



PUBLIC-PRIVATE PARTNERSHIP MANUAL

PHASE 4

Managing and Implementing a Public-Private Partnership Contract



WORLD BANK GROUP



UKaid
from the British people

2021

Acknowledgments

This PPP Manual for Ukraine was prepared as part of the World Bank project on Strengthening the Use of Public-Private Partnerships through Better Public Capital Investment Management in Ukraine, funded by the Good Governance and Investment Climate Reform (GGICR) Trust Fund which is housed in the World Bank and supported by the UK Government.

The World Bank's Strengthening the Use of Public-Private Partnerships through Better Public Capital Investment Management in Ukraine Project expresses appreciation to the Ministry for Development of Economy, Trade and Agriculture for their excellent collaboration in the development of this PPP Manual.

This work is a product of the staff of the World Bank in Governance Global Practice and Infrastructure Finance, PPPs and Guarantees Global Practice with external contributions. The findings, interpretations, and conclusions expressed in this work do not necessarily reflect the views of the Executive Directors of the World Bank or the governments they represent. The World Bank does not guarantee the accuracy of the data included in this work.

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Abbreviations

ARM	automated remote meter-reading
BOO	build-own-operate
DRP	dispute resolution process
ICSID	International Center for the Settlement of Investment Disputes
ICT	information and communications technology
MDETA	Ministry for Development of Economy, Trade, and Agriculture
MoF	Ministry of Finance
MPSS	minimum performance standards and specifications
ROT	rehabilitate-operate-transfer
RPI	retail price index

Introduction

Scope of PPP Manual Phase 4

This is the fourth of four manuals on identifying, preparing, procuring, and implementing PPP projects. The previous manuals explained the steps in identifying a PPP project, preparing a concept note and a proposal, and selecting the private partner. The Phase 3 Manual concluded with signing the contract with the private partner and financially closing the transaction. Therefore, the Phase 4 Manual focuses on the role of the public partner, through its PPP public management unit, in actively monitoring the performance delivered by the private partner, during both the construction and the operating phases.

The Phase 4 Manual is structured as follows:

- **Chapter 1** discusses the activities and tasks the public partner should conduct during the construction phase.
- **Chapter 2** discusses the activities and tasks the public partner should perform during the project operation phase.
- **Chapter 3** focuses on the tasks and activities that take place at the end of the PPP contract period and how the public partner prepares for the asset's hand back to the government (municipality) or other final options.
- **Appendix 1** provides the good practice and recommendations for developing and using a Contract Administration Manual and other tools to ensure efficient management of the PPP project during the construction and operation phases.
- **Appendix 2** describes a variety of changes that may take place during project implementation and what the public partner can do to handle them, including contract modifications, renegotiation, refinancing, price adjustments, and other approaches.
- **Appendix 3** offers suggestions for engaging with an advisor during contract execution and the role and Terms of Reference for advisors.
- **Appendix 4** discusses the importance of and mechanisms for establishing and maintaining an effective relationship with the project stakeholders and particularly with the private partner throughout contract execution.
- **Appendix 5** describes how to prepare for the unexpected during contract implementation and how to make contingency plans.
- **Appendix 6** explains how to manage the wealth of information, knowledge, and systems used during PPP project implementation.
- **Appendix 7** provides good practice and recommendations on how to deal with disputes during contract implementation.

Preamble

The objective of PPP contract management is to obtain the services specified in the output specifications and ensure ongoing affordability, value for money (VfM), and appropriate management of risk transfer. PPP contract management enables the public partner to exercise its rights and meet its obligations to ensure the objectives required from the PPP contract are met.

Contract management is also important because a project is rarely undertaken in complete isolation from other initiatives of the public partner and other government (municipal) agencies. For example, a road PPP will form part of the wider road network and may link with other transport infrastructure such as airports and ports, and a hospital PPP forms part of the government's overall strategy for providing healthcare services to the community. The public partner's management of PPP contracts ensures that PPPs play their role as part of the overall network of infrastructure that supports positive economic and social outcomes.

Sound contract management is crucial to the success of a PPP. A failure by the public partner to adequately manage the contract will inevitably erode the value for money outcome expected at the time the contract was awarded. Poor contract management may ultimately undermine the project's objectives.

Although PPP contracts are output-driven, these contracts require considerable management efforts on the part of the public partner. This is because PPP contracts have long terms, require the private party to provide substantial works and services, and provide a framework for the parties to manage many uncertain future events. Risks will materialize over the life of the contract, and changes are likely to be required due to the occurrence of these risks, changing needs, or other factors. The larger and more complex the project, the greater the likelihood and magnitude of these events.

The public partner must actively manage the contract to ensure that the private party delivers the works and services as specified in the contract. The public partner must also respond to future events and risks and manage changes by applying the contractual framework.

The initial allocation of risk must be managed over the entire life of the project in order to:

- Ensure that the private partner bears the risks it is required to bear and mitigates them adequately; and
- Monitor and effectively manage the risks borne by the public partner.

Good contract management will not guarantee a successful outcome. Unexpected events may occur that result in the actual project outcomes falling short of expectations. Good contract management provides the best possible management of these events, however, as well as of any changes and risks that emerge. This minimizes the impact on services, costs, and ultimately the value for money outcome, creating the greatest opportunity for project success.

The contract as the main framework for contract management

The PPP contract sets out the rights and obligations of both the private partner and the public partner. It forms the main framework for contract management and provides remedies for underperformance (such as penalties and deductions or abatements to payments), and processes for dealing with changes, claims due to emerging risks, and disputes. The public partner should ensure that any actions or decisions it makes in relation to the project are implemented through the contractual framework. For example, if an unexpected event delays project construction or prevents the private partner from delivering some services, the public partner should respond to that event as in the contract. It should not respond by ignoring the existing PPP contract framework and coming to a new agreement with the private partner. The public partner should also be aware of the other contracts and legal or administrative instruments that form part of the framework for contract management. For example, it is common to have a direct agreement between the public partner and the lenders to the project dealing with certain issues related to project financing. Various permits and approvals may create rights or obligations in relation to the project. The public partner should understand these contracts and legal or administrative instruments and ensure compliance with them.

Roles and responsibilities of the public partner and the private partner

The private partner is responsible for delivering the works and services specified in the PPP contract. The public partner retains ultimate accountability to the public for delivery of those works and services, even though the contractual responsibility is transferred to the private party through the PPP contract. According to the contract, the public partner assumes the obligation to pay for the service or allows the private partner to charge users. The procuring authority therefore has a number of roles:

- The public partner has a strategic role in sharing policy and other strategic developments with the private partner and in implementing these through the contractual framework where appropriate.
- The public partner must perform its own obligations under the PPP contract, including making any required payments, making land available, and granting approvals.
- The public partner has a monitoring role requiring it to monitor the performance of the private partner so that works and services are delivered to the required standard.
- The public partner must take corrective action under the contract if the private partner does not deliver the works and services to the required standard.

The public partner will need to use expert external resources from time to time to supplement the resources of the contract management team and to provide specialist advice on issues. The external resources may include legal advisors, financial advisors, insurance advisors, and a range of operational and technical advisors. The public partner should ensure that it has a sufficient budget available for the contract management team to hire advisors when they are required. (Appendix 3

of this manual provides further guidance on the appointment of advisors to assist with contract management.)

1. Tasks performed during the construction phase

During the construction phase, the private party finalizes its financing for the project through the financial close process and draws down on the project finance, using it to pay the construction contractor (or contractors)¹ to design, construct, test, and commission the project according to an implementation schedule.

The public partner must manage the PPP contract from the outset to ensure timely completion and satisfactory operation of the project.

The objectives of contract management in the construction phase are as follows:

1. To ensure that the private partner performs its obligations to finance, deliver, and commission the infrastructure;
2. To ensure that the public partner performs its obligations to oversee the construction phase and accept the infrastructure;
3. To manage stakeholder interfaces to support project outcomes.

The following key activities typically occur during the construction phase of a PPP:

1. The private party establishes itself on site and obtains the necessary permits and licenses to enable it to carry out the construction works.
2. The design for the construction works is finalized.
3. The construction works are carried out.
4. The completed infrastructure is commissioned and handed over to the operational team.

In most projects, these activities are performed by the private party's construction contractor; however, the private party remains responsible to the public partner under the PPP contract. During this phase the public partner manages changes (see Appendix 2 of this Manual), monitors liabilities and reports to central agencies in the framework of PPP contract performance monitoring, plans for unexpected events and responds if these occur (see more detail in Appendix 5 of this Manual), manages knowledge and information (see more detail in Appendix 6 of this Manual), and manages any disputes that arise (see more detail in Appendix 7 of this Manual).

1.1. Site availability, permits, licenses, and mobilization

In the majority of PPPs that involve construction of infrastructure, the public partner must make the site available to the private party.² The public partner should follow the processes set out in the PPP

1. In some projects, more than one company may be involved in the construction under a contract with the private party.

2. If the contract provides for the private partner to manage land acquisition or expropriation, the public partner should monitor and proactively manage the associated risks and threats. The public partner may

contract for making the site available. For projects with a single site, the public partner usually ensures the site is available and handed over immediately after financial close. For projects with extensive land requirements over a large number of distinct properties, the situation may be more complex, and the PPP contract may provide for the public partner to progressively hand over properties as the project progresses. This is often the case in linear infrastructure projects such as roads, rail lines, pipelines, and transmission lines. The private party (or its construction contractor) may need to obtain various permits and licenses before occupying the site or commencing construction work. The public partner should monitor the private party's progress in obtaining these permits and licenses.

1.2. Design development

At bid submission, the private party usually will not yet have finalized its design for the infrastructure. It must further develop its design after commercial close and contract signature. The PPP contract typically requires the private party to submit the final design to the public partner for review before a certain date specified in the RFP or committed by the private party in its proposal. Typically, the private party will first submit the design in draft form. The public partner will have to approve the design or provide comments or feedback within a certain time limit defined in the PPP (concession) contract before the final version of the design is submitted for approval. Some contracts will allow the private party to submit the final design in packages related to specific parts of the project and may provide for the public partner to give the order to start construction for each individual package once it has been finalized. (See Task 1.3 for guidance on the public partner's review of designs.)

1.3. Construction

The private party's construction contractor will usually split the construction work into phases or smaller packages to achieve its milestones and will often tender individual work packages to subcontractors. However, the construction contractor will remain responsible under its contract with the private partner for the quality of all work and for coordinating subcontractor activities.

The public partner must monitor the construction process and review progress and compliance with the PPP contract. It may also need to provide various construction-related approvals. See Task 1.5, "Oversight of construction," and Task 1.6, "Public partner review and approvals during the construction phase" for guidance on these activities.

also need to manage associated claims if the contract provides some risk relief to the private partner in cases of delays or cost overruns during the land acquisition process). See Task 1.5 below for more information on monitoring and Task 1.8 for more information on claims management.

1.4. Commissioning and handover to operations

Once construction is finished, the infrastructure must pass a range of commissioning tests specified in the PPP contract before the construction phase can end and the operations phase can begin. The public partner must monitor the commissioning tests and review compliance with the PPP contract. It may also need to provide various approvals related to commissioning and the handover to the operations phase.

The contract management team should start preparing for commissioning well in advance so that detailed processes and a dedicated commissioning team is in place in time for commissioning. See Task 1.5, “Oversight of construction,” and Task 1.6, “Public partner review and approvals during the construction phase” for guidance on these activities.

Some projects may proceed with handover to operations in two stages. The first stage is typically known as provisional acceptance or provisional completion. It allows the operational phase of the project to commence, provided that:

1. Construction has been substantially completed;
2. Operation can commence under appropriate safety standards; and
3. Any remaining construction defects or noncompliance are minor in nature and do not prevent commencement of operations (the listing of minor noncompliance is often referred to as the *punch list*).

The defects and noncompliances must be resolved within a certain time to complete the second stage of the handover process. This second stage is typically known as *final acceptance* or *final completion*. Some projects may have more complex staged completion and handover processes. The public partner should ensure that it understands the process as described in the PPP contract.

1.5. Oversight of construction

The public partner should monitor whether the construction pace is meeting the works program and likely to meet the future project milestones committed to by the private partner and required by PPP contract provisions on project construction quality and functionality. This public partner will assess quality and functionality during project commission but, to mitigate the risk the private partner will fail to meet the commissioning requirements (possibly delaying the start of operations), the public partner should proactively monitor quality and functionality throughout the construction phase.

The public partner’s construction monitoring activities should reflect the needs of the project and the requirements of the PPP contract. These activities typically include:

1. Reviewing the various construction plans to check that they are in accordance with the agreed specifications;
2. Auditing the private partner’s adherence to design and construction quality plans;

3. Monitoring the time progress of the construction so as to manage proactively the risk of delays (see more details below);
4. Linked to the former, progressively assessing the actual costs of the works, which may be relevant for determining the compensation payable by the public partner in an early termination of the PPP contract;
5. Financial monitoring of the private party's drawdown on financing arrangements and payments by the private party to its construction contractor;
6. Attendance works meetings between the private partner and its contractors;
7. Witnessing the completion process conducted by the private party and its contractors;
8. Monitoring the performance of checks and inspections by independent parties;
9. Formally accepting the facility before operations commence, in accordance with the contract.

