invest in) a service to specified standards and outputs</td>
<td>Land for ICT Infrastructure Development, Existing airport or port facilities</td>
</tr>
<tr>
<td>BOO &amp; BOOT</td>
<td>15-25</td>
<td>The government mostly pays the service provider on a unit basis</td>
<td>Construct and operate, to specified standards, the facilities necessary for service provision</td>
<td>ICT Infrastructure; e-procurement systems; e-business portals; Network of Kiosks</td>
</tr>
<tr>
<td>Concession</td>
<td>15-30</td>
<td>All revenues from consumers service provision; the service provider pays a concession fee to the government and may assume existing debt</td>
<td>Manage, operate, repair, maintain and invest in public service infrastructure to specified standards</td>
<td>Telecom operations and expansion, New airport or seaport facilities, toll road or bridge</td>
</tr>
</tbody>
</table>
PPPs have inherent risks.....

- A key principle of PPPs is that risk should be allocated to the party best able to manage it.

- The effective allocation of risk has a direct financial impact on the project.

- Achieve cost effective risk transfer not simply risk allocation for its own sake.
PPPs have inherent risks.....

- **Revenue risk (foreign exchange; price fluctuations)** - Revenues flows are generally determined by two factors: utilization levels, and tariffs.

- **Construction risk.** Because the capital construction cost of any project is one of the fundamental factors upon which financing is based, when cost overruns are incurred, the financial feasibility of the project can be jeopardized.

- **Environmental Risk** PPP projects in EIs have the potential to provoke environmental concern.
PPPs have inherent risks.....

- **Regulatory / Contractual Risk.** Although governments negotiate contract terms and conditions with their concessionaires, they are not always successful in maintaining their commitments.

- **Political Risk** Assessments of the inherent strength and stability of local political institutions are common in the investment field. As political risk increases, so does the cost of obtaining financing.
PPPs risk transfer..... CAUTION!

the cost of risk transfer must not be neglected as, given the nature of PPPs, the achievement of value for money will majorly depend on the level and cost of risk transferred to the private sector.
PPPs risk transfer····· CAUTION!

PPPs’s Optimise Risk Transfer

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Auditing of PPP contracts by SAIs.

Section 30(1) of the PPP Act 2015 of Uganda states … the Auditor General .. Shall in each financial year …. Audit each PPP entered into by a contracting Authority

30(2) ..... The Auditor General shall audit a PPP from Inception stage to the conclusion of the project.

30(3) ... The Auditor General shall within Nine months of the end of the Audit report to Parliament.
The Role of SAIs in Auditing PPPs

i. Check your core in-house skills ability to do authoritative audits of PPP projects.

ii. Did the Contracting Authority - CA state its requirements that clearly from the start.

iii. Examine how an audited body took account of these Government policy objectives....

iv. Investigate appropriate allocation of risk between the public and private;

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v. Credible project timetable with identified milestones

vi. Examine whether the audited body assessed costs and benefits of the PPP option against an alternative procurement option.

vii. Whether the audited body succeeded in maintaining competitive tension to contract award and managed the negotiations with the preferred bidder well.

viii. Contract’s provisions on matters such as performance measurement and supplier remuneration on Project.
ix. Check if CA has right governance structures for the project and maintains a good relationship with the contractor(s).

x. Whether the audited body maintains a skilled and knowledgeable team to manage the public/private finance contract.

xi. Does the allocation of risk remain optimal throughout the project lifetime.

xii. Whether the audited body planned and managed effectively its exit from the contract on its expiry.