Public-private partnerships in China: A responsive participation

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Abstract: This article reflects on the rise of public-private partnerships (PPPs) in China. Though PPP is relatively new in China, it draws on a recent series of policies, guidance materials and rules relating to the provision of public facilities and services in tandem with global developments. This paper reviews the development of PPPs in China with selected project cases in the first two sections. The third section of the paper highlights some of the key challenges facing PPPs in China following some considerable controversies and experiences in the delivery of public service and infrastructure development. Hence, given the many limitations of PPPs and complex deals, it is suggested that other countries’ experiences be drawn upon as comparisons and lessons learnt for better governance of PPPs in China.

Key words: public-private partnerships; China; service delivery; infrastructure; governance

1. Introduction

Public-private partnerships (PPPs/PPP) are the latest “new public management” development for the public services, a worldwide development, an alternative means of providing public infrastructure with a focus on services and/or outputs. The PPP model we have most in mind is that developed in the UK, Australia and Canada under which a PPP project results in a contract for a private entity to deliver public infrastructure-based services, a switch from traditional public procurement methods to provision of infrastructure. Many countries have released its policy on PPPs, and China’s relatively new in joining governments around the world in exploring and developing PPPs has potential due to the internal demand for more and improved public facilities and services. Partnership has been the fashionable trend since the UK Thatcher Government embarked on a large-scale privatisation program beginning with the sale of British Telecom in 1984. In China, the position was only experienced in the year 2000 when a series of policies, guidance materials and rules relating to the provision of public facilities and services were presented, for example, the Ministry of Construction issued the “Opinions on Acceleration of Privatization Process of Public Facilities” in December 2002 and the “Rules on Management of Franchised Operation of Public Facilities” in May 2003. Among others, the Shenzhen Government also advocated the “Rules for the Franchised Operation of Public Facilities” in May 2003, and the Beijing Government advocated the “Rules for the Franchised Operation of Basic Urban Facilities” in October 2003.

2. New initiative in partnership

China has been fortunate to have a history of economic prosperity. With a strong resource base and natural advantages, the capacity to provide responsible financial management of the nation is essential for future growth.
The government is mindful of keeping within the financial targets and in delivering infrastructure projects and ancillary services to its citizens.

In recent years, the terms “public-private partnerships” (PPPs) and later “private-finance initiative” (PFIs, though not much yet in China) have been used throughout the world to describe joint approaches to infrastructure and service delivery between the public and private sectors. In many countries, this engagement has occurred in the presence or the absence of a formal policy to protect the public interest and guide the private sector. In some countries like Australia, United Kingdom and Canada, such formal policy and related documents are evident for commitments to the highest standards possible for strategic partnerships in order to establish a strong record of responsible economic management.

However, in China, it is not clear when and how PPPs should be applied as there are still insufficient legal policy frameworks in use comparatively to other countries. Successful partnerships between the public and private sectors do rely on the creation of a business opportunity, which in turn relies largely on the existence of sufficient consumer demand. If bringing forward PPP projects simply because there exists the possibility of a private funding source, then it is unlikely to lead to a successful partnership arrangement.

Though there exist policy frameworks such as “Opinions on Acceleration of Privatization Process of Public Facilities” in December 2002, “Rules on Management of Franchised Operation of Public Facilities” and “Rules for the Franchised Operation of Public Facilities” both in May 2003 and the “Rules for the Franchised Operation of Basic Urban Facilities” in October 2003, they are relatively minimum as compared to other developed countries who have been practicing PPPs. Though minimum, it serves as a start towards the circumstances of supporting PPPs.

3. Development of PPPs in China

Within the Chinese context, the reasons for advocating PPPs in China are mainly:

(1) Due to inadequate investment in public facilities and services given high rate of urbanization, relatively low standard of public facilities and services;

(2) Limited funding sources and inadequate private investment in public facilities and services given the main source is of government funding;

(3) Slow rate of reform of state-owned enterprises and poor provision of public facilities and services.

On the last point above, perhaps many have viewed the state-owned enterprises (SOEs) as relics of a failed economic experiment as in the pursuance of privatization policy by the conservative administration of Thatcher and Major from 1979 to 1997 for majority of state-owned enterprises. In the case of China, an out-of-date impression of SOEs distorts the picture of China’s competitive landscape, as the line between SOEs and private-sector companies has blurred considerably (Woetzel, 2008). Many observers define a Chinese SOE as one of the 150 or so corporations that report directly to the central government. Thousands more fall into a grey area, including subsidiaries of these 150 corporations, companies owned by provincial and municipal governments, and companies that have been partially privatized yet retain the state as a majority or influential shareholder. The oil company China National Offshore Oil Corporation (CNOOC) and the Chinese utility State Grid Corporation of China (SGCC), for instance, are clearly SOEs under the first classification, while the computer maker Lenovo and the appliance giant Haier are less clear-cut cases, in which the state is the significant shareholder. A majority of the equity in the automaker Chery Automobile belongs to the municipal government of Wuhu. Furthermore, market
forces unleashed by government reforms are pushing SOEs to become more open (Woetzel, 2008).

