

# LESSONS FOR DEVELOPMENT OF PUBLIC - PRIVATE PARTNERSHIPS IN ALBANIA

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## ABSTRACT

During the last 25 years Public-Private Partnerships are seen as a mechanism that modern governments consistently use to fulfill their responsibilities in providing infrastructure and public services. Their use has expanded from the transport sector to other areas such as health or education.

Gradually, Albania is underway to build its legal basis of PPPs, but in this regard there are many difficulties as the adoption of PPPs requires the fulfillment of certain conditions, among which it is worth mentioning the existence of a qualified, knowledgeable and experienced staff in the field of public-private partnership. Albania's aim for integration into the European Union created the necessity of studying the PPPs, advantages and benefits of the implementation of these contracts in the economic, political and social aspects as well as recognition of the potential risks that must be taken into consideration by the government.

Albania is currently in the first phase of the development of PPPs and the purpose of this paper is to study the efficiency of PPPs contracts in different countries and sectors as well as drawing valid conclusions on creating the right conditions and environment for the adoption and implementation of these practices in our country.

**Keywords:** *public-private partnership, benefits, threats, PPP phases*

**JEL Classification:** *H41, H42, E22*

## 1. Introduction

Public-private partnership in offering of public services has generated a great interest around the globe. This kind of partnership is seen by governments as a way to further improve the quality of services provided to citizens and to increase the efficiency of public investment. Public-private partnership is the best option to combine the private sector with its resources, managerial skills, innovative capacity and advanced technology and public sector with its regulatory authority and its major objective to protect public interest. One of the reasons that prompted not only our – government but also the governments of other countries to use this form of partnership has been the financial inability to realize investments simultaneously in various projects.

Gradually, Albania is underway to build its legal basis for PPPs, but in this regard there are many difficulties since the adoption of PPPs requires the fulfillment of certain conditions, among which it is worth mentioning the existence of skilled staff, knowledgeable and experienced in the field of public-private partnerships.

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In this paper we will make a comprehensive presentation of the Public-Private Partnership, concepts, definitions and main characteristics. Later in this paper will address the main factors that led to the birth and development of PPP practices, benefits arising from their implementation and what are the main current issues which have been highlighted in these partnerships in order to find the ways that lead to improving and increasing the effectiveness of these contracts and the implementation of a successful cooperation.

Further work will focus on the main areas of application of PPP in two main European countries (although after Brexit) to assess the efficiency of public-private partnership practices and based on past experiences conclude whether these practices can be successfully applied in our country.

## 2. Literature Review

Public-Private Partnerships are widely accepted and recognized in public sector management. The 1990s saw the creation of PPPs as the main means of public policies worldwide (Osborne 2000, p.1), as a novelty of the New Public Management. Starting from the 1980s, the key words of the New Public Management (NPM) were privatization, market mechanism, the distribution of public goods and services, competitiveness and reinventing the role of government. At the centre of NPM were: reduction of public sector expenditure, delegation of responsibilities to the private sector and promotion of voluntary commitment of private sector to providing public goods (Mitchell-Weaver and Manning 1991). The principles of New Public Management encouraged the establishment of Public-Private Partnership as a new management tool.

Nowadays there is a large variety of public-private partnership definitions worldwide. The content and objectives may vary in accordance with the special background of country-specific and individual interests of different authors.

According to the "Green Paper of EU for Public-Private Partnerships and Community law on public contracts and concessions" public-private partnership refers to forms of cooperation between public authorities and the business world, which provide financing, construction, renovation, management or maintenance of an infrastructure or providing a service. A key characteristic of PPPs is the relatively long duration of the relationship, regardless of the role of private financing or distribution of risks between the public partner and the private partner.

### **The main features of this partnership are:**

- Long-term contractual cooperation, 25 or 30 years.
- The contract stipulates the integration of all stages of the project, sharing of investments, responsibilities and loans as long as the contract is valid.
- The contract determines the final performances required as well as product specifications.
- Public partner is the one that defines the requirements in terms of construction, maintenance and service quality standards.
- The private partner assumes the risk that was previously held by public sector.
- Public partner pays a fee to the private partner for the realization of the product or service.
- After expiry of the contract term, public sector resumes the ownership of the product or service.

But all definitions are based on the idea that PPPs fill the space between traditional government projects and full privatization (Grimsey and Lewis, 2005, cited in OECD, 2008). OECD also

notes that the feature that determines if it is provided in traditional public way or a PPP, is whether a significant amount of risk is transferred (OECD, 2008).