Many PPP contracts appoint an independent certifier (sometimes called the independent engineer or construction supervisor), who is then responsible for certifying whether the private party has met certain of the requirements in the PPP contract regarding project construction. This usually includes certifying whether the commissioning tests have been met. In some cases, the independent certifier may also have a broader role, assessing whether the private party's construction activities comply with the PPP contract.

If an independent certifier has been appointed, the public partner should:

1. Understand the role of the independent certifier under the PPP contract and allow the independent certifier to perform its role without interference; and
2. Monitor the performance of the independent certifier to ensure the role is properly fulfilled.

The responsibilities of an independent engineer could be broadly categorized as follows:

1. Review and audit the design documentation.
2. Monitor site availability, land acquisition, and permits (including reporting on progress in removing existing facilities, diverting existing services, and any other work necessary to enable construction on the construction works to proceed).
3. Review the construction program (including auditing the program for compliance with the completion requirements specified in the procuring authority's requirements (if any) and the relevant construction contract and, if necessary, recommending any amendments and monitoring the progress and reporting on any variance).
4. Control construction quality (review and audit the performance of the quality assurance system, and audit compliance of the completed construction works with the public partner's requirements).
5. Make a determination as to an extension of any date or period, any monetary compensation, or any relief from penalties as provided for in the concession contract.
6. Inspect facilities and issue certificates.
7. Audit compliance with the environmental requirements and social obligations.

8. Audit operation and maintenance (conduct periodic audits of operations and routine maintenance for compliance with the public partner 's requirements, audit the operation and maintenance manuals and systems, the management information systems and procedures). Review the periodic condition surveys and proposed remedial actions of the concessionaire and arrange independent surveys, if necessary, to establish compliance with performance specifications.
9. Perform financial control (review the proposed payment schedules, report on the contractor's control of progress of works and risks to completion within the time established, Receive the contractor's application for progress payments for construction works and certify amounts due for payment under the construction contract, certify the final amounts, adjudicate claims, submit bi-monthly status reports).

1.5.1. Monitoring the schedule and managing delays

Failure by the private party to complete the construction works on time, and the consequent delay in the delivery of services, is one of the most common challenges experienced in PPPs. To ensure that it has early warning that this might occur and can take any necessary corrective action, the public partner should closely monitor progress of construction against the contractual timelines.

The most efficient monitoring technique is to require the private party to regularly report on progress against the construction schedule. The reporting requirements should be clearly described in the contract. The reporting should include information on the progress of the works, notice of any anticipated delays, the program for managing any delays, and other issues of importance during construction.

The public partner should ensure that the private party is updating the construction schedule to reflect any delays or changes. This is critical because:

- Some obligations of the private party may be mutually interdependent on the public partner's obligations (such as its obligation to hand over land). Any failure by the public partner to perform its obligations at the necessary time may delay the private party, and the private party may be entitled to make a claim against the public partner for costs resulting from the delay.
- Although the PPP contract typically requires the private party to bear most risks that may cause delays, there is always a residual risk for the public partner when a project is delayed. A delay may result in reputational damage for the public partner or in significant impacts on the delivery of public services.

The public partner or its independent certifier should also conduct on-site inspections to check that the construction schedule correctly reflects the actual progress on the ground. If it does not, the public partner should require the private party to update the construction schedule to make it accurate.

1.6. Public partner's review and approvals during the construction phase

In addition to monitoring the performance of the private party and its construction contractor, the public partner typically also has certain review rights during the construction phase of the contract and may be required to give various approvals to the private party. The PPP contract will usually set out the review and approval processes. The public partner should follow these processes to ensure that the contractual risk allocation is maintained.

The first review task during the overall construction phase is ***the review by the public partner of the private party's design*** so as to approve it before construction works commence.³ This gives the public partner an opportunity to identify any potential noncompliance with the output specification. The public partner's feedback in this respect should focus on noncompliance. It should avoid positive confirmations that the design is acceptable to the public partner, as this may result in the public partner "taking back" design risk that has been transferred to the private party. That is, if the public partner confirms that the design is acceptable, and when construction is completed it turns out that the design is incapable of meeting the output specification, the private party may be in a position to argue that it has constructed what was requested by the public partner and therefore is not responsible.

Other approvals necessary during the construction phase relate to ***acceptance of the works and commissioning*** and to ***contract changes*** (see Appendix 2 of this Manual for further guidance on managing changes).

In exercising its review and approval rights under the PPP contract, the public partner should:

1. Follow the process set out in the contract.
2. Ensure that it has all the information required to properly conduct the review or consider whether the approval should be given; if additional information is required, this should be requested from the private party.
3. If the subject matter is complex or technical in nature, consider whether the public partner should engage advisors to assist it in conducting the review or determining whether approval should be given.
4. Conduct the review or make a decision on the approval promptly; an unjustified delay on the part of the private party may result in a claim for relief or compensation by the private party (see Claims Management below).

3. Possible issues related to design (including risks) should be analyzed at the feasibility study preparation stage and reflected in the tender documentation, particularly in the draft PPP (concession) agreement.

1.7. Establishing processes for and managing payments during construction (if any)

Some PPP contracts require the public partner to make payments to the private party during the construction phase of the project. The most common situation in which this occurs is where there is funding support by the public partner, whereby the public partner makes payments to the private party either progressively at milestones during the construction phase, or at the end of the construction phase when all requirements to commence operations have been satisfied.

The public partner must meet its payment obligations. Failing to do so has multiple consequences, such as the public partner breaching the terms of the PPP contract and damaging perceptions of its creditworthiness, potentially adversely affecting its ability to successfully procure future PPPs. Furthermore, the failure of the public partner to make a payment to the private party may in turn result in the private party being in breach of its obligations to its lenders. This can have devastating consequences for the project.

To ensure that the public partner meets its payment obligations, its contract management team should ensure it understands the payment obligations in the PPP contract. Furthermore, it should monitor construction progress, establish a process to assess construction progress (by construction units or as otherwise established in the contract), and ensure that it has accurate forecasts of the amount and timing of payments (see the oversight of construction task above for further information on monitoring construction progress). Moreover, the team should ensure that the necessary internal processes are in place within the public partner to enable it to make the payments when they are due, including ensuring that the necessary budget is available. These internal processes should be documented in the Contract Administration Manual. Finally, the public partner should also ensure that the private party uses any payments it receives in the way required by the PPP contract. For example, if the PPP contract requires the private party to use payments received from the public partner during the construction phase to make progress payments to the construction contractor, the public partner should ask the private party to provide evidence that this has occurred.

in accordance with the PPP Law and the Law on Concession of Ukraine, availability payments are typically paid after the PPP asset/object is in the operations stage, not during construction, since its amount depends on achievement by the private partner of performance indicators defined by the PPP agreement.

1.8. Claims management (compensation and relief events)

During the construction phase, certain events may occur for which the private party is entitled to make a claim under the PPP contract. These events typically fall into two categories:

1. Some events may entitle the private party to claim an extension of the time within which it is required to meet particular obligations under the PPP contract. For example, if the private party is required to complete construction by a specific date, the PPP contract may state that the date

for completion will be extended to a later date if certain events delay construction. These events are often referred to as “relief events.”

2. Some events may entitle the private party to claim compensation from the public partner, in addition to an extension of time. These events are often referred to as “compensation events.”

Often a claim by the private party is a result of the construction contractor making a similar claim against the private party; however, the fact that the construction contractor may have a claim against the private party does not necessarily mean that the private party has a claim against the public partner. If the public partner receives a claim from the private party, it should take the following steps:

1. The public partner’s contract management team should report the claim to senior management (and, if appropriate, central agencies) through the project’s governance arrangements. (Please see Task 15 in the PPP Manual Phase 3 for further information on governance arrangements.)
2. The public partner should analyze the claim to determine whether it is a valid claim under the PPP contract. That is:
 - a. The event must fall within one of the categories defined in the contract or foreseen in the law as a compensation or relief event.
 - b. The claim must be made in the form required under the contract and within any time limit applicable under the contract.
 - c. The conditions, if any, for being entitled to compensation or relief must be met, including the obligation to mitigate the consequences of the event to the maximum extent possible (for example, if the event has delayed the construction works, relief or compensation should only be granted to the extent that the private partner could not have avoided the delay by applying best practice and proper diligence).⁴

Construction of a project is complex, and consequently it can be difficult to separate the impact of a relief event or compensation event from other factors affecting the project. The public partner should seek external expert advice where appropriate to develop an informed view as to the private party’s entitlement in respect of the claim.

3. If a claim is valid, the public partner should ensure that the relevant contractual processes are followed to confirm the private party’s entitlement and should calculate and implement the corresponding relief or compensation. This will include:
 - a. Agreeing on and approving the relief or loss to which the private partner is entitled;
 - b. Deciding which method of relief or compensation (out of those described in the contract) will be applied;
 - c. implementing the relief or compensation (which may include a revision of tariff or the term of the contract if addressing the loss requires capital investment and the procuring authority requests the private partner to finance loss).

4. The definition of general conditions for an event to be qualified as relief or compensation, such as the one cited as an example, should be clearly stated in the contract (defining all relevant matters regarding compensation and relief events).

4. If the claim is wholly or partly invalid, the public partner should seek legal advice on the appropriate form of response to the private party and should develop an appropriate management strategy if it is expected that the private party will persist with the claim, including preparing for and managing a possible dispute (see Appendix 7 of this Manual for further guidance on preparing for disputes).

Box 1. Calculating and implementing compensation

When the private partner makes a claim for compensation, it must advise the public partner of the amount of the direct impact or loss that it has suffered. This will usually be measured as the direct impact of the event on the private partner's cash flows. It will typically consist of a capital cost overrun, an operating and maintenance cost overrun, or a delay or decrease in revenues. If the risk that resulted in compensation being payable is entirely allocated to the public partner, the amount of compensation will be equal to the loss suffered by the private party.

If the risk that resulted in compensation being payable is shared by the parties, the contract will specify that either:

- The amount of compensation will be equal to the loss in excess of a threshold or trigger (for example, the private partner may bear the first \$100,000 of a cost overrun and will only be compensated for the part of the loss in excess of that threshold); or
- The amount of compensation will be equal to a pro rata proportion of the loss (for example, the private partner will bear the 20 percent of a cost overrun and will only be compensated for the other 80 percent).

After the public partner accepts or agrees to the amount of loss suffered by the private partner and the consequent amount of compensation payable, it will have to decide how it will pay the compensation.

Generally, there are two routes for financially compensating the private partner: those that require the private partner to finance the loss, and those that don't.

In general terms, losses that are ongoing (like a downturn in demand or an increase in operating and maintenance costs that is expected to be permanent or continuous) should be compensated by a revision in the tariff or level of service payments. However, events that require additional capital investment (an increase in construction costs or the cost of a significant renewal) may be dealt with by requesting the private partner to bear the loss in first instance (that is, the private party finances the loss) or by granting direct compensation (that is, the government finances the loss).

When the private partner finances the loss, it will be necessary to assess the impact on the equity IRR, so as to restore the financial equilibrium originally expected at contract signature (or at the last time that the financial model and financial plan were reviewed because of a previous compensation event). The financial equilibrium can be restored by means of a higher tariff or higher service payments, a contract term extension, or a combination of all these changes. For that purpose, the financial model will be used to calculate the values of the direct losses expected as well as the financial conditions if the loss is financed partially or totally by lenders.

The contract management team should follow the provisions described in the contract to proceed with these calculations.

1.9. Mechanisms for dealing with private party underperformance and noncompliance during the construction phase

In a PPP, the private party usually only receives revenue once the infrastructure is operational and services are being delivered. The private party therefore has a strong natural incentive to complete the construction phase of the project. This is particularly the case where the contract has a fixed expiration date, so that delays in construction result in a reduction of the operation period, thus reducing the private partner's total revenue over the life of the contract. However, the public partner should not rely on this incentive alone to address underperformance and noncompliance during the construction phase. The public partner should actively use the mechanisms provided in the contract to address underperformance and noncompliance.

The mechanisms commonly included in PPP contracts to address underperformance and noncompliance in the construction phase, beyond the proactive management of risks to mitigate the probability and impact of default, include the following:

1. Liquidated damages or penalties, which are payable by the private party to the public partner. These are usually linked to a delay in meeting the expected date for completion of construction but may also be linked to other contract breaches, such as a failure to submit proper or timely reports. The amount of any liquidated damages or penalties should be determined in accordance with the breach and penalty regime described in the PPP contract.⁵
2. Construction bonds, which usually take the form of an on-demand bank guarantee that can be called by the public partner when, for example, the expected date for completion of construction is not met. The proceeds of the bond are typically used to meet the private party's obligation to pay liquidated damages and may also compensate the public partner for other financial impacts of underperformance and noncompliance.
3. Sponsor support, which usually takes the form of undertakings from the private party's equity investors or key subcontractors to support the private party's obligations. If the private party has failed to perform or to comply with the PPP contract, the undertaking may enable the public partner to demand that an equity investor or key subcontractor remedy the problem or compensate the public partner.
4. Contractual default processes, through which the public partner can issue a warning notice, and demand that the private party remedy the underperformance and noncompliance or provide a "cure plan" detailing how it intends to remedy the problem. If the private party fails to do so, the default process typically leads to more severe consequences including, ultimately, a right for the public partner to terminate the PPP contract.