The Chinese Government has been promoting PPPs in the provision of public services to meet the needs of public facilities and improve quality, service delivery and efficiency. In early October 2004, 54 infrastructure projects involving RMB 70 billion were bid for by private companies through the Ministry of Finance. There are 14 different modes of PPP existing within three generic types—outsourcing, concession and divestiture (for more information, see Beh, 2007).

4. Selected cases of PPPs in China

The government remained much in control of public sectors such as water services, energy, waste management and public transport. In the mid 1990s, the China Government promulgated the Circular on Attracting Foreign Investment through BOT Approach (No. 89 policy paper of 1994, the former Ministry of Foreign Trade and Economic Cooperation, January 16 of 1995) and the Circular on Major Issues of Approval Administration of the Franchise Pilot Projects with Foreign Investment (No. 208 policy paper of foreign investment, the former National Development and Planning Commission, the Ministry of Electric Power Industry, and the Ministry of Communications, 1995). These legislative circulars formed the basis for public-private partnerships and foreign capital investments. Following that, the National Development and Reform Commission firstly approved three BOT infrastructure projects in 1996, including Chengdu No. 6 Water Supply BOT Plant, Guangxi Laibin Power BOT Plant, and Changsha Wangcheng Power BOT Plant (failed) (ZHONG, Mol & FU, 2008).

4.1 Water and waste management

In China, BOT/BTO contracts, transferring risk and payment to the public sector (i.e., with payments by a public authority rather than end-users), have been used for the development of new water-services projects. This is a positive phenomenon, but how real is the risk transfer? It might be argued that if the PPP fails, it is quite likely that the public authority will incur extra costs to maintain the public service, so risk transfer will fail anyway to this extent. However, it would not be correct to suggest that this is what always happens if PPP projects get into trouble.

One of China’s first wastewater treatment plants to be delivered using a PPP, the Guangzhou Xi Lang Wastewater Treatment Plant, was recently completed by the Guangzhou Sewage Treatment Co. (GSTC) and Earth Tech. (Anonymous, 2008). The consulting firm, which also helped arrange part of the project’s financing, served as the plant’s designer and construction manager and operator. As part of Guangzhou’s commitment to promote sustainable development and improve water quality in the Pearl River, the city decided to pursue an innovative approach to constructing new wastewater treatment facilities. The build-operate-transfer project was completed six months ahead of schedule and came in under a budget cost of approximately USD 130 million. It has a maximum capacity to treat 260,000 m³/d and features a biological nutrient removal process and an ultraviolet disinfection system that are both state of the art. Earth Tech will operate and maintain the plant’s treatment systems for 17 years, after which operation of the plant will be returned to GSTC. The plant’s design includes a possible second phase that would double its capacity. The plant was financed in part by Tyco International, Earth Tech’s parent company and a major Chinese bank.

Direct investment demand for urban wastewater infrastructure (including wastewater treatment, sewers and sludge treatment) in China is expected to be over USD 30 billion between 2006 and 2010, to meet the objective of 60% municipal wastewater treatment. Accordingly, local governments prefer direct private sector investment in new wastewater management resulting in high levels of Greenfield modes that financing is based on negotiated
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prices between the government and the private sector and is less dependent on the user fee/charge (ZHONG, Mol & FU, 2008).

In the rural water management, it involves a 4-year USD 6.792 million joint project by UNDP, Ministry of Water Resources, China International Center for Economic and Technical Exchange under the Ministry of Commerce, and the Coca-Cola Company in the provinces of Sichuan, Heilongjiang, Xinjiang and Liaoning in providing basic sanitation, water safety technologies, rebuilding of drainage pipelines and ecologically sustainable agricultural technologies for water conservation.

4.2 Health

The China Health Alliance (CHA) is a new PPP catalysed by the World Economic Forum’s Global Health Initiative. Founding members and partners of the China Health Alliance to date include Accenture, China National Textile and Apparel Council (CNTAC), Constella Futures, Esquel, Institute of Contemporary Observation, iKang, Karstadt Quelle, Marie Stopes International China, Pfizer, Social Accountability International, Standard Chartered Bank, Swire Beverages, UNAIDS, UNDP, World Health Organisation (WHO) and World Vision International. Each member is actively supporting the set-up and implementation of the Alliance’s programmes.

The partnership is designed to educate, test, treat and support Chinese company employees at risks of TB and AIDS besides raising public awareness of growing public health threats in China witnessing the pilot project in Guangdong (China Daily, 2007, September 14).

Merck Sharp & Dohme and Daimler Chrysler have formed partnerships with China’s non-governmental organizations and government agencies, for example Ministry of Health on USD 30 million project on HIV/AIDS prevention and treatment. Other partnerships include Quality Brands Protection Committee, International Council of Toy Industries, the China Business Council on Sustainable Development and Global Business Coalition on HIV/AIDS.

