

APPLICABILITY OF SECOND GENERATION PUBLIC PRIVATE PARTNERSHIP PROJECTS IN TURKEY: A CONCEPTUAL FRAMEWORK

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ABSTRACT

Public-private partnerships (PPP) is a procurement model in which the value for money is optimized through efficient allocation of risks, whole life service approach, private sector management skills as well as synergies from inter-linking the design, finance, construction and operations. Considering the implementation of several PPP models in Turkey, due to the dispersion of the legal regulations involving PPP, the lack of a systematic in certain context, the decree of nullity by the Constitutional Court and the Supreme Administrative Court at various times, has revealed the need for a framework law to be regulated in accordance with the Constitution. In this context, the government intends to establish a new legal and administrative framework for so called “Second Generation of the PPP Projects”. The purpose of this study is to propose a conceptual framework to assess the applicability of Second Generation PPP Projects that are on the agenda and to be implemented in the near future in Turkey. The framework characterizes the PPP projects in terms of technical, financial and economic, social, political and legal, environmental, and cultural dimensions. Each dimension is then characterized by a set of variables that are more relevant to characterize the PPP projects. The conceptual framework can be considered a starting point of future research aiming at developing a tool for assessing the expected performance of Second Generation PPP projects. This tool could be a useful instrument to support decisional process about the adoption of PPP Projects. The framework would become a benchmarking tool that can be used by stakeholders in order to derive managerial guidelines on how PPP projects should be correctly arranged and thus to move towards the best practices in applying PPP.

Keywords: Public-Private Partnerships, Procurement, Public Construction Projects, Turkey

INTRODUCTION

Partnering between the public and private sectors, in some form or other, has been fairly common practice in the construction industry for over 100 years. Depending on the level of risk, the variety of arrangements range from public procurement to privatization. Since the 1990's, there has been a rapid rise of PPPs across the world. Governments in developing as well as developed countries are increasingly using this procurement method to bridge the much needed infrastructure gap. As infrastructure funding gaps

escalate worldwide and PPPs offer an increasingly valuable solution to the financial and administrative constraints of the public sector. Nowadays, in a whole range of aspects, PPPs are becoming more mature. Different types of PPPs have been practiced in worldwide infrastructure development. In April 2004, The European Commission issued a green paper entitled On Public–Private Partnerships and Community Law on Public Contracts and Concessions in which (PPPs) were referred to as ‘a phenomenon’ (Carlidge, 2006). Also, a review of the academic literature illustrates that the concept of ‘PPP’ is an ambiguous term with a number of differing meanings and usages in various contexts. According to Gunnigan and Rajput (2010) in its widest sense, PPP is a generic term for the relationship formed between the private sector and public bodies often with the aim of introducing private sector resources and expertise in order to help provide and deliver public sector assets and services. PPPs can cover all types of collaboration across the interface between the public and private sectors. PPP arrangements come in many forms and are still an evolving concept which must be adapted to the individual needs and characteristics of each project and project partners. (Gunnigan and Rajput, 2010). In their meta analysis Ke et. al, (2009) found that various modes of PPP have been applied in different parts of the world, and the diverse concept of PPP has been publicly accepted instead of the more traditional Build-Operate-Transfer (BOT) scheme alone. A number of variations of the PPP models such as alliancing, bundling, competitive partnership, incremental partnership, integrator and joint ventures have been developed in recent years in response to the challenges faced in specific situations and sectors (Deloitte, 2009). One offshoot of the rapid growth of infrastructure PPPs is that countries remain at vastly different stages of understanding and sophistication in using innovative partnership models. Each country—and even individual states and localities—takes its own path in developing infrastructure PPPs. Many factors play a role in development including local geography, political climate, the sophistication of the capital market, the forces driving formation of partnerships and the factors enabling their creation. Nevertheless, three distinct stages of PPP maturity can be observed across the world. Deloitte (2006) assessed Turkey’s current PPP market maturity and its potential movement compared with other countries with similar partnership programmes.

Table 1. Stages of PPP Maturity Model. Deloitte (2006).