5. Note that penalties may be enforced through a stepped method, by means of accruing performance points that, once accrued up to certain level/amount, then trigger a dollar amount fine or penalty. These and other nuances regarding penalty systems should be part of contract provisions.

If there is underperformance or noncompliance by the private party during the construction phase, the public partner should:

1. Review the contractual mechanisms available to address the underperformance or noncompliance, and identify:
 - Mechanisms to respond to the underperformance or noncompliance.
 - What, if any, further conditions must be met (for example, expiry of a time period) before the public partner can activate these mechanisms.
 - Consequences of activating these mechanisms, including any consequences under the private party's financing arrangements and construction contract.
 - Required internal approvals before activating each of these mechanisms. In many public partners, an approval by the relevant head of department, director-general or executive board may be required before formal action can be taken under the PPP contract.
 - External advice or other assistance that should be sought before activating each of these mechanisms.
2. Assess the potential impacts of the underperformance or noncompliance and determine the significance of the breach (so as to identify which contractual category the underperformance or noncompliance falls within in terms of the level of the penalty).
3. Determine which mechanisms should be activated. The public partner may have a number of different courses of action open to it. In this situation, it should determine which course of action will provide the best outcome for the government and the public. When taking action in response to the breach, the public partner should follow the process described in the contract and any process required by legislation, including providing any necessary formal default notice.

Not every underperformance or noncompliance necessarily justifies the public partner seeking the full remedies provided for in the contract. The action taken should be determined in light of the overall relationship with the private party. In some instances, it may be appropriate to take no action or to not fully exercise the public partner's rights under the PPP contract. However, failing to fully exercise rights under the PPP contract may have unexpected legal consequences. The public partner should therefore seek legal advice before finalizing a decision to take this approach.

4. Determine what communications to stakeholders and the public may be required. A proactive communication strategy can prevent the public partner becoming inundated with incoming queries from concerned end users, the public, and the media. This includes meeting any obligations under the direct agreement between the public partner and the lenders to notify the lenders and give them the right to propose a remedy plan or even step in.
5. Properly record the breach to have an ongoing record of breaches and performance for the purpose of dealing with persistent breach situations. Underperformance or noncompliance by the private party during the construction phase, and the public partner's response, can introduce significant tension into the PPP relationship. Transparent communication between the public partner and the private party is the key to managing this tension. The public partner should clearly and consistently communicate with the private party about the importance of both performance and compliance with the contract, and the ultimate outcomes sought from

the project. (See Appendix 4 of this Manual for information on communicating and managing the relationship with the private partner.)

By effectively managing the PPP contract through the construction phase, the public partner maximizes the likelihood that the construction phase will be completed on time and on budget so that the operation phase can commence and the project benefits begin to be realized.

2. Tasks performed during the operations phase

The way in which performance should be monitored during the operational stage of a PPP depends greatly on the sector, the way the PPP contract allocates risks, and especially the required output performance indicators and levels of service required of the specific PPP project.

In some PPP projects, the private party operates and maintains the infrastructure throughout the operations phase. In other projects, the private party maintains the infrastructure and may provide certain operational services (such as accident response in transport projects) or some ancillary services (such as security and cleaning in some social infrastructure projects), but the government or municipality (through the public partner or a related government (municipal) agency) operates the infrastructure (that is, it provides the service to the final user or retains the fares or tariff collected from users). Regardless of who operates the infrastructure, the public partner must manage the PPP contract throughout the operations phase to ensure delivery of the expected project benefits. The objectives of contract management in the operations phase are as follows:

1. Ensure that the private partner performs its obligations to maintain and (if relevant) operate the infrastructure.
2. Ensure that the public partner performs its obligations in overseeing the operating phase.
3. Manage stakeholder interfaces to support project outcomes.

2.1. Transition from the construction phase

During the construction phase of a PPP, much of the focus is on completing construction on time and on budget. While completing construction is an important foundation for the success of the project, it is not the primary objective, and it is not enough on its own to deliver the project benefits.

The success of the project ultimately depends on the services provided by the project through its operations phase. The public partner should therefore proactively plan ahead for the transition from the construction phase to the operations phase to ensure that this transition is smooth and that project benefits can be delivered.

The role of the public partner in the transition from the construction phase to the operations phase depends on whether the private party or the government (municipality), through the public partner or a related government (municipal) agency, will operate the infrastructure during the operations phase.

1. In a PPP in which the private party is responsible for operating the facility, the private party will have appointed an operations and maintenance contractor for this purpose. During the construction phase, the public partner should ensure that the private party and its operations and maintenance contractor are planning for the transition to operations and that this activity begins early enough. If the infrastructure operated by the private party forms part of a broader

system or network managed by the public partner, the public partner will also need to plan ahead for the broader system or network impacts of the PPP becoming operational. For example, in a PPP toll road project, the public partner will need to plan ahead for the changing traffic patterns in the surrounding road network once the new toll road opens.

2. In a PPP in which the public partner or a related government (municipal) agency is responsible for operating the facility, the public partner should develop a detailed operational readiness and transition plan well in advance of the completion of construction. If the operator will be a related government (municipal) agency, the public partner should work jointly with this agency in developing the operational readiness and transition plan. The plan should include:
 - a. A recruitment strategy for hiring of staff to operate the new facility or for the transfer of staff from other roles.
 - b. A procurement plan for purchasing any equipment that must be provided by government (municipality) for use in operating the infrastructure (for example, in a hospital project operated by a government agency, some of the medical equipment may be provided by that government (municipal) agency).
 - c. Change management plans to capture the efficiency gains that the new facilities are designed to achieve. These plans may include training operational staff in the new and more efficient ways of working enabled by the new infrastructure and potentially restructuring the operational workforce.
 - d. Familiarization of staff and, where relevant, users with the new infrastructure.
 - e. Communications processes to ensure relevant stakeholders receive timely information that the project is entering its operations phase and are properly prepared for this.

The transition from the construction phase to the operations phase is also a point at which there can be significant changes in the personnel involved in the project. This can include changes in the contract management team; for example, team members with engineering backgrounds who have been monitoring construction progress may be replaced with team members with service management backgrounds who will monitor operational performance of the project. These changes in the contract management team should be managed through the public partner's succession planning processes. (See Appendix 6 of this Manual for further information on succession planning.)

2.2. Operation phase project activities

The following key activities typically occur during the operation phase of a PPP:

1. The private party maintains the infrastructure and provides ancillary services (such as cleaning and security).
2. Either the private party or the government (municipality), through the public partner or a related government (municipal) agency, operates the infrastructure.
3. The public partner monitors the private party's performance, conducts any reviews, and considers any approvals requested by the private party under the PPP contract.
4. The public partner makes the required payments to the private party.

5. The public partner manages any claims by the private party.
6. The public partner responds to any underperformance or noncompliance by the private party.
7. The public partner manages changes (please see Appendix 2 of this Manual), monitors liabilities and reports to central agencies (see the subtask below on monitoring liabilities), plans for unexpected events and responds if these occur (see Appendix 5), manages knowledge and information (see Appendix 6), and manages any disputes that arise (see Appendix 7).

During this phase, the public partner's contract management team has a regular workload conducting its monitoring activities and administering any payments. The team's workload can increase significantly in response to specific events such as changes, unexpected events, or disputes. The public partner must be prepared to provide increased contract management resources when these events occur. (See Appendix 1 of this Manual for more information on resourcing the contract management team.)

2.3. Monitoring liabilities and other reporting obligations

PPP contracts are long-term commitments by the government (municipality) and create long-term liabilities. To perform their whole-of-government roles related to overall management of the government's fiscal position and PPP programs, central agencies require comprehensive information on all of the government's PPP projects and associated liabilities.

The liabilities forecast to arise as a result of the project will have been assessed during the project's appraisal phase. The government must continually monitor and control the PPP program's liabilities and fiscal impact. This requires recurring updates of the fiscal position and value of liabilities of each project. In this sense, at the project level, the public partner plays a key role in monitoring liabilities associated with its PPP projects and reporting to MDETA and MoF on these projects.

The objectives of monitoring liabilities and other reporting obligations are to:

1. Ensure that government decision-makers are aware of long-term fiscal costs through good information and advice on benefits and costs of governmental commitments.
2. Monitor outstanding fiscal obligations and ensure that these obligations can be met.
3. Enable effective (MDETA) oversight of the government's entire PPP program.
4. Disclose obligations to the public in accounts or budget documents in an accurate and transparent manner.

Monitoring liabilities and providing information on liabilities to MDETA and MoF

The public partner must understand and monitor the liabilities created by the PPP so that it can meet its financial management and reporting obligations. The public partner must also provide information on liabilities to MDETA and MoF so that they can take these liabilities into account for whole of government budgeting and accounting purposes.

MoF has whole of government roles that require them to monitor PPP liabilities. In particular, the Ministry of Finance controls the overall fiscal burden of PPP projects and manages government guarantees.

The liabilities created by PPP contracts include:

1. Direct liabilities, which are payments agreed under the contract, such as availability payments in a non-concession PPPs or government support to PPPs in a form of co-funding from state and/or local budget (for example, grant payments).
2. Contingent liabilities, which are potential liabilities that may occur, depending on the outcome of an uncertain future event. In a PPP context, contingent liabilities generally relate to retained and shared risks and represent the estimated value of those risks.

To monitor liabilities the public partner should:

1. Regularly update the estimates of future direct liabilities payable under the PPP contract to take account of any adjustment factors applicable under the contract, such as adjustments for inflation or foreign exchange fluctuations.
2. Ensure that all material fiscal risks are identified in a risk register and the contingent liabilities associated with these risks have been estimated.
3. Regularly update the estimates of the contingent liabilities.

To ensure that the Ministry of Finance can fulfill its whole of government liability monitoring responsibilities, the public partner should regularly report on the liabilities associated with the PPP (concession) contract performance. The public partner should provide for the timing and format of these reports in accordance with the legislation.

The order on monitoring PPP project implementation was adopted in 2020 by the MDETA of Ukraine.⁶ In accordance with this decree, all public partners must report to the MDETA on their PPP (concession) contract performance. The decree also establishes the frequency and format of these reports. After reviewing these reports, MDETA must provide the update report to the Ministry of Finance reflecting the situation under all valid PPP (concession) contracts.

Monitoring reports for the body responsible for PPP portfolio oversight

MDETA has an oversight role of the government's entire PPP portfolio. In particular, the MOEDTA is responsible for coordinating the PPP process and providing knowledge support and advice to public partners.

6. Order of the Ministry of Development of Economy, Trade, and Agriculture of Ukraine from May 26, 2020 No. 986 (registered in the Ministry of Justice of Ukraine on July 6, 2020, for No. 628/34911) "On the statement of the Procedure for submission by the state partners (concessionaires) of the annual report on performance of the contract concluded within the limits of the public-private partnership, including the concession contract."

To ensure that the MDETA can fulfil its whole of government portfolio oversight, the public partner should regularly report to the MDETA on the performance under of the public partner's PPP contracts. The public partner should do this in accordance with the timing and format of the reports established in the legislation. Table 1 sets out the suggested content of these reports, and Figure 1 depicts the process of monitoring the implementation of the PPP contract.

Table 1. Content of reports of public partners in accordance with MDETA Order No. 986, of May 26, 2020

Report Component	Guidance on Content
General information	<ol style="list-style-type: none"> 1. Form (type) and details of the contract 2. Public partner(s) / grantor(s) 3. Private partner / concessionaire (name of legal entity, code according to the Unified State Register of Legal Entities, Individuals — Entrepreneurs and Public Associations, location) 4. Information on amendments to the contract and additional agreements during the reporting period 5. Information on the general status of the contract, in particular: <ol style="list-style-type: none"> i. Information on registration of the right to land plots; ii. Information on the transfer of PPP (concession) object; iii. Information on attracting project financing by a private partner / concessionaire; iv. Information on the commencement of fulfillment of obligations by the private partner in accordance with the agreement; v. Information on the fulfillment of social obligations by the private partner / concessionaire in accordance with the contract.
Performance indicators in accordance with the contract	<ol style="list-style-type: none"> (a) Terms of fulfillment of obligations of the private partner / concessionaire under the contract: <ol style="list-style-type: none"> i. Term of construction (new construction, reconstruction, restoration, overhaul, and technical reequipment) of PPP (concession) object (month, year) ii. Term of the beginning of rendering of the services provided by the contract (day, month, year) iii. Other terms of fulfillment of obligations according to the contract (month, year) (b) Volume of services provided under the contract (for each service) (c) Contract requirements for the quality of services provided under the contract (for each service) (d) Indicators of demand and/or supply for services provided by the contract, in particular the number of consumers of services (for each service) (e) Creation of new jobs under the contract (f) Other performance indicators provided for in the contract, including energy efficiency, environmental, etc.