There is currently no a major definition of a public-private partnership in Europe. As a result, PPP is a kind of umbrella that covers a wide range of agreements between public institutions and the private sector with the aim of providing public infrastructure and public services. Existing European legislation does not regulate PPPs, but only the general principles of the EC Treaty and the specific secondary legislation for public safety and concessions have established some guidelines in this regard (Public-Private Partnerships National Experiences in the European Union, 10.02.2006 ; EP 369.858;)

Despite the fact that there is no unified definition of public-private partnerships, their main characteristics fall in five categories (Akintoye et al 2006):

- 1- The partnership includes two or more subjects, one of whom represents the public sector and the other the private sector.
- 2- In public-private partnership, all participants in the project have a leading position.
- 3- In public-private partnerships, it is established a long and steady cooperation between the parties.
- 4- In the PPP model each party gives its contribution in the created partnership. For a successful cooperation, each partner must contribute material or non material resources in order to achieve the synergy effect.
- 5- This type of partnership involves joint responsibility for the results achieved (for example for services provided). Such a relationship varies significantly from the traditional position of the public sector, in which it holds responsibilities for the provision of services and implementation of public policies, based on the available advice from the private sector.

**Figure 1. Types of Public-Private Partnerships**



Source: World Bank

### 3. The potential benefits of public-private partnership

Faced with restrictions on public resources and the importance of infrastructure investment on economic growth, it urged governments of developed countries and developing ones to be supported by the private sector to provide the necessary additional funding to cover the financing gap. The benefits that the public sector gains from the partnership with the private sector are numerous, such as:

- *Transfer of risk* - In the case of a public-private partnership, the risks will be transferred to the partner, who is keen to manage them in an efficient and low cost manner and has the ability to

cope with the incentives that they convey. Thus, it is proved that the private sector is better at managing the risks of the construction, operation and financing, while public sector manages political risks. It is this transfer of risks that ensures that private sector will be motivated all the time to evaluate and produce efficiently.

- *The most innovative techniques in design and construction*- Experts generally believe that the private sector is able to develop newer models of design and construction that government entities. This is due to the specialized expertise that the private partner brings to a project. Innovations that the private sector brings produce a variety of benefits including lower project costs, higher quality, shorter working hours and other more extensive features of the project.
- *Fast Implementation* - Division of design and construction responsibility with the private sector, combined with payments related to the provision of a service, offers important incentives for the private sector to complete projects within a short timeframe.
- *Incentives to perform* - The project risk division stimulate a private sector contractor to improve the management and performance achieved in each project undertaken. In most partnerships, full payment to the contractor shall be made only if the required standards regarding the service are consistently met.
- *Economies of scale* - PPPs enable benefits from economies of scale, by minimizing costs per unit of service produced, as the service is provided in cooperation with the private sector.
- *Higher efficiency in the use of resources* - The privatization experience has shown that many activities, even those traditionally undertaken by the public sector, can be undertaken in a more cost effective way by private sector managerial competence.
- *Investments infrastructure* - Economic growth depends a lot on the development and growth of infrastructure, especially in utilitarian objects (energy, water and telecommunications) and transport systems. Also, in many countries there is an urgent need for new social infrastructure, such as hospitals and health care equipment, prisons, education and housing facilities. For many governments this is seen as the most pressing areas for the involvement of private sector investment.
- *Management skills of private sector* - private sector management skills enable the project to be implemented on time or before the deadline. Using public-private partnerships for investment in infrastructure government will have access to new skills.
- *Monitoring and controlling the quality of offered public services* - Unlike the public sector, which does not employ enough experts to monitor and control the quality of services provided, private companies are known for numerous internal audit processes and increasing the efficiency of product delivery that is subject of the signed contract.
- *Competition* - Competition is observed during the tendering phase, creating in this way a kind of competitive market. As long as the product is specified correctly in terms of production requirements (instead of specifying the inputs), then each private provider tends to minimize costs as much as possible.

#### **4. Potential Risks of Public-Private Partnership**

Costs of development and delivery during the PPP project may result higher than traditional processes of service delivery by government. Therefore, the government considers as necessary to determine whether these higher costs are justified or not. The main risks the government faces in the implementation of public-private partnerships are:

- Some projects may be politically or socially challenging to introduce and implement than others. Such cases are when the existing workforce of the public sector has the feeling of fear to be transferred to the private sector, when fees increases are needed to enable the realization of the project or when displacement is deemed as necessary.
- Procedure in providing services through PPP contract is longer and more expensive, if compared with the traditional way of providing public services.
- PPP agreements are long-term, complicated and relatively inflexible, because of the impossibility of forecasting and evaluating all special events that may influence future activity.
- Deferral of public sector payments to PPP projects for subsequent periods may affect negatively on future fiscal indicators of public sector.
- The private sector will do that for which it is paid and no more than that. Therefore incentives and performance requirements must be set correctly in the signed contract. The focus of the government, generally need to be set on performance requirements.

## **5. Lessons learned for PPPs from international institutions**

### **Lessons learned from the World Bank**

The World Bank's website contains a significant number of reports about PPPs on basis of which there are identified some valuable lessons:

1. PPPs are more likely to be successful when special attention is paid to planning and a detailed study of the feasibility of the project is undertaken.
2. PPPs require transparency and competition.
3. PPPs require robust monitoring and flexibility, in order to ensure a rapid response to unforeseen events.
4. Governments must learn how their PPP programs are developed in order to make adjustments whenever necessary.
5. The participation of international firms increases finances, reliability and expertise.
6. Financial profitability and sustainability of PPP's depends directly from the observance of contractual obligations by promoters.
7. A solid legal framework is necessary to specify the "rules of the game" for the private sector and to reduce project risk.
8. In developing or in transition economies, a strong macroeconomic shock could create an unexpected situation for a government putting it in difficulties to meet its contractual obligations with regard to PPPs.