Stage 1; the developing PPP market	Stage 2; the active PPP market	Stage 3; the well-functioning and mature PPP market
<ul style="list-style-type: none"> • Establish policy & legislative framework • Initiate central PPP policy unit to guide implementation • Develop deal structures • Get transactions right & develop public sector comparator model • Begin to build market place • Apply early lessons from transport to other sectors 	<ul style="list-style-type: none"> • Establish dedicated PPP units in agencies • Begin developing new hybrid delivery models • Expand and help shape PPP marketplace • Leverage new sources of funds from capital markets • Use PPPs to drive service innovation • PPP market gains depth—use is expanded to multiple projects & sectors 	<ul style="list-style-type: none"> • Refine new innovative models • More creative, flexible approaches applied to roles of public & private sector • Use of more sophisticated risk models • Greater focus on total lifecycle of project • Sophisticated infrastructure market with pension funds & private equity funds • Public sector learns from private partner methods as competition changes the way government operations function • Underutilized assets leveraged into financial assets • Organizational & skill set changes in government implemented to support greater role of PPPs

The maturity analysis groups PPP markets into three stages. Table 1 shows the stages of PPP Maturity model. Considering the implementation of several PPP models in Turkey, due to the dispersion of the legal regulations involving PPP, the lack of a systematic in certain context, the decree of nullity by the Constitutional Court and the Supreme Administrative Court at various times, has revealed the need for a framework law to be regulated in accordance with the Constitution. In this context, the government intends to establish a new legal and administrative framework for so called “Second Generation of the PPP Projects”. The purpose of this study is to propose a conceptual framework to assess the applicability of Second Generation PPP Projects that are on the agenda and to be implemented in the near future in Turkey. The framework characterizes the PPP projects in terms of technical, financial and economic, social, political and legal, environmental, and cultural dimensions. Each dimension is then characterized by a set of variables that are more relevant to characterize the PPP projects.

MAIN CHARACTERISTICS OF PPP IN TURKEY

Current PPP Legislation and Legal Framework

Turkey is one of the first countries in the world which developed its own PPP legislation. With the Law numbered 3096 from 1984 the private sector involvement specifically in to power plants projects was allowed. PPP stakeholders are State Planning Organization (SPO), Treasury, Ministry of Finance, Public Procurement Agency, Privatization Administration, Line Ministries and Municipalities, respectively. In the first instance, private sector contributed projects in energy sector with the BOT Law numbered 3096. Law no. 3465 has removed the monopoly position of the General Directorate of State Highways for highway construction, maintenance and operation. Since 1994, Law no. 3996 is the basis law for different infrastructure areas like transportation, energy and water supply and treatment in Turkey. Electricity production, drinking water facilities have been firstly realized as BOT and later as Built-Operate (BO) projects by Law no. 4283. Sometimes transfer of ownership is not possible. In such a case, Transfer of Operational Rights (TOR) is used as a method of PPP, which is legalized by Law no. 4046, 5335, 3465, and 3096 respectively. Long Term Rent (LTR) was introduced by Law no. 5335, and 4046. Law no. 4046 allows the application of PPP Models in correlation with privatization implementations. Law no. 5335 leads to transferring operation rights of airports authorized by state to the private sector. Finally, with Law no. 5396, Built-Rent-Transfer (BRT) model of PPP is administered in health sector. According to World Bank (2012), between 1990 and 2011, with 61.862 US million, Turkey is ranked 7 out of the countries which have a foreign private sector involvement. Various forms of private sector participation in provision of public services in Turkey were realized in this respect, the concession, land tenure, the BOT, BO, TOR. Indeed, there is no another sector in the PPP projects to be successful and widely applied except energy and air transport sectors. A widely used method of concession during the Ottoman period was not used and more public services except a few examples realized by the state within the Republican era. However, with the need for public services showed an increase in quantity and quality of public services, resources allocated by the state led the investments inadequate. Deficiencies in the use of these resources efficiently, the classical management approach of public services due to failure to meet the desired quality and level of implementation of

alternative models were considered. In this context, the various legal regulations since the 1980s, the concession of public services by the private sector, but the realization of the method studied in different models. However, it was found unconstitutional by the Constitutional Court and the legal arrangements have been canceled. Due to the cancellation of the decisions of the Constitutional Court and the Supreme Administrative Court by the various periods, clutter of legal arrangements for the PPP, the lack of a systematic framework has created a need of the regulation for a framework of the law in accordance with the Constitution. In this respect, in order to establish a legal basis for a stable and healthy process handle of PPP, a draft law has been prepared by the coordination of the Under secretariat of State Planning. Former legislation consists of many weak points. Former PPP legislation consists of a limited scope. For instance, justice, education, and culture were out of the scope. There were a limited number of PPP models. Also, there was a lack of a central public body that is responsible for both setting PPP policies and coordination. First of all, the draft PPP law is aimed to overcome the aforementioned imperfections of the former legislation. The most important goal of the draft law is to allocate risk to the party which can best handle it, whether public or private. PPP Projects will be executed through flexible tender methods. Hence, the bureaucratic delay or difficulties occurred in the bidding process will be eliminated. Objectives of the draft law are listed as follows (SPO, 2012; Treasury, 2012):