Report Component	Guidance on Content
Financial obligations of the private partner / concessionaire under the contract	<ul style="list-style-type: none"> (a) Total amount of investments made by a private partner / concessionaire, including: <ul style="list-style-type: none"> i. at the expense of borrowings, thousand hryvnias; ii. at the expense of own funds of a private partner / concessionaire (b) Fulfillment of obligations to the creditor(s) by the private partner / concessionaire, in particular compliance with the schedule of payments and other obligations in accordance with the provisions of the direct agreement (c) Net income of a private partner / concessionaire from the project implementation (d) Total amount of paid payments (fixed, one-time, concession, or other payments) of a private partner / concessionaire (if any), in particular, in favor of: <ul style="list-style-type: none"> i. the state budget ii. local budget iii. balance holder (e) Total amount of penalties applied to a private partner / concessionaire and amount of payments of a private partner / concessionaire for breach of contract (if any) (f) The total amount of penalties applied to the public partner / grantor and the amount of payments of the public partner / grantor for breach of contract (if any) (g) Tariffs for services (cost of services) provided by a private partner / concessionaire under the contract: <ul style="list-style-type: none"> i. base level for the first year of service provision, hryvnias per unit of service; ii. the percentage of net income of a private partner / concessionaire, which is formed at the expense of the tariff; iii. adjustment of tariffs (cost of services) in connection with indexation or by agreement: the period after which the tariff is reviewed (service cost); basis for adjustment (index, coefficient, other) (h) The amount of funds transferred by a private partner / concessionaire to the state, local budgets and state trust funds, including: <ul style="list-style-type: none"> i. VAT; ii. corporate income tax; iii. Income tax; iv. payment for land; v. single contribution to the obligatory state social insurance; vi. other taxes and fees (i) The amount of debt of a private partner / concessionaire to state, local budgets and state trust funds, including: <ul style="list-style-type: none"> i. arrears of value-added tax ii. corporate income tax arrears iii. arrears of personal income tax iv. arrears of land fees v. arrears of payment of a single contribution to the obligatory state social insurance

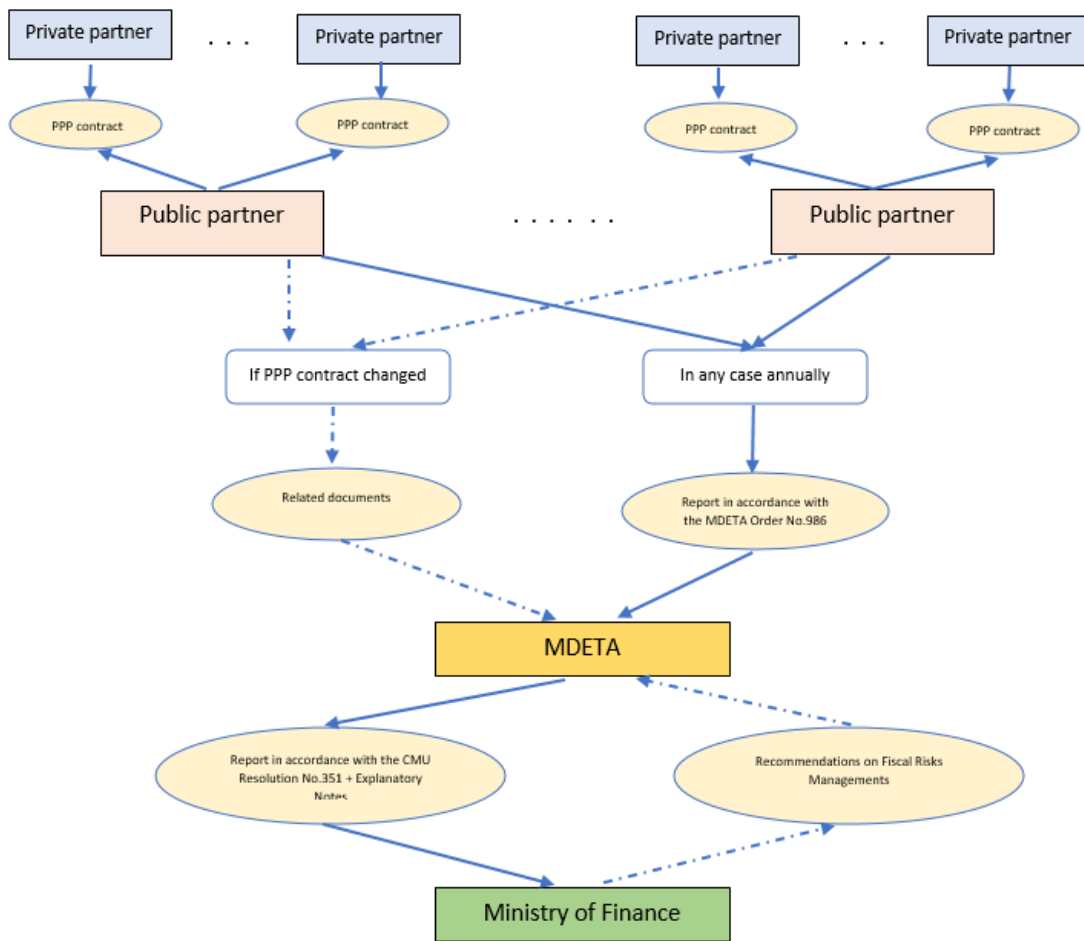
Report Component	Guidance on Content
	<ul style="list-style-type: none"> vi. arrears of other taxes and fees (j) Amount, form, term of validity of the security provided by the private partner / concessionaire, in particular security of the competitive offer and other security within the limits of performance of the contract (k) Debt of a private partner / concessionaire for payment of wages
State support under the contract (if available)	<p>Form of state support:</p> <ul style="list-style-type: none"> (a) Providing a private partner with state and / or local guarantees: volume of guarantee obligations; conditions of occurrence of a guarantee case; warranty period (day, month, year) (b) Volume of PPP project financing at the expense of state or local budgets (c) Amount of payment to a private partner / concessionaire, including in the form of an availability fee (d) Acquisition by a public partner / grantor of a certain amount of goods (works, services) produced (performed, provided) by a private partner / concessionaire under a contract: list of relevant goods (works, services) and their quantity (unit of measurement); frequency of purchase of relevant goods (works, services) (monthly, quarterly, annually); cost (excluding value added tax) (e) Supply to a private partner / concessionaire of goods (works, services) necessary for PPP (concession) implementation: list of relevant goods (works, services) and their quantity (unit of measurement); frequency of supply of relevant goods (works, services) (monthly, quarterly, annually); cost (excluding value added tax) (f) Construction (new construction, reconstruction, restoration, overhaul, technical re-equipment) by state, communal enterprises, institutions, organizations, and/or business associations, 100 percent of shares of which belong to the state, the Autonomous Republic of Crimea, or territorial community, objects of adjacent infrastructure that are not PPP (concession) objects, but are necessary for the implementation of the contract, including: railways, highways, communication lines, heat supply, gas supply, water supply and sewerage, electricity, engineering communications, other objects provided by the contract: a description of the work to be carried out and the status of their implementation; capital investments; date of completion of works in accordance with the contract (month, year); annual costs for operation and maintenance of the facility by the public partner / grantor (g) Form and amount of state support under the contract in another form provided by law
Analysis of risks assigned to the public partner / grantor in accordance with the contract	<ul style="list-style-type: none"> (a) Violation of the term or non-receipt (late receipt) for use by a private partner / concessionaire of the land plot, in case it is necessary for the performance of the contract (b) Violation of the term or untimely transfer of PPP (concession) object to a private partner / concessionaire (c) Delay by the public partner / concessionaire in fulfilling its obligations necessary to ensure the implementation of the project

Report Component	Guidance on Content
	<ul style="list-style-type: none"> (d) Violation of the deadline for access (connection) of PPP (concession) object to the networks of electricity, gas, water supply, sewerage, etc. (e) Delay in obtaining the necessary permits (f) Change in prices (tariffs) for services provided by the contract (g) Increasing funding needs from the state (local) budget, if the relevant payments are determined depending on the volume of services provided (h) Low demand for services provided under the contract (i) Financial and macroeconomic risks (inflation, devaluation (revaluation) of the national currency, etc.) (j) Social and political risks (strikes, protests, war, conflicts in a certain territory) (k) Change of legal regulation leading to losses of a private partner / concessionaire under the contract (changes to laws, adoption of decisions by state bodies or local self-government bodies that violate the rights of private partners / concessionaires, etc.) (l) Force majeure (force majeure) with a high level of impact on the project (m) Other risks assigned to the public partner / grantor in accordance with the contract (n) Termination of the contract at the initiative of the public partner / grantor in case of a significant change in the circumstances that guided the parties in the process of concluding such a contract

By monitoring liabilities associated with its PPP contracts and reporting to the bodies responsible for PPPs on these projects, the public partner ensures that the government has a clear understanding of its liabilities, that financial accounts and budgets are accurate, and that the government's entire PPP program is managed and reported on in a comprehensive and coordinated manner.

Figure 1 presents the process for monitoring and reporting in Ukraine.

Figure 1. Roles and responsibilities in PPP project monitoring and reporting



2.4. Monitoring performance

The public partner should monitor whether the private party is meeting the operations and maintenance requirements in the PPP contract, especially on the service standards or target levels of services. This will also directly affect the calculation of payments to be made in government (municipality)-pays projects and may result in the public partner identifying contract breaches and any corresponding penalties. (See also Task 2.5.)

Contract management actions taken in the early days of the operations phase sets the basis and expectations for later behavior. The public partner therefore must appropriately implement the monitoring arrangements from the beginning of the operations phase.

The public partner's operations phase monitoring activities should reflect the needs of the project and the requirements of the PPP contract. These activities typically include:

1. Reviewing performance reports provided by the private party (in many PPPs, the private party is obliged to collect information on its own performance and regularly provide these reports to the public partner).
2. Conducting audits and spot checks of the private party's performance (where the private party reports on its own performance, the public partner should conduct sufficient audits and spot checks to have confidence that the private party's reporting is accurate).
3. Attending operations meetings with the private party to discuss performance.
4. Reviewing any feedback received from users or beneficiaries of the project.

Box 2. Examples of performance monitoring practices

Airport PPP contracts require the conformity of the services delivered at airports/terminals with national and international guidelines. Furthermore, each contract specifies its own operational rules and performance criteria. Each of these are monitored by the State Airports Authority. In addition:

- All services are audited either regularly or randomly.
- Documents and complaints received from users are rigorously assessed.

The Ministry of Customs and Trade receives regular activity reports during the operations phase of its PPPs. In addition, the performance of the operator is evaluated against feedback from ministry personnel serving in the field and from users.

Monitoring should also include financial monitoring of the private party's financial position, financing arrangements and payments by the private party to its operations and maintenance contractor. This enables the public partner to assess the risk that certain contingent liabilities will arise and contractual guarantees will be called upon (for example, minimum revenue guarantees). It also enables the public partner to value any potential benefits to be shared by the private partner (such as payments to the public partner that accrue when certain traffic thresholds are met).

The public partner should ensure that the private party has in place operations and maintenance plans and manuals and promptly updates these over the life of the PPP to reflect any changes. The private party should provide copies of these plans and manuals to the public partner. This is critical because these plans and manuals are essential to enable the public partner to take over operations of the infrastructure at the expiration or early termination of the PPP contract.

Given the long-term nature of most PPPs, in addition to its regular monitoring the public partner should also carry out project and contract reviews on a periodic basis. These reviews can have two objectives:

1. Periodic reviews are a way of monitoring the project in order to assess its overall fitness for purpose and to identify how it can be adapted to a changing environment (such as changes in the public partner's requirements).

2. Periodic reviews are a way of checking whether the private party is actually delivering the required services and of evaluating its efficiency in doing so.

Often, reviews will help maintain and/or improve the value for money of the PPP project. In some instances, a periodic review may result in the public partner identifying that a change in the PPP contract is necessary or desirable. (See Appendix 2 of this Manual, which provides further information on how the public partner can implement such changes.)

2.5. Establishing processes for and managing payments

Many PPP contracts require the public partner to make payments to the private party during the operations phase of the project. This is naturally the case in a government (municipality)–pays PPP. It may also be the case in user-pays PPPs (concessions), for example, if viability gap funding is payable as a subsidy during the operational phase of the project.

Payments by the public partner to the private party are typically made in a regular cycle, usually monthly, quarterly, or biannually. The PPP contract will usually require the private party to issue an invoice to the public partner at the conclusion of each specified contractual payment period.

The contract will also set out the payment mechanism, outlining the base amount of the payment, any automatic adjustments (for example, adjustments for macroeconomic variables such as inflation), and the calculation of deductions for underperformance or noncompliance. Some payment mechanisms can be complex, and it is critical that they are fully understood by the contract management team.

The contract will usually require the public partner to make the relevant payment within a specified period of time after receiving a correct invoice from the private party.

The public partner must meet its payment obligations. Failing to do so has multiple consequences:

1. The public partner is in breach of the PPP contract.
2. Perceptions of the creditworthiness of the public partner may be damaged and may adversely affect its ability to successfully procure future PPPs.
3. The failure of the public partner to make a payment to the private party may in turn result in the private party being in breach of its obligations to its lenders. This can have catastrophic consequences for the project.

To ensure that the public partner meets its payment obligations, its contract management team should:

1. Ensure that they understand the payment obligations in the PPP contract.
2. Establish the necessary internal processes to enable the public partner to calculate or validate the payments, deductions, and adjustments required. These internal processes should be documented in the Contract Administration Manual. Unless the payment mechanism is very

simple, the public partner should develop a payment model for the purposes of calculating or validating the payments, deductions, and adjustments. (See Appendix 1 of this Manual for further information on payment models.)