### **Conclusions drawn from the State Treasury in England**

The United Kingdom has the largest program in the world regarding PPPs in terms of the number of implemented projects and of the number of sectors in which they are applied. British Treasury has revised the guidelines PPPs over the years to reflect all the lessons learned from central and local government agencies.

Treasury has identified key features that should have a project that is suggested as suitable for being part of a PPP. These features include:

1. A major capital investment program that requires effective management of risks associated with the construction and delivery.

2. Appropriate service structure that allows the public sector to determine its needs, to create partnerships with parties that ensure the realization of the project effectively and fairly, and the risk is shared accurately between the parties.
3. Nature of assets and services identified as part of the PPP scheme and risks associated are capable of being costed on a whole-of-life basis.
4. The project value is too large to ensure that service costs are not excessive.
5. Technology and other aspects of the sector are stable and not susceptible to rapid changes.
6. If planning horizons are long-term and the private sector has good expertise to offer assets and services that are intended to be used for long periods of time, then there are strong reasons to believe that this partnership will offer value for money and strong performance incentives.

### **Efficiency of public-private partnerships in UK**

UK developed the concept of public-private partnerships in the 90s. These partnerships between the government and private sector provided efficient and cost-effective services.

Countries around the world such as Canada, Portugal, Ireland, Japan, Sweden and Australia work with UK organization and rely on their expertise to develop their respective models of PPPs.

It is universally acknowledged as the leader state of Public-Private Partnership in the field of health care by constantly bringing innovations in this field. For years they have successfully implemented a number of PPP programs. Projects range from the giant project of St. Bartholomew's and the Royal London Hospital, worth 1.1 billion pounds to the residential care home worth 2.8 million pounds. Since the early beginnings NHS in cooperation with British advisers has developed extensive expertise in terms of PPPs, ie the method of management, contracting and management of a public- private partnership project. Another main objective of british experts has been the realization of projects with lower costs by increasing the efficiency.

### **Efficiency of public-private partnerships in France**

Public-Private Partnerships have had a wide range in France since their first appearance in 2004. Like any other innovation, these types of agreements were faced with some difficulties, as they were new concepts in legal terms. In August 2012 the number of signed public-private partnership contracts reached 150 with a cumulative value of 12 billion Euro in total since 2005. Since 2011 France has dominated the European market in terms of contracts volume.

To evaluate the efficiency of the Public-Private Partnerships in France, will be used data generated from a study performed in 2012 by Stéphane Saussier and Phuong Tien Tran, the first study that covers the construction and operational phase of PPP contracts. Evaluation of the efficacy of the above-mentioned contracts in terms of costs, deadlines, quality and value for money is obtained through a questionnaire addressed to the executive directors of 30 projects that were in the operational phase.

After processing the data from the questionnaires showed that a large proportion of the contracts included in the sample obtained in the study (97%) were renegotiated at least once after the initial contract signing. Renegotiations included adjustments to the scope of the contract (73%), to financial arrangements (3%) and reagrding the completion term of the project (30%). In the study conducted, 70% of public authorities stated that they were satisfied or very satisfied with the negotiated changes and renegotiation generally has not been conflictual.

## 6. Conclusions and recommendations

Public-private partnership is the best option to combine the private sector with its resources, managerial skills, innovative capacity and advanced technology and public sector with its regulatory authority whose major goal is the protection of public interest.

Nowadays there is no widely accepted definition of PPPs. Eurostat, the IASB (Board of International Accounting Standards), the IMF (International Monetary Fund), IRFS (Institute for Reporters Freedom and Safety) and others bodies work with different definitions.

Public-Private Partnership ensures the transfer of risk, the most innovative design and construction techniques, rapid implementation of the undertaken project, better incentives to perform, benefits from economies of scale, high efficiency in the use of resources, investment diversity in infrastructure, expertise in monitoring and controlling the quality of public services and increased competition.

The development of PPPs is associated with a number of worth mentioning risks such as: political risk, longer and more costly procedure of providing services, complex and inflexible procedures in signing long-term agreements, etc.

England is the first country in the world that developed the concept of public-private partnership in the 90s. Partnership between the government and the private sector provided efficient and cost-effective services, especially in the health sector.

Starting from 2011 France has dominated the European market with more than 50% in terms of volume of signed contracts. Based on the processed data of the distributed questionnaires during the study conducted by the Stéphane Saussier and Phuong Tran Tran, it was concluded that most of the contracts included in the sample obtained in this study have achieved a good performance, thus laying down all the criticisms that have been made towards public-private partnerships.

The government of our country should pay particular attention to various aspects when compiling the institutional framework supporting PPP's. Requirements for Successful Public-Private Partnerships include: a) good governance in Public-Private Partnerships b) creation of PPPs legal framework.

The first PPP projects in Albania are carried out in the health sector, where based on the experiences of Spain and England it is foreseen that these contracts will also be successful in our country.

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