4.3 Infrastructure

Infrastructure development in China increased tremendously especially over the past 15 years. There are numerous projects to be elaborated upon within the complex interdependencies and networks. One such project is the Citong Project where there were many challenges faced. Among those challenges were that the ownership of local transportation facilities localized from provincial government to the municipal government, revenue of Quanzhou Bridge is channelled fully into the city public accounts instead of partially as agreed upon earlier and the design of the connectivity of the highway to the city. Others include absence of operation right assurance, finance, standardized operation procedures, complex procedures of obtaining approval, and lack of regulation. Hence, the situation in which difficulties arise due to changes of agreements from time to time, deficiencies and unnecessary secrecy surrounding the contracts and public interests and allocation of risks accurately defined in the policy seems vital.

China’s rapidly growing aviation industry has challenged on-going efforts to maintain effective safety and security operations. The US Training Development Aviation helped to structure the China Aviation Cooperation Program with the goal of facilitating U.S. Government and U.S. aviation industry training and technical cooperation with China identified by the General Administration of Civil Aviation of China (CAAC). This program is supported by twenty-one U.S. private sector member companies and public sector contributions from the Federal Aviation Administration and the CAAC.

4.4 Other PPPs

China Gas Holdings enters PPPs with municipal governments to distribute natural gas supply. There are 48
PPPs up to date serving 800,000 households with projects worth USD 4 million. With the expanding potential of abundant natural gas reserves, capital expansion and expertise available, there is large potential for demand in power generation and residential use and opening downstream activities to private sector, thus introducing competition as compared to distribution traditionally controlled by municipal governments.

5. Key challenges PPPs face in China

Since relatively PPPs are a new initiative in China, there exist commonly key challenges, namely:

(1) Limited capacity of civil society/NGOs to manage partnership;
(2) Lack of experience on commercial, technical, legal and political aspects of PPPs;
(3) Too much emphasis on attracting investment from private sector and too little attention to market competition;
(4) PPPs have been treated as privatization of public facilities/services focusing on short-term return without a spirit of long-term partnership;
(5) The financial risk and burden shifted to public without the corresponding increase in service quality;
(6) Inadequate knowledge on PPPs, lack of proper risk assessment;
(7) Lack of administrative framework for PPP projects.

A key aspect of PPPs, as the name suggests, is the central involvement of a private-sector entity with a public-sector entity. The objective of the partnership is to import private sector to the delivery of service which has previously been accepted as the responsibility of government, and it is the introduction of a private-sector entity which creates an accountability dilemma. After all, the choice of using a PPP as a medium to deliver services is a policy decision of the government. Rosenau (1999) argued that the success of a partnership arrangement was dependent on setting out clear goals and clear lines of responsibility. This can only be accomplished if the problem is well understood and the government service required is clearly specified.

PPPs are generally introduced for a lengthy period of time, and are developed in an uncertain environment. Hence it is important to develop a governance framework that would involve performance aspects, tools of analysis and key issues. There are many suggestions as to how PPPs can be better managed. One of these is pointed out here. According to Grimsey and Lewis (2004), the key ingredients in developing a typical PPP project together with the roles of the government at each stage are:

(1) A focus on defining services, with the emphasis on the delivery of infrastructure services using new or refurbished public infrastructure assets;
(2) Planning and specification, so that government’s desired outcomes and output specifications are clear to the market;
(3) Creating a viable business case for the private party;
(4) Certainty of process, ensuring that any conditions to be fulfilled are clearly understood before the project proceeds;
(5) Project resourcing to enable government to advance the project and address issues in line with published time-frames;
(6) Clear contractual requirements, centred on key performance specifications to promote performance and minimise disputes;
(7) Formation of a partnership to encourage good faith and goodwill between government and the private
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party in all project dealings;

(8) Contract management to monitor and implement the contract.

The key question that needs to be addressed is whether PPP projects deliver better results in terms of time and cost outcomes in comparison to traditional projects? Regardless of any viable complex risks allocation framework and service delivery performance in place, it should be mindful that the ultimate responsibility for service delivery and performance of essential public services rests with the government.

6. Concluding remarks

PPPs may be a new initiative and a responsive participation currently developing in China. It is a new expression in the language of public management, even though history indicates there has always been some degree of cooperation between the public sector and the private sector, and in some cases blurs distinctions between the governments’ state-owned enterprises beneath the line of reasoning and interpretation. Nevertheless, China can draw comparisons from PPPs experiences in different countries in areas where the private sector has a proven track record in the successful delivery of assets and their ancillary service needs. This provides the opportunity for major public assets to be maintained and preserved to a standard which is higher than that has been traditionally possible by the public sector. Whilst this is evidenced, the procurement plan must clearly justify why a PPP is the preferred procurement approach. In developing the expressions of interest in a PPP project, development and evaluation of those interests must be fully documented with all recommendations fully justified.

On the other hand, the case made by a public authority for a PPP can be equally one-sided, for example with claims of large cost savings compared to public-sector procurement which cannot be proved objectively, or which do not compare like with like, and PPPs may be promoted for short-term political advantage. Furthermore, PPPs have been subjected to considerable controversy following some high profile “failures” in many countries which have long developed PPPs. In the context of the on-going debate on PPPs, many governments of the day continue to support the PPP model with well-developed implementation frameworks.

References:

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