3. Ensure that the necessary internal processes are in place within the public partner to enable it to make the payments when they are due. These internal processes should also be documented in the Contract Administration Manual.

2.6. Claims management (compensation and relief events)

During the operations phase, certain events may occur for which the private party is entitled to make a claim under the PPP contract. As was the case during the construction phase, these events typically fall into two categories:

1. Some events may entitle the private party to claim an extension of the time within which it is required to meet particular obligations under the PPP contract. For example, if part of the infrastructure ceases to be available and the contract requires the private party to then ensure that the infrastructure becomes available again within a specific period of time, the contract may state that this period of time will be extended if certain events outside the private party's control delay it in remedying the unavailability. These events are often referred to as *relief events*.
2. Some events may entitle the private party to claim compensation from the public partner, in addition to an extension of time. These events are often referred to as *compensation events*.

A claim by the private party may be a result of the operations and maintenance contractor (or another contractor appointed by the private party) making a similar claim to the private party; however, the fact that a contractor may have a claim against the private party does not necessarily mean that the private party has a claim against the public partner.

If the public partner receives a claim from the private party, the steps it should take are consistent with the steps that applied in the construction phase:

1. The public partner's contract management team should report the claim to senior management (and, if appropriate, central agencies) through the project's governance arrangements (see Task 15 of the PPP Manual Phase 3 for further information on governance arrangements).
2. The public partner should analyze the claim to ensure that it is a valid claim under the PPP contract. That is:
 - a. The event must fall within one of the categories defined in the contract or foreseen in the law as a compensation or relief event.
 - b. The claim must be made in the form required under the contract and within any time limit applicable under the contract.
 - c. The conditions, if any, for being entitled to compensation or relief must be met, including the obligation to mitigate the consequences of the event to the maximum extent possible (for example, if vandalism is a compensation event and it occurs, compensation should

only be granted if the private partner complied with its obligations to avoid such events or minimize losses, for example through supervision of the site and adequate storing and protection of materials sensitive to vandalism).

An operational PPP project may be complex, and consequently it can be difficult to separate the impact of a relief event or compensation event from other factors affecting the project. The public partner should seek external expert advice where appropriate to develop an informed view as to the private party's entitlement in respect of the claim.

3. If a claim is valid, the public partner should ensure that the relevant contractual processes are followed to confirm the private party's entitlement and to make any necessary payment of compensation.
4. If the claim is wholly or partly invalid, the public partner should seek legal advice on the appropriate form of response to the private party and should develop an appropriate management strategy if it is expected that the private party will persist with the claim.

2.7. Mechanisms for dealing with private party underperformance and noncompliance during the operations phase

In a PPP, the private party's revenue during the operations phase is linked to its performance. The private party therefore has a strong natural incentive to perform its obligations during the operations phase of the project. However, the public partner should not rely on this incentive alone to address underperformance and noncompliance during the operations phase. The public partner should actively use the mechanisms provided in the contract to address underperformance and noncompliance.

The approach used by the public partner to deal with private party underperformance and noncompliance in the early days of the operations phase sets the basis and expectations for later behavior. The public partner therefore must appropriately respond to any underperformance and noncompliance from the beginning of the operations phase.

The mechanisms commonly included in PPP contracts to address underperformance and noncompliance in the operation phase, beyond the proactive management of risks to mitigate the probability and impact of default, often differ from those in the construction phase. In the operations phase, liquidated damages and penalties are less commonly used, as deductions from government (municipality) payments achieve the same financial outcome with less difficulty. Bonds and sponsor support are also less common in the operations phase than in the construction phase but may be available to the public partner in some projects. In addition to these, the contract may contemplate that, during operation, the public partner has a right to conduct increased oversight at the expense of the private partner, typically when there are persistent breaches or any other evidence that the private partner's quality management systems are not working effectively.

If the underperformance and noncompliance does not have consequences under the payment mechanism, a default process under the PPP contract is likely to apply. The default process may also

be triggered in addition to payment deductions if an issue for which there are payment deductions persists for an extended period or if there are multiple such issues within a defined period of time (known as *persistent breaches*). The default process typically allows the public partner to demand that the private party remedy the underperformance or noncompliance (or provide a *cure plan* detailing how it intends to remedy the problem). If the private party fails to do so, the default process typically leads to more severe consequences including, ultimately, the public authority's right to terminate the PPP contract and exercise the step-in rights of the public partner and lender.⁷

In cases of underperformance or noncompliance by the private party during the operations phase, the steps to be taken by the public partner are consistent with the steps that applied in the construction phase:

1. Review the contractual mechanisms available to address the underperformance or noncompliance and identify:
 - a. Mechanisms that may be used to respond to the underperformance or noncompliance.
 - b. Further conditions that must be met (for example, expiry of a time period) before the public partner can activate these mechanisms.
 - c. Consequences following from activating these mechanisms. With respect to this, the public partner should consider any consequences under the private party's financing arrangements and any operations and/or maintenance contracts.
 - d. Internal approvals required before activating each of these mechanisms and formal action that can be taken under the PPP contract. (Procedures related to organizing cooperation between the partners including the timing should be documented in the PPP (concession) agreement.)
 - e. External advice or other assistance to be sought before activating each of these mechanisms.
2. Assess the potential impacts of the underperformance or noncompliance and determine the significance of the breach (to identify which contractual category the underperformance or noncompliance falls into for determining the level of the penalty).
3. Determine which mechanisms should be activated. The public partner may have a number of different courses of action open to it. In this situation, it should determine which course of action will provide the best outcome for the government (municipality) and the public. When taking action in response to the breach, the public partner should follow the process described in the contract and any process required by legislation, including providing any necessary formal default notice. Not every underperformance or noncompliance necessarily justifies the public partner seeking the full remedies provided for in the contract. The action taken should be determined in light of the overall relationship with the private party. In some instances, it may be appropriate to take no action or to not fully exercise the public partner's rights under the

7. CMU Decree No. 541, July 1, 2020, "On approval of the Procedure for replacement of a private partner (concessionaire) under an agreement concluded within the framework of a public-private partnership (concession agreement)."

PPP contract. However, failing to fully exercise rights under the PPP contract may have unexpected legal consequences. The public partner should therefore seek legal advice before finalizing a decision to take this approach.

4. Determine what communications to stakeholders and the public may be required. A proactive communication strategy can prevent the public partner becoming inundated with incoming queries from concerned end users, the public, and the media. This includes meeting any obligations under the direct agreement between the public partner, private partner and the lenders to notify the lenders and give them the right to propose a remedy plan or even exercise step in.
5. Properly record the breach to have an ongoing record of breaches and performance for the purpose of dealing with persistent breach situations.

Underperformance or noncompliance by the private party during the operations phase, and the public partner's response, can introduce significant tension into the PPP relationship. This is particularly the case where the issue persists for an extended period of time or significantly reduces the service outcomes and benefits delivered by the project. Transparent communication between the public partner and the private party is key to managing this tension. The public partner should clearly and consistently communicate with the private party about the importance of both performance and compliance with the contract and the ultimate outcomes sought from the project.

Box 3. Step-in rights and contract termination

Often the private partner's under performance and breach of contract may lead to risk of early termination. Early termination of a PPP contract is truly a last resort and must follow a whole range of processes, commencing with an act of default by one of the parties or some continuing force majeure. From a contract management perspective, the focus should be on avoiding termination by managing performance adequately, identifying and mitigating risks that might lead to a default, dealing with defaults in good time and in accordance with the PPP contract, and managing disputes in accordance with the dispute resolution process (DRP). One way lenders seek to protect themselves against termination of the PPP contract following the private partner default is to negotiate step-in rights through a direct agreement with the public partner, the private partner, and the lenders (or their representatives).

In principle, there are two types of step-in rights in PPPs: (a) public authority step-in rights; and b) lender step-in rights (both are allowed according to the legislation in Ukraine). These provide the benefit of time and flexibility to fix whatever the private partner has done to risk termination of the project. At best, step-in rights can benefit all parties, i.e., lenders have a chance to protect their investment, and the public partner and users of the infrastructure may benefit from continuity of the project.

The public partner's immediate concern is to ensure that, if step-in occurs, both the risk allocation and the service provision are preserved and that the step-in does not make the situation worse

and result in the public partner receiving back an asset that it can do nothing with. The formal existence of step-in rights gives lenders comfort in terms of bankability and provides a framework within which the parties can come together to negotiate solutions in a default/termination scenario, subject to the impact of mandatory law. Lenders should be given every opportunity to step in and even to exercise preemptive rights to dispose of the private partner rights and retender these to a new private partner. Lenders will also request this right when they have called a default under their financing agreements and accelerated their debt (in this circumstance the private partner will have to be replaced if the PPP contract is to continue). The step-in period is usually agreed to be a reasonable length of time for the lenders to try to rectify the problem or find a new private partner and will end when the agreed step-in period expires, the lenders formally step out, a new private partner is appointed, or termination occurs due to new default events. The public partner and its advisers should ensure that the time periods under the relevant agreements are correctly aligned so that the whole process can work effectively.

The public partner will, however, normally reserve the right to terminate the PPP contract for any new breaches that occur during the period of step-in. Decisions to terminate the PPP contract should be taken after consideration of the financial and nonfinancial consequences of doing so.

Sources: ADB, EBRD, IsDB, IDB, WBG (2016), PPP Certification Guide; World Bank (2017), Guidance on PPP Contractual Provisions, 2017 ed.; EPEC (2018), A Guide to the Main Provisions of an Availability-Based PPP Contract: PPPs in the Western Balkans.

Step-in-rights procedures have been adopted by CMU Decree No. 541, of July 1, 2020, “On approval of the Procedure for replacement of a private partner (concessionaire) under an agreement concluded within the framework of a public-private partnership (concession agreement).”⁸

2.8. Monitoring project benefits

In addition to monitoring the private party’s performance and conducting periodic project and contract reviews, the public partner should monitor the delivery of the expected project benefits. These benefits reflect the underlying reasons for the original decision to undertake the project. If the benefits are not being delivered, the question arises as to whether that decision was a good one and whether the infrastructure and associated services should continue in their current form. A failure to achieve the expected project benefits may be due various causes, including:

1. *Poor structuring of the PPP.*
2. *Poor performance by the private party.*
3. *Poor performance of any components of the project that were delivered separately from the PPP.* For example, if a rail project includes civil works procured using traditional delivery and operating systems and rolling stock delivered as a PPP, faults in the civil works may result in

8. <https://zakon.rada.gov.ua/laws/show/541-2020-%D0%BF#Text>.

speed and service frequency restrictions on the rail line for safety reasons, thus reducing the benefits of the project as a whole.

4. *Macroeconomic, demographic, or technological changes.* For example, if a public transport PPP was intended to improve accessibility to employment and services for a low-income community that lacked other transport options, macroeconomic and demographic changes over a number of years might result in growing wealth of the local community and a preference to use private vehicles rather than public transport.
5. *Errors in the assumptions used for the original calculation of the expected benefits.* The expected benefits will have been identified during the preparation and structuring phase of the project and, in most cases, will have been quantified as part of the cost benefit analysis conducted to assess the economic feasibility of the project. The public partner should develop and implement a plan for monitoring the delivery of these benefits. It may need to engage external advisors to assist in this work; for example, it may need the assistance of an economic analyst to measure the economic impacts of a project. If the project is not achieving its expected benefits, the public partner should identify the underlying cause or causes of this and consider whether any corrective action is required in order to deliver greater benefits. If the underlying causes include poor structuring of the PPP, or poor performance of the private party, a change in the PPP contract or action to correct the poor performance may be required. (See Appendix 2 of this Manual, which provides further information on how the public partner can implement changes in the PPP contract, and Task 2.6 above, which provides further information on correcting poor performance by the private partner.)

3. Tasks performed during the hand-back process

In most PPP projects, the private party hands back the infrastructure to the public partner at the expiration of the contract or upon its earlier termination, and the public partner puts in place new arrangements for the ongoing operation and maintenance of the infrastructure. The public partner's objectives during the hand-back process are as follows:

1. To ensure that the public partner receives the infrastructure from the private party at hand back in the condition required under the PPP contract.
2. To manage a smooth transition to the new arrangements for the ongoing operation and maintenance of the infrastructure (as governed by the Decree No. 621 on the procedure for return of the concession object approved by the Cabinet of Ministers of Ukraine, July 22, 2020; it applies for non-concession PPPs as well as concessions).

This Decree determines the procedure for returning the concession object to the grantor after the termination of the concession agreement in connection with the expiration of its validity or early termination of the concession agreement. The Decree states that the technical conditions at hand-back should be specified in the concession agreement. The Decree also lists the various activities the concessionaries should undertake at various points in time leading to the hand-back (at least two years prior to hand back, one year and six months before the expiration of the contract). The grantor is required to form a commission to inspect and assess the status and conditions of the hand-back asset and document in a report. The Decree also includes the procedure to be followed in cases of early termination of a concession agreement.