- Defining the Concept of the PPP
- Standardization of the PPP Legislation
- PPP Models for identifying and bringing flexibility to the models
- Extension of the scope by adding new sectors
- Introduction of objective criteria for the PPP process
- Establishment of a central unit in charge of the PPP projects
- Introduction of the concept of the PPP Projects Risk and identification of guarantees

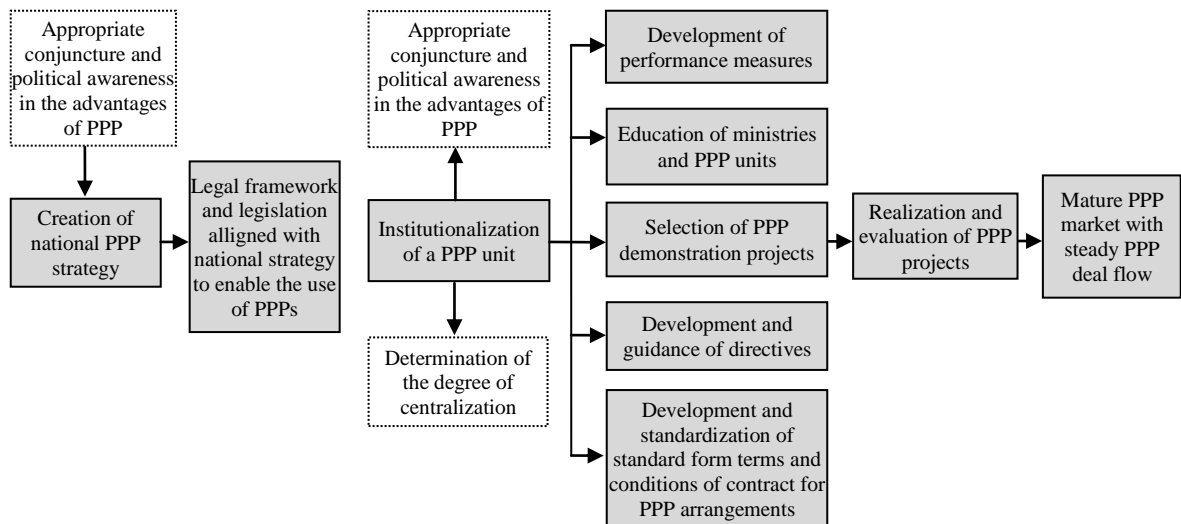


Figure 1. Proposed Framework for the Institutionalization of PPP in Turkey.

Effective legal, regulatory and contractual conditions are crucial for the success of PPPs, but such conditions can only perform successfully when they are based on and supported by a country's institutional framework. This institutional structure should aim at both

facilitating PPP development and providing clear boundaries to protect the interests of all stakeholders. The institutional framework is crucial if the public sector is to change its role from that of a single provider of services to fulfilling the duties of an independent regulator and manager (EC, 2003). The draft law revokes all the existing separate laws and regulations mentioned above and standardize the provisions applicable to all sub-models (*i.e.*, BOT, BO, TOR et al) by improving them in line with international best practices, in appreciation of the public and private sectors' roles as equal partners. It also establishes a central unit in the government to supervise and promote the model in Turkey. A supporting institutional structure will entail the development of supporting national and local legislation and regulations enabling PPPs, the development of institutional capabilities and importantly the creation of effective management and oversight structures. In Figure 1 the proposed framework for the institutionalization of PPP in Turkey is given.