3.1. *Ensuring compliance with the hand-back conditions*

The specification in a PPP contract typically includes a set of "hand-back conditions" that specify the required condition of the infrastructure at the end of the contract term. The PPP contract should include a process that is activated in the final years of the contract to ensure that the private party complies with the hand-back conditions. The process typically includes the following steps:

1. Several years before the contract is scheduled to end (or as early as possible in case of early termination), a technical audit is conducted to assess the condition of the infrastructure.
2. Based on the outcome of the technical audit, the private party is required to produce a revised maintenance plan, setting out any activities required to meet the hand-back conditions in addition to the private party's preexisting maintenance plans. This plan and the technical audit will usually be updated yearly.
3. The contract usually provides a financial mechanism to ensure the private party performs the necessary work to meet the hand-back conditions or (if this does not occur) to compensate the public partner for the private party's failure to meet those conditions. Such a mechanism is necessary because otherwise, by the time a noncompliance with the hand-back conditions is identified, the cash flow to be received by the private party over the remaining life of the

contract may be insufficient to remedy the problem. These financial mechanisms can take a number of different forms. Common examples of such mechanisms include the following:

- a. In projects with government (municipal) payments, the contract may allow the public partner to hold back part of those payments until the private party has completed the work identified in the revised maintenance plan.
- b. The contract may require the private party to deposit funds in a reserve account that can only be accessed to pay for the work required to meet the hand-back conditions or to compensate the public partner for a failure to meet those conditions.
- c. The contract may require the private party to provide a bond (typically in the form of a bank guarantee) that the public partner can draw on to compensate it for any failure by the private party to meet the hand-back conditions.

To properly manage the process for ensuring compliance with the hand-back conditions, the public partner should:

1. Plan ahead for the technical audit to ensure that it is comprehensive and is conducted at the right time in advance of the expiry of the contract.
2. Closely monitor the private party's performance of the revised maintenance plan.
3. If required, use the mechanism provided in the contract to ensure the private party performs the necessary work to meet the hand-back conditions or the public partner is compensated for any failure to meet those conditions.

3.2. Planning the future method for managing the project and ensuring continuity of operations after hand-back

If the infrastructure will be handed back to the public partner upon expiration or termination of the contract, and there is an ongoing need for the infrastructure and the associated services, the public partner must ensure continuity of the operation and maintenance of the infrastructure after hand-back. There are usually a range of options available to the public partner in these circumstances. The options typically include:

Option 1: The public partner may itself take responsibility for delivering the services currently performed by the private party (such as operations and maintenance of the infrastructure).

Many PPP contracts are structured so that the ultimate legal ownership of the project's underlying or immovable assets rests with the public partner itself, while the private service provider is given the right to construct and "use" those assets for a temporary period of time. However, the public partner is advised that taking over an asset that was constructed some 20 years ago and becoming responsible for its continued operations may not provide it with the best value for the public's money. The long-term assets and buildings be some 20-years-old and rely on out-of-date technologies. If the initial PPP contract was successful in realizing better value for money by allocating the risks of design, financing, construction, and maintenance to the private sector, then perhaps a new, similarly structured follow-on PPP contract may be a better option. Such a successor

PPP contract could be structured on a Rehabilitate-Operate-Transfer (ROT) basis. Before making such a decision, public partners should conduct a new feasibility analysis for the project to systematically evaluate which option does in fact provide the best value for the public's money. While it can appear attractive to public partners and even to end users to know at the very start of a PPP contract that all long-term assets being constructed will eventually be transferred to the public sector, it may not be attractive after 19 years.

Option 2: The public partner may be able to conduct an open competitive tender process to outsource the services currently performed by the private party under a new arrangement, possibly with a new private provider to invest in their renewal and rehabilitation and to operate them for a suitable period of time to recover their costs.

This option should also only be selected if it is demonstrated, through a systematic PPP feasibility analysis, to provide the best value for the public's money. Some advantages of this approach are that it can continue to transfer risks like construction/rehabilitation and operating risk to the private sector while using the competitive pressures from open tendering to realize the best value for the public's money. However, when existing assets have been designed, built, and maintained by an incumbent private service provider for some 20 years, many potential competitors may decline to bid on a follow-on PPP contract like this, believing that the incumbent service provider has superior information and is more likely to win any follow-on PPP tender.

Option 3: The public partner negotiates with the existing private service provider to extend the termination date of the contract, including investments in asset renewal.

This option may offer value for money, but the lack of competition brings with it risks of an unfavorable outcome and concerns over the lack of transparency, and the option may be prohibited or the contract term limited by law. This should only be selected after a systematic analysis demonstrates that this option can provide the better value for the public's money. If the incumbent private service provider's new proposed price for the follow-on ROT contract is above this level, then their proposal should be accepted. The possible disadvantages of this option are that, if not done thoroughly and systematically, it may allow the incumbent private service providers to become more like a monopoly that sets its own prices free of the competitive pressures of open tendering.

Option 4: If the PPP contract is structured on a Build-Own-Operate (BOO) basis, and it is the private service provider that owns the project's residual assets, then the public partner may simply allow the contract to expire and let the private service provider dispose of its residual assets.

The majority of PPP contracts are for infrastructure assets that governments assume will continue to provide their current functions beyond the 20-year contract term. Assets like roads, water treatment plants, natural gas piped networks, and schools will continue to be needed to perform their original purposes past 20, 30, or more years. However, in some specific sectors this long-term continuity of purpose is less relevant. For example, in information and communications technology (ICT) sectors, the technology-driven changes in the market make it difficult to predict whether the

new investments of today will still be relevant in five, seven, or ten years. Such PPPs are sometimes structured as BOO contracts. At the end of the contract term the project is assumed to simply stop its operations. It then becomes the job of the incumbent private service provider to dispose of the project's residual assets, for which the private service provider is the legal owner. This may be done by selling them for their salvage value (if any), properly disposing of any hazardous materials or equipment, and selling any buildings or land through the open real estate market. BOO contracts are often used in the power generation sector. Even though governments assume that the land and buildings will continue to be needed for power generation well beyond the term of the initial PPP contract, they may find it contractually simpler to structure them as BOO rather than BOT contracts and to make management of the project's 20-year-old assets the responsibility (or liability) of the private service provider. Governments (municipalities) may also benefit from this because it gives them greater contracting flexibility. They can now wait for some 15 years or more before having to choose the best option that fits their needs at the time and provides the best value for money: they can seek to negotiate an extension for the private service provider to renew the project, or they can simply let the contract expire.

The public partner should use the process described below to determine which option is the most appropriate (including extending the term of the current contract or directly negotiating with the current private partner if this is a legally valid option). The public partner's process to identify the appropriate option and ensure continuity of operations after hand-back should begin several years before contract expiration. The process should involve the following steps:

1. The public partner should conduct due diligence to understand:
 - a. The contract expiry conditions and any contractual options available to the public partner (for example, any requirements that the private party assist the public partner in retendering the services);
 - b. Infrastructure condition (this should be covered by the technical audit conducted to ensure compliance with the hand-back conditions);
 - c. The past performance of the private party;
 - d. Lessons learned from the current contract (including any reviews that have been undertaken);
 - e. Current market conditions for any potential new contract for the operation or maintenance of the infrastructure;
 - f. For user-pays projects (concessions), the level of viability of the project, including an estimate of the potential value of projected benefits and a range of value that an investor could be willing to pay.
2. The public partner should identify its future service delivery needs for the relevant sector and how they are best delivered (proposed mode of service delivery), including the infrastructure required to support service delivery. This analysis should determine the specific future role of the infrastructure provided under the PPP contract in meeting these future service needs following expiration of the contract. The analysis should include consideration of whether any modifications or expansion of the infrastructure are required.

3. Based on the due diligence and analysis in steps 1 and 2, the public partner should develop a strategy for the future operation of the infrastructure and delivery of associated services. This strategy should be developed in accordance with the government frameworks that generally apply to decisions about the operation of infrastructure and delivery of services. In particular, if the preferred strategy is for private sector operation through a new PPP arrangement, the same processes should be followed as for any new PPP project to the extent they are relevant. For example:
 - a. The strategy should include analysis of commercial feasibility, affordability and fiscal impacts, and value for money.
 - b. The strategy should describe the proposed governance structure and resourcing required for its implementation.

The procuring authority should refer to the Manuals for Phases 1, 2, and 3 for further information on the processes that apply if the preferred strategy is for private sector operation through a new PPP arrangement.
4. The public partner should then seek government (municipality) approval and funding for the strategy and for any additional resourcing required to manage that transition. The approval requirements should be the same as for any other similar PPP proposal.

Following approval, the public partner should manage the transition to the new arrangements in accordance with the strategy. Development and implementation of the strategy for continuity of operations after hand-back will require significant work. The contract management team for the operations phase may not have the capacity to do this work in addition to their regular contract management roles. The public partner should either expand the contract management team so that it has the capacity for both its regular work and the development and implementation of the strategy or set up a separate team to develop and implement the strategy.

Appendix 1. Key Tools in contract management, including the Contract Administration Manual

The public partner's contract management team will require a range of tools to assist it in managing the PPP contract. The objectives of implementing and using contract management tools are to:

1. Ensure that complex and repetitive contract management tasks are performed efficiently and consistently with the contract.
2. Ensure that the public partner understands and properly exercises its rights under the PPP contract and performs its obligations under the contract.
3. Assist the public partner in managing risk over the life of the PPP contract.
4. Ensure that the contract management team retains and can easily access all necessary documents and information over the life of the PPP contract.
5. Enable changes in the membership of the contract management team to occur without a loss of project knowledge.

a. Developing a Contract Administration Manual

The PPP contract sets out the rights and obligations of the public partner and the risks allocated to the public partner. However, the contract generally does not explain the internal processes that are necessary within the public partner to exercise those rights, perform those obligations, and manage or respond to those risks. For example, in a government (municipality)–pays PPP, the contract may state that the private party must issue an invoice for the availability payment to the public partner by a particular date each quarter, and the public partner must then either pay the amount invoiced or dispute the invoice (if it is incorrect) within a certain number of days. The PPP contract will not set out the internal processes that the public partner must follow in order to approve and make the payment or to verify whether the invoice is correct or should be disputed.

This information should be collated in a Contract Administration Manual. Box 4 sets out a suggested outline of a Contract Administration Manual for the operations phase of a PPP. Public partners should adapt this outline to the circumstances of each individual project.

Box 4. Outline of a Contract Administration Manual for the operations phase of a PPP**Part A Preliminary details**

- Purpose and scope of Manual
- Responsibility for developing the Manual
- The project and its status
- Summary of the deal
- Parties to the contract
- History of the project to date
- Key dates
- Other interested stakeholders and communication arrangements

Part B Governance and resourcing

- How will the public partner's role be performed?
 - Staffing
 - Operational budget
 - Use of advisors
- Governance arrangements
- Internal reporting
- Knowledge management tools
- Succession Plan

Part C Contract management strategy and framework

- Contract management strategy
- Risk analysis
- Risk register and its review and update
- Contingency arrangements
- Dispute resolution
 - Contractual provisions and their implementation

Part D Contract obligations and management processes

- Obligations of the public partner (government or municipality)
- Obligations of the private party
 - The public partner's monitoring processes
- Invoicing, payment and abatement
- Public communications
- Change events and change processes
- Processes for relief events and compensation events

Part E Ongoing review and development

- Project reviews
- Reviewing and updating the Contract Administration Manual

Adapted from State of Victoria (Department of Treasury and Finance), Partnerships Victoria Contract Management Guide (January 2018). Available at <http://www.dtf.vic.gov.au/Infrastructure-Delivery/Public-private-partnerships/Policy-guidelines-and-templates>. Used under a Creative Commons Attribution 4.0 license.

Some of the processes required in the Contract Administration Manual will be developed specifically for the PPP project (see Box 5 for an example). These processes should be:

1. Developed by the contract management team;
2. Approved by an appropriate decision maker within the governance structure;
3. Included in the Contract Administration Manual; and
4. Reviewed on a regular basis and updated if necessary.

Box 5. Example of a contract management process specific to the project

Some of the processes required to administer a PPP contract will be developed just for that project.

For example, the contract for a toll road PPP may require the private party to provide regular reports to the public partner detailing traffic volumes and revenue received from users. The public partner's contract management team should develop a process for verifying the accuracy of these reports and the correctness of the calculations.

The contract management team may also need a process for then passing the traffic volume and revenue information on to other key stakeholders. These may include:

- Relevant departments within the public partner, for example, the department responsible for future road network planning.
- Central agencies, for example, if the PPP contract includes a minimum revenue guarantee or other financial support, the public partner may need to keep the Ministry of Finance informed of the traffic volumes and revenue.

Other processes required to administer the PPP contract may already exist within the public partner. For example, in a government (municipal)–pays PPP, the public partner may be required to make regular availability payments to the private party. The public partner will have existing financial management processes that govern how payments to suppliers and contractors must be approved within the public partner and how the payments are made. Where such processes exist, the public partner's contract management team should:

1. Include in the Contract Administration Manual a cross-reference to the existing process and an explanation of how that process applies to the PPP;
2. Ensure that the contract management team is consulted in relation to any changes in the existing process, in which case the team should consider any implications of that change for the PPP project and update the Contract Administration Manual accordingly.

The Contract Administration Manual should also contain background information on the project so it can serve as a reference document throughout the life of the contract and help new members of the contract management team understand the project. The Contract Administration Manual should be:

1. Written in a reader-friendly style, without legal jargon;

2. Concise, using flowcharts, diagrams, charts, tables, and lists where these will aid comprehension, rather than lengthy sections of text;
3. Modular, to enable the contract management team to easily access information when needed and to facilitate regular updating of the manual;
4. Regularly updated, to ensure it contains current information about the project and reflects current processes.