Conceptual Framework for the Applicability of PPP Projects

The development of a successful PPP requires attention to a large variety of issues. PPPs must demonstrate additional value for money over and above traditional procurement systems and must be designed to maximize benefits to all parties according to their objectives. Effective institutional and regulatory structures must be developed to manage and monitor PPPs. The Public sector should be clear that some control must be given to the private sector (EC, 2003). In order to analyze the applicability of Second Generation PPP projects in Turkey, a conceptual framework has been developed as shown in Figure 2. The framework characterizes the PPP projects in terms of technical, financial and economic, social, political and legal, environmental, and cultural dimensions. Each dimension is then characterized by a set of constructs that are more relevant to characterize the PPP projects. In the framework SLEEPT attributes adopted as the SLEEPT+C mnemonic and used as dimensions (Eaton et al., 2006). The dimensions are as follows:

Social: The social and cultural norms within a nation can significantly alter the behaviors of people, ultimately affecting the operation of systems and structures in place. Because of the complex nature of PPP procurement implementing authority were also confused with privatization and thus not readily accepted in some countries (Gunnigan and Rajput, 2010). As social acceptance is indispensable in today's society, the government should never commission a PPP scheme for the sake of expediting the facilities or services provision without satisfying the requirements and expectations of the community. Citizens are more cautious about the service quality, charges, environmental impact, job opportunities, etc. when the facilities or services are delivered through the PPP mode. As a result, engaging the public to make them realize the potential impacts and benefits of the scheme, and hopefully gaining their trust and support at the end would be of significant importance (Ng et al., 2010).

Legal framework: A legal and regulatory framework that supports PPPs is meant to facilitate investments in complex and long-term PPP arrangements, reduce transaction costs, ensure appropriate regulatory controls, and provide legal and economic mechanisms to enable the resolution of contract disputes (EPEC, 2010). A PPP legal framework should include:

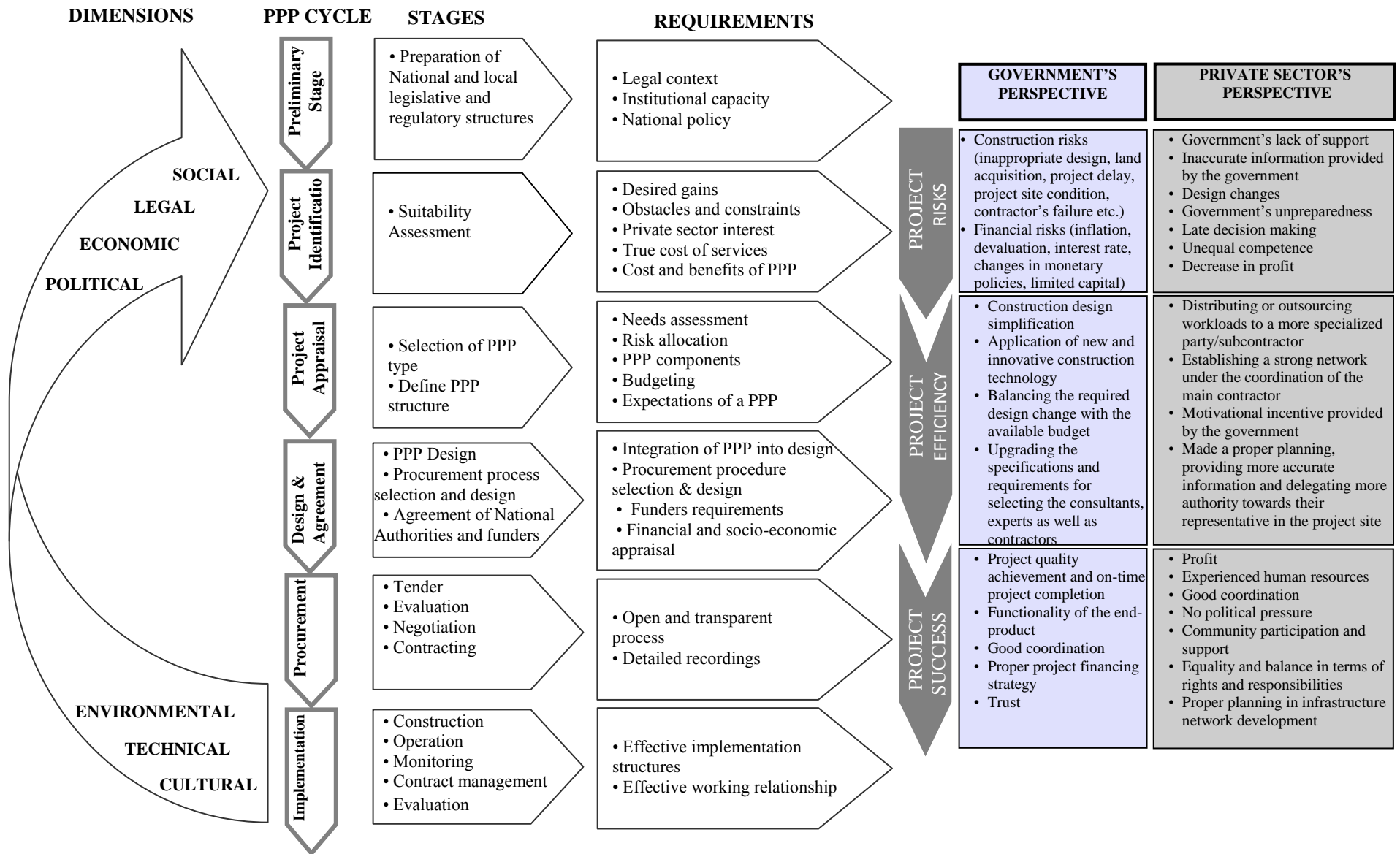


Figure 2. Conceptual framework for the applicability of PPP projects in Turkey

i) provisions that make a PPP project possible and facilitate its functioning (e.g. the legal right to establish a PPP Company, the terms and conditions under which public assets may be transferred to non-public entities, the power of the PPP Company to choose subcontractors on its own terms); and ii) provisions that enable governments to provide financing, where relevant (for example, to provide subsidies or make long-term commitments of public expenditure for the life of the PPP contract).

Economic: Effective PPP models will have to make economic sense to the parties involved for their success. Thus it has to devolve sensibly the roles and fair sharing of responsibilities, costs, and risks between the public and private sectors. PPP projects often raise debt funding on a limited-recourse project finance basis. This means that the lenders rely merely on project assets and cash flows and do not have recourse to the project sponsors. PPP design and documentation should provide adequate protection to debt service against non-commercial risks related to force majeure, regulatory changes, contract termination, etc. (Gunnigan and Rajput, 2010). In order for the partnership to be attractive to investors, a PPP project must be self-sustainable, financially viable, and profitable (FIDIC, 2001) which in turn, depends largely on the economic environment, government policy, and severity of competition (Grilo et al, 2005). Foreign capital will only be flowing in, when a PPP scheme is of significant financial interest and of a reasonable scale, given the extra costs involved in the procurement process (Ng et al., 20010).

Environmental: Since most infrastructure projects have an impact on the environment, a proper legal framework seeking the right balance between infrastructure development and the protection of the environment is required. A view of the current development of environmental controls enacted by various governments is closely linked to both the social and political components. A well developed impact and sustainability control regime would indicate that the PPP projects are likely to encounter more detailed scrutiny in countries with less developed controls (Gunnigan and Rajput, 2010). Requirements relating to planning and environmental approvals can have a significant impact on project deliverability.

Political: A strong political will from the government can only promote the commissioning of PPP projects by overcoming resistance and giving a clear signal of the government's intention to meet its contractual commitments. The political stability of government interacts most significantly with the economic and technological components. While political commitment is welcome and necessary, pressures for overly optimistic timelines need to be dealt with appropriately. A lack of political support is considered a potential barrier to PPP projects (Zhang, 2005) and a PPP scheme may be turned down if it is politically sensitive (Duffield, 2005). From the investors' perspective, consideration into a PPP project's political and legal feasibility prior to submitting a concession proposal is essential, as any changes in the political environment or deviations in the legal framework/institutional arrangements would add to the uncertainties and increase the risk of failure in a project (Pearson, 2005; Ng et al., 20010).

Technical: PPP would not be considered as an attractive option if the requirements and technologies continuously change during the expected lifespan of the project, unless sufficient flexibility is built into the contract to facilitate such changes. The experience of the public and private partners in a PPP scheme is also critical to success, as it can help to resolve how the scheme should be packaged and delivered, especially when it is complex and sensitive in nature (Jaselskis and Ashley, 1991). Pearson (2005) considered the prospect of creating innovative solutions as influential, if value-for-money is to be achieved. When the consortium is to be financially

rewarded based on their performance, decision makers should assess whether service quality can be objectively defined and measured before considering the use of the PPP approach (Duffield, 2005; Ng et al., 2010).

Cultural: Construction procurement cannot be seen apart from the influence of the participants culture involved. Cultural norms of the parties and the institutions involved in the construction procedures may pose challenges to PPPs. Private sector companies who have become involved in partnerships also experience organizational culture change as they have to take on board a number of social issues in order to provide a service that will meet the requirements of the public and the conditions laid down by the public sector.

The applicability assessment “Stages” in connection with the “PPP Cycle” and related “Requirements” which give reference to both the governments and private sector’s perspective have been explained in this section. A major component of any PPP is risk allocation. There is some debate as to how much risk should be transferred from the public to the private sector. Generally, the more risk transferred to the private sector partner, the more financial reward the private partner will demand. Risk should be allocated to the party who can best assume it in the most cost effective manner. Particular attention is required for the design of procurement procedures and contract management / monitoring systems. While both public and private sectors have reason to be concerned about the outcome of the financial assessment, their perspectives will usually be different. This will cause them to focus on different aspects of the process, giving more emphasis to some and less to others and possibly using different framework parameters. The key areas of concern for both groups are financial viability, distribution of revenues, and assessment of risk.

A degree of flexibility is required throughout implementation corresponding to the different needs of all parties. However project structures need to be sufficiently robust to allow effective monitoring and to ensure that the public interest is guaranteed. PPP relationships will require changes to the implementation systems associated with classical grant financed projects. This is primarily because the role and responsibilities of the parties change with increased private sector involvement.

With respect to the government’s perspective, risks that should be considered as their main concern in PPP projects are financial risks, which include inflation, devaluation, interest rate, changes in monetary policies, limited capital, etc. and construction risks, which include inappropriate design, land acquisition, project delay, project site condition, contractor’s failure, etc. As for the private sectors that will be involved in PPP projects, the risks that they should consider to be main concerns were government’s lack of support, inaccurate information provided by the government, design changes, government’s unpreparedness, land acquisition, late decision making, unequal competence and decrease in profit. Also from the government’s perspective, project’s efficiency involves value engineering including construction design simplification as well as the application of new and innovative construction technology. In addition to that, project’s efficiency level should also be maintained by balancing the required design change with the available budget. Another way to improve efficiency is to upgrade the specifications and requirements that will be used for selecting the consultants, experts as well as contractors. Project efficiency level can also be increased by some sort of motivational incentives to be provided by the government for any contractors that are able to complete their work ahead of schedule

or below the budget while maintaining the quality. Additionally, according to the government, the factors that should be considered to have significant impact in determining the success of a project are project quality achievement and on-time project completion, functionality of the end-product, government total support, good coordination, proper project financing strategy, trust, good system for contractor selection, information dissemination and communication system, compelling managerial capabilities, and continuous project monitoring and control.

Effective PPP development requires effective regulatory and strategic structures to be in place. The suitability of a PPP approach to project realization should firstly be assessed given the capability and capacity of the public sector to implement PPPs and derive benefit. Suitability of PPP approach includes whether there is sufficient private sector interest and whether PPP is the best delivery method. Potential PPPs can be hindered by several constraints and obstacles which must be considered by National Authorities. The main ones include extent of legislative authority, taxation framework, reporting and accounting requirements, and financial issues. National authorities have a major role to play in adding to the value of a project. Generally the private sector will give priority to projects which demonstrate sufficient demand, revenue generating and development potential, strong viability, strong political commitment, and meet internal development criteria. The benefits and costs should be systematically analyzed considering both quantifiable and non quantifiable items. Crucial to the selection process of a PPP is whether it will provide value for money and above all additional value than traditional public procurement methods. The benefits and costs should be systematically analyzed considering both quantifiable and non quantifiable items.

CONCLUSION AND RECOMMENDATIONS

This paper presents a conceptual framework to assess the applicability of Second Generation PPP Projects to be implemented in Turkey. The framework characterizes the PPP projects in terms of technical, financial and economic, social, political and legal, environmental, and cultural dimensions. The applicability assessment “Stages” in connection with the “PPP Cycle” and related “Requirements” which give reference to both the governments and private sector’s perspective have explained. The study defines the legal environment for PPP projects. The importance of effective legal structures is stressed together with the fact that PPP implementation may require a review of existing legal provisions to ensure compatibility. PPPs will operate in a complex legal environment characterized by the national legislation detailed project contractual documents and importantly, specific, procurement regulations. The study considers the PPP project cycle with the objective of providing a detailed discussion of the issues encountered and possible solutions. PPPs are a developing concept and in some cases have required substantial reform of legal and financial systems in Turkey to make applications possible. This will require possibly actions to define the role of the public sector, institutional capacity building at all levels including the allocation of qualified and motivated staff to specialized PPP units, reduction of market risk through user-oriented strategic approaches and development of private sector investment facilitation mechanisms. The degree of private involvement needs to be carefully matched to the objectives and needs of the project and the public. Appropriateness, cost, the ability to effectively implement and manage should be the paramount considerations in selecting a PPP structure.

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