It is recommended that the initial contract management team prepare the initial version of the manual during (or soon after) the tender preparation and procurement phase of the project, in collaboration with the project team who managed the tendering of the project. This approach has three advantages:

1. It ensures that the manual will be written in a style that is most useful to the contract management team;
2. It enables the contract management team to capture the knowledge of the project team that managed the structuring and tendering of the project; and
3. It helps the contract management team to become familiar with the PPP contract.

If a public partner has multiple PPP contracts of a similar type, it is beneficial for the Contract Administration Manuals for each project to have a similar format and structure. This enables contract management team members to more easily work across multiple projects and facilitates the sharing of lessons of good practices between projects.

The Contract Administration Manual is a valuable tool for the contract management team. However, the team should always remember that the manual is not a substitute for the contract, which will always remain the source of the parties' legal rights and obligations.

b. Other key contract management tools

The contract management team will need a variety of tools in addition to the Contract Administration Manual. The particular tools will vary from project to project. The public partner should identify the necessary tools when it is developing its contract management strategy (see Task 15 of PPP Manual Phase 3). The tools required are likely to include:

1. *An electronic document management system for storing electronic documentation related to the project.* This should include copies of the contract for reference purposes, the Contract Administration Manual in electronic form, copies of all correspondence between the parties to the contract, and all other information that should be retained consistent with good record-keeping practices. The public partner's existing electronic filing systems may be largely suitable for this purpose; however, the long term of a PPP contract can create some document management challenges. As the technology changes and is updated over the life of the contract, the contract management team should ensure that it can continue to access all historical documentation. With the introduction of new systems over time, the contract management

team may need to convert documentation to a new storage format or to retain access to old systems.

2. *A filing system for hard copy records.* The contract management team should ensure that it will have easy access to key documents throughout the life of the contract. The public partner's existing filing systems may be largely suitable for this purpose. The signed contract and other legal documentation should be stored in a secure location.
3. *A system for recording and analyzing data related to the performance of the private partner and for producing reports as required to senior management of the public partner and to other stakeholders.* In some projects, the public partner's systems will receive data directly from the private party's performance recording systems or the public partner will have access to the private party's systems.
4. *A workflow management system that records the tasks the contract management team are responsible for in managing the contract and automates key processes, such as the receipt and approval of reports from the private party.* The public partner may not need such a system for a single small PPP managed by a single person. For public partners with more complex projects, larger contract management teams, or a portfolio of PPPs, however, a workflow management system can provide significant efficiencies. It can also be an important risk management tool, assisting the public partner to exercise its rights and perform its obligations under the contract in a timely manner.

The private party (or one of its main sub-contractors) may use a particular workflow management system for managing communication with its subcontractors and suppliers. The parties should consider using this system for managing the formal communications between the public partner and the private party under the PPP contract.

Box 6. Risk management plan

To properly monitor and manage contingent liabilities in a PPP contract, it is important for the public partner to formulate a risk management plan based on the earlier risk allocation matrix formulated for the project. The plan would set out the following:

- *For the public party's risks or shared risks*
 - An evaluation of the different options for treating each risk;
 - The public partner official/officer who will be responsible for managing the risk;
 - The procedures and mechanisms that will be used to control the risk; and
 - An estimate of the resources that the institution will have to allocate to manage the risk.
- *For the private partner's risks*
 - The obligations and reporting requirements the government has imposed on the private partner to ensure that risks are managed;
 - The officer/official who will be responsible for monitoring the risk on behalf of the private partner;
 - An estimate of the resources that the institution will allocate to monitoring the risk; and
 - The mechanisms to be used by the public partner in dealing with any failure of the private partner to manage the risks (i.e., penalty deductions, step-in rights, etc.).

The plan should also include the business contingency plan the institution will follow to ensure continued service delivery in the event the private partner cannot maintain the service or the public partner is forced to terminate the PPP contract for whatever reason and apply the step-in procedure allowing lenders to step in to the private partner's position in the contract and take control of the infrastructure project where the project company is not performing.

5. *The base case financial model.* The financial model is a critical contract management tool in a PPP project. The private party will have developed its financial model during the tender process. This model sets out in detail the specific cash flows required by the private party to deliver its proposal. It is usual in PPP projects for the model to be updated at financial close, becoming the "base case financial model" for the purposes of the contract. The base case financial model is used throughout the term of the PPP contract, particularly as a key input to the calculation of the financial consequences of change events and compensation events. The contract typically includes a specific process for updating the model to reflect such changes. In user-pays (concession) projects such as toll roads, the financial model is often an important input to various demand risk-sharing mechanisms, such as government sharing in additional revenue generated by the private party. Given the complexity of the base case financial model, the public partner should consider seeking advice from its financial advisors on the use and interpretation of the model. The public partner should also institute quality assurance processes to ensure that any updates to the model are correctly made.

The base case financial model in government-pays projects and user-pays projects with government (municipal) payments (for example, viability gap funding payments) includes the forecast amounts payable by the public partner to the private party. However, the base case financial model may not have the functionality required to easily calculate or validate the actual amount payable in each payment period, taking into account any performance-based deductions (for example, due to unavailability of the infrastructure) and other payment adjustments provided for in the contract. In this situation, unless the payment mechanism is very simple, the public partner should also develop a payment model for the purposes of calculating or validating the payments, deductions, and adjustments required.

6. *A payment model.* A payment model is a computer spreadsheet that allows the contract management team to input the level of performance achieved by the private party against each of the key performance indicators, together with any other parameters that affect the amount of the payments (for example, current inflation or exchange rates) each payment period. Based on those inputs, the payment model calculates the payment due for that payment period, including any deductions and adjustments, in accordance with the contract. The public partner should consider seeking assistance from its financial advisors to prepare the payment model. A well-designed payment model can significantly reduce the time required for payment calculations and can eliminate or reduce the risk of calculation errors.
7. *Progress report.* The template of such report is outlined below.

Project	Title of Project																				
1	<p>Progress Report</p> <p><i>For a structured report, reference should constantly be made to the project milestones as indicated in the PPP contract.</i></p>																				
2	<p>Performance Review</p> <p><i>The report/review will focus on the Private Partner’s compliance with the minimum performance standards and specifications (MPSS) agreed upon in the PPP contract. The public partner should note if there have been instances of non-compliance, or delay in compliance, as well as the private partner’s liability thereto.</i></p>																				
3	<p>Contractual Issues</p> <p><i>This section should highlight both existing and foreseeable contractual issues raised by either party. These issues will be prepared in tabular form, as follows:</i></p> <table><tr><th>Contractual Issue</th><th>Status</th><th>Proposed Solution</th></tr><tr><td></td><td></td><td></td></tr><tr><td></td><td></td><td></td></tr><tr><td></td><td></td><td></td></tr><tr><td></td><td></td><td></td></tr><tr><td></td><td></td><td></td></tr></table>			Contractual Issue	Status	Proposed Solution															
Contractual Issue	Status	Proposed Solution																			
4	<p>Status of Payments / Obligations</p> <p><i>Details on status of payments/obligations to be settled, either by the public partner or the private partner to the other party or to other parties are to be specified, especially those that incumbent upon the public partner for budgetary planning purposes.</i></p>																				
5	<p>Updates on Risk Exposure</p> <p><i>Updates on the risk exposure of the public partner shall be detailed here. Reference should be made on the risk management plan and its corresponding risk register. The idea is to continually update these two documents and two reflect such updates herein.</i></p>																				

Appendix 2. Change management

During the term of a PPP contract, a number of change events are likely to occur, either initiated by a party or occurring at times prescribed in the contract, that will require proper management. The public partner may have foreseen some of these change events at the time of the project tender preparation and may have provided for them in the contract. The public partner should manage these events in accordance with the process specified in the contract.

Other changes may not have been foreseen at the time of the tendering preparation but may be necessary or desirable to achieve better project outcomes. If the PPP contract does not contain a process for managing a change, the public partner and the private party may need to renegotiate some elements of the contract.

The objectives of change management are to:

1. Ensure that changes affecting the project are managed in a coordinated and properly planned manner;
2. Preserve the risk allocation, unless a change in the risk allocation is in the interests of the government and the community;
3. Improve or protect the value for money outcomes achieved by the project.

A range of other events may result in a change in a party's rights or obligations under the contract. For example, if the private party is entitled to make a claim under the contract as a result of the occurrence of a particular event, this may result in a change in the time within which the private party must perform an obligation and may entitle the private party to additional payment as compensation for the event. (See Sections 1 and 2 of this Manual for guidance on the management of claims during the construction and operations phases, respectively.) If an unexpected event such as a force majeure event occurs, the private party may be relieved of its obligations to the extent it is affected by the force majeure event (see Appendix 5 of this Manual for guidance on the management of unexpected events).

a. Government-initiated modifications

In good international practice, many PPP contracts include a *modification* or *variation clause* that enables the public partner to request changes to the infrastructure and the services provided by the private party under the contract.

A *modification* is a change in the infrastructure or the services that is implemented through a process set out in the contract. Therefore, it is different from renegotiation (see section f of this Appendix).

These clauses typically have the following features:

1. The public partner has a right to request modifications to the infrastructure and services provided under the contract. The contract typically also includes limits on the value, size, or nature of modifications that the public partner can request or require the private party to implement. Limits on the range of possible modifications may also be contained in legislation.
2. The contract includes a process for the private party to consider and respond to modification requests.
3. The modifications process includes mechanisms by which the public partner can determine whether the costs of the modification represent value for money. If the private party is asked to offer a price for the modification, there is a risk that the pricing may reflect a noncompetitive margin. In some circumstances, PPP contracts mitigate this risk by requiring the private party to conduct a competitive tender for the construction work or additional services requested by the public partner.
4. The contract specifies how costs and savings arising from modifications will be allocated between the parties and how and when payments for modifications are made.

Some PPP contracts also include a streamlined process for small modifications.

In managing government-initiated modifications, the public partner should apply the following principles:

1. Follow the processes set out in the PPP contract. This helps to maintain the project's risk allocation, ensures that the public partner has access to robust information for decision making, and ensures that there is adequate documentation of decisions taken that may later reduce the likelihood of disputes.
2. Ensure that modifications are subject to the same degree of scrutiny and control as would apply to any similar government investment or action implemented outside of a PPP contract. The change process in the PPP contract should not be regarded as a way of circumventing ordinary government processes, and care should be taken to ensure that any changes offer value for money. For example, if a modification involves an additional capital cost for the public partner, the modification should be approved through a similar process to an equivalent capital expenditure that occurs outside the PPP, as the additional capital expenditure is a new public investment.
3. Begin with a carefully developed scope a clear output specification and performance standards for the modification. The output specification and performance standards should be developed in conjunction with users and other stakeholders to ensure a thorough understanding of what is needed and what will be delivered. For complex modifications, the public partner should consider engaging technical advisors to assist in developing the output specification and performance standards for the modification.

The public partner should also assess whether any permits may be required from other institutions or agencies and who should be responsible for obtaining these permits. If a permit is necessary for the modification to proceed, the public partner will need to

determine whether it or the private partner should obtain the permit. As a general rule, if the permit is required regardless of the particular solution adopted by the private partner to implement the modification, the permit should be obtained by the public partner. However, if the need for the permit or its terms will be affected by the solution adopted by the private partner to implement the modification, the permit should be obtained by the private partner.

4. Ensure that users, stakeholders and decision makers have realistic plans for delivery timeframes and a realistic expectation of the costs and service impacts of the modification. The public partner should ensure that the relevant decision makers understand and consider all cost impacts of the modification, including any changes in ongoing operations and maintenance costs and future replacement or refurbishment costs.
5. Identify any short-term disruption that will occur when the private party implements the modification and ensure that the relevant stakeholders are aware of and can manage this disruption. For example, if a modification involves new construction activities in a hospital PPP built and maintained by the private party but operated by the government, the public partner should consider how the construction activity will disrupt hospital operations.

If a modification in a toll road PPP involves construction of a new interchange between the toll road and another road, the public partner should consider how the construction activity will affect the use and management of the surrounding road network, as well as the traffic volumes and hence the revenue on the toll road.

6. Identify any tests that the private party should be required to undertake in order to demonstrate that the modification has been completed. For example, if a modification in a hospital project involves installing new equipment in an operating theater, the private party should be required to undertake tests to confirm that the operating theater meets all of the contractual requirements related to infection control, temperature, lighting, etc., once the new equipment is installed.
7. Consult with the private party with respect to the potential modification prior to issuing the formal request for the modification. Such interaction enables the parties to clarify possible issues arising from the modification, while fostering greater understanding of both the public partner's and the private party's needs and concerns.
8. Critically review the cost of the modification quoted by the private party. If the PPP contract requires the private party to conduct a competitive tender for the construction work or additional services, the public partner should review that tender process to ensure it was properly managed and achieved a value for money outcome. If costs of the modification are not determined through a competitive tender, the public partner should benchmark the cost quoted by the private party against costs for similar construction works or services. The public partner should also ensure that the private party has taken into account any cost savings or additional revenues when quoting the cost impact of a modification. For example, if a modification in a toll road PPP involves constructing a new interchange between the toll road and another road, the construction activity may cause short-term traffic disruption and

hence lower toll revenue at that time; however, once construction is completed, the new interchange may result in higher traffic volumes and hence higher revenue.

9. Ensure that appropriate insurance, warranties, and updated manuals and plans are in place to reflect the modifications. For example, the hand-back package provided by the private party to the public partner (see tasks performed during the hand-back process in Chapter 3 of this Manual) should be updated with “as built” design drawings showing the modification. If a modification materially increases the replacement cost of the infrastructure, the public partner should usually require the private party to increase its insurance to cover the new replacement cost.

b. Private party–initiated modifications

PPP contracts focus on outputs. The contract typically gives the private party significant flexibility as to how they deliver the outputs. However, in some circumstances, the private party may wish to modify how it delivers the infrastructure or the services but can only do so with the public partner’s consent. See Box 7 for examples of these circumstances.

Some PPP contracts provide a process through which the private party can request the public partner’s consent for modifications to how it delivers the infrastructure or services. These processes typically have the following features:

1. The private party has a right to propose modifications to the infrastructure and services provided under the contract.
2. The contract includes a process for the public partner to consider and respond to modification proposals.
3. The contract usually specifies that all costs resulting from a private party–initiated modification must be met by the private party. The contract may provide that any cost savings must be shared between the parties.

Box 7. Circumstances in which the private party may propose modifications

Circumstances in which the private party may propose modifications include the following:

1. It is common for the public partner to incorporate the private party's tender proposal into the PPP contract at the conclusion of the tender process. The private party is therefore obliged to deliver the project in accordance with its proposal. During the term of the contract, the private party may identify an alternative approach to delivering the output specification.

For example, in a road project the output specification may include design and strength requirements for bridges and overpasses, without specifying what construction materials must be used. The private party may have proposed to use concrete beams for constructing the overpasses and bridges, but due to a fall in the price of steel it may now be more cost effective to use steel beams. The appropriate way of requesting the ability to use steel beams rather than concrete beams as specified in the private party's proposal is for the private party to propose a private party-initiated modification.

2. Some elements of the output specification may become outdated or prove to be unnecessary during the life of the contract. The private party may therefore request an amendment to the output specification.

For example, in a hospital PPP the output specification may include a range of requirements to ensure that medical imaging equipment can be used in the hospital. These may include special electricity supply requirements and provision of radiation shielding for the rooms in which the equipment is located. Due to changes in technology, new equipment that does not require a special electricity supply or radiation shielding may become available. The private party may therefore wish to remove the special electricity supply and radiation shielding from the hospital to save costs. As these items are required by the output specification, the private party cannot remove them without the public partner's consent. The appropriate way to obtain this consent is by proposing a private party-initiated modification.

In managing private party-initiated modifications, the public partner should apply the following principles:

1. Follow the processes set out in the PPP contract.
2. Carefully review the proposed modification and identify any potential risks and issues that may arise as a result of the modification, seeking further information from the private party when necessary. For complex modifications, the public partner should consider engaging technical advisors to assist in reviewing the proposal.
3. Identify any tests that the private party should be required to undertake in order to demonstrate that the modification has been completed.
4. If the public partner is entitled to share in the cost savings resulting from a private party modification, the public partner should critically review whether the private party has properly identified all likely cost savings.
5. If the public partner consents to the modification, it should ensure that appropriate insurance, warranties, and updated manuals and plans are put in place by the private party.

For example, the hand-back package provided by the private party to the public partner (see THE tasks performed during the hand-back process described in Chapter 3 of this Manual) should be updated with "as built" design drawings showing the modification.

c. Resetting events

Some PPP contracts provide for a significant aspect of the contract to be reset when certain triggers are reached. For example:

1. In many social infrastructure PPPs, such as hospital projects, the costs of soft services (such as catering, cleaning, and security) are benchmarked or market-tested at periodic intervals, typically every five years. The benchmarking or market-testing identifies the current market price for the services. In the case of benchmarking, this is done by comparing the cost and performance of the services delivered by the private party with a sample of other comparable service providers. In the case of market-testing, the private party is obliged to periodically retender certain services to test their value for money on the market. The government (municipality) payments made by the public partner to the private party are adjusted to reflect the market price determined through the benchmarking or market-testing. This ensures that the public partner receives value for money for these services.
The PPP contract will state whether benchmarking or market-testing is required, and if so, when it is to occur and which services are benchmarked or market-tested. In some contracts, the public partner may have discretion as to which of the two approaches is used. Otherwise, only one approach (benchmarking or market-testing) is specified.
2. In some airport PPPs, an obligation for the private party to invest in expansion of the airport is triggered when passenger volumes reach certain thresholds. The term of the PPP contract is extended to enable the private party to recover this additional investment.

In managing these events, the public partner should apply the following principles:

1. Follow the processes set out in the PPP contract.
2. Begin planning well before the relevant trigger is reached. Resetting events require significant additional work by the public partner's contract management team, even if the private party has primary responsibility for running the benchmarking or market-testing process or making the additional investment. The market-testing process in a complex social infrastructure PPP such as a large hospital may take up to two years from when the parties begin planning the process to the finalization of all of the resulting changes to the project. The public partner may need to expand its contract management team and engage technical, financial, and legal advisors to assist it in the process.
3. Ensure that key stakeholders and decision makers are properly briefed and involved in the process when required. For example:
 - If market-testing may result in changes in availability payments made by the public partner to the private party, the contract management team should ensure that the public partner's internal finance department is aware of the process and the nature and timing of the changes so that it can make the necessary budgeting and financial reporting changes.

- If an increased investment trigger may result in expansion of an airport, the contract management team should ensure that the government agencies responsible for transport links to the airport are aware of the size and timing of the expansion so they can plan for the likely increase in travel to and from the airport.
4. Validate and, where appropriate, challenge the information provided by the private party in relation to the resetting event. For example:
 - If the market-testing process in a social infrastructure PPP contract requires the private party to conduct tenders to establish the prices for services such as cleaning and catering, the public partner should ensure that the tender processes conducted by the private party represent a genuine competitive process to secure an efficient market price for the services.
 - If an increased investment trigger may result in expansion of an airport and a consequent increase in the term of the PPP contract to enable the private party to recover its investment, the contract management team should ensure that the private party has secured competitive financing for the expansion and the increase in the term of the PPP contract is no more than is necessary to recover that investment.
 5. Fully document the outcome of the resetting event and capture it as required within the PPP contract. For example:
 - Following a market-testing process in a social infrastructure PPP, it may be necessary to update the payment amounts set out in the contract to reflect the new price for the relevant services.
 - If increased investment has been triggered in an airport project, it may be necessary to record the increase in the term of the PPP contract as well as a range of details of the proposed airport expansion.

The contract management team should also update the Contract Administration Manual (see Appendix 1 of this Manual) to capture the key details and lessons learned from the resetting process to prepare for such processes in the future for the same or any similar PPP.

d. Refinancing

Many PPP contracts contain provisions that regulate changes in the private party's debt financing arrangements, requiring the private party to obtain the public partner's consent for certain of those changes. These provisions often regulate not only refinancing in the sense of raising new debt and using it to repay existing debt, but also other changes in the debt financing arrangements, such as:

1. Changes in the interest rate charged on the debt
2. Extension of the debt maturity
3. Increase in gearing (that is, the amount of debt relative to equity)
4. Changes in the debt providers' requirements for the private party to hold cash in reserve accounts

Such changes are often regulated in the PPP contract because they can affect the risk profile of the project. In addition, in some cases these changes can result in financial benefits for the private party's investors. These benefits are known as *refinancing gains*. In some PPP contracts, the public partner is entitled to a share of the refinancing gains.

If the private party requests the public partner's consent for a refinancing or other change in the debt arrangements regulated by the PPP contract, the public partner should apply the following principles:

1. *Follow the processes set out in the PPP contract.* The public partner should not unnecessarily resist refinancing proposals, as they are a desirable and sometimes necessary feature of an active PPP market. However, the public partner should follow the processes set out in the PPP contract when assessing refinancing proposals, as these processes have been included in the contract to ensure that the risks associated with the refinancing are properly assessed and the public partner receives any share of the refinancing gains to which it is entitled.
2. *Consider what skills and capabilities are required to assess the refinancing proposal and, if the contract management team does not already have those skills and capabilities, find them elsewhere.* Unless the refinancing is clearly a very simple transaction, the public partner should engage financial and legal advisors to assist it in assessing the refinancing proposal.
3. *Ensure that the private party has provided all information that the public partner needs to assess the refinancing proposal.* Private parties' refinancing proposals are often developed without any consultation with the public partner. The private party then provides the public partner with a simple explanation of the proposal and requests the public partner's consent. Often the information provided by the private party is insufficient for the public partner to assess how the refinancing will change the project's risk profile and the amount of any refinancing gain. If necessary, the public partner should request additional information from the private party to enable proposal assessment.
4. *Assess the impact of the refinancing.* The public partner should assess each of the impacts of the refinancing that the contract allows the public partner to consider in deciding whether to consent to a refinancing. If the contract allows it to do so, the public partner should consider any impacts that the refinancing may have on the risk profile of the project. Possible risk impacts include the following:
 - If the refinancing will result in a higher interest rate on the private party's debt or an increase in gearing, there may be a greater risk of the private party encountering future financial difficulties and possible bankruptcy.
 - A higher interest rate, increase in gearing, or changes in the repayment profile of the debt can result in an increase in any contingent liabilities of the government affected by the level of debt. For example, if a termination payment or the amount of a guarantee provided by the government is calculated based on the amount of debt outstanding at a particular time, an increase in gearing may increase the amount of the termination payment or the contingent liability that exists as a result of the guarantee.

- Restrictions in the private party's loan agreement or other contracts with the new financiers may reduce future flexibility in the project. For example, the loan agreement may have greater restrictions on the private party's ability to agree to modifications requested by the public partner or to propose its own modifications that could benefit both parties.

The public partner may need to use the base case financial model to assess the impact of the refinancing. (See Appendix 1 of this Manual on contract management tools for more information on the base case financial model.) If the public partner is entitled to a share of any refinancing gains, it should assess whether any negative impacts of the change in financing are offset by the public partner's share of the refinancing gains.

5. If necessary, calculate the amount of any refinancing gain. If the PPP contract allows the public partner to share in refinancing gains, the public partner should calculate the amount the gains in accordance with the contract, using the base case financial model and, if necessary, seeking assistance from its financial advisors.
6. Consult with other government stakeholders if necessary. If the refinancing will have significant impacts for the government, either through changes in the project's risk profile or by generating a significant refinancing gain for the government, the public partner should consult with the other relevant stakeholders within the government. In particular, if the refinancing may result in significant changes in contingent liabilities, the public partner should consult with the relevant entities (such as the Ministry of Finance). (See tasks performed during the operation phase in Chapter 2 of this Manual for more information on monitoring contingent liabilities and reporting to MoF.)

If the private party experiences significant financial distress, it might attempt to refinance in order to overcome the immediate financial distress through renegotiated debt terms. While such rescue refinancing might reduce the likelihood of the private party becoming insolvent in the short term, in the long term, the new debt might be on unfavorable terms that increase the risk profile of the project for the public partner. In this situation, the public partner should consider whether, despite the unfavorable terms, the refinancing puts the government in a better position than the alternative that the private party becomes insolvent and the consequences of that under the PPP contract and financing documents occur.

e. Change in ownership or control

PPP contracts typically contain provisions that regulate the potential changes in ownership and/or control of the private party that may occur or be requested by shareholders during the life of the contract. In this context, *ownership* generally refers to ownership of shares in the private party, whereas *control* generally refers to the ability to direct or influence the management of the private party (which may or may not relate to holding a specific percentage ownership of the private party). Ownership and control may be direct or indirect.

1. An investor may directly own shares in the private party or directly influence the day-to-day management of the private party.
2. An investor may be an indirect owner or controller of the private party because the investor owns shares in a holding company that in turn owns shares in the private party, or because the investor directs or influences other people or another organization that in turn controls the private party.

The contract will usually provide a specific definition of ownership and/or control and indicate whether they apply to indirect ownership and/or control as well as direct ownership and/or control.

Changes in ownership and/or control are regulated in the PPP contract because they can affect the risk profile of the project. The need to regulate transfers of shares is also linked with transparency and fairness of the procurement, as the proposed ownership of the PPP company is likely to have been considered in the evaluation of the bids. The contract therefore typically requires the private party to obtain the public partner's prior consent for certain of these changes (for example, changes during construction and any changes that amount to a change in control).

In some cases, the public partner may have absolute discretion as to whether it consents (that is, it can refuse consent for any reason); in other cases, it may only be permitted to refuse consent for a limited range of reasons set out in the contract (for example, the incoming controlling shareholder may only need to meet the pass/fail requirements in the original request for qualification (RFQ)).

If the private party requests the public partner's consent for a change in ownership or control regulated by the PPP contract, the public partner should apply the following principles:

1. *Follow the processes set out in the PPP contract.* The public partner should not unnecessarily resist changes in ownership or control of the private party, as they are a desirable feature of an active PPP market. However, the public partner should follow the processes set out in the PPP contract in assessing these changes, as these processes have been included in the contract to ensure that the risks associated with these changes are properly assessed and mitigated.
2. *Consider what skills and capabilities are required to assess the change and, if the contract management team does not already have those skills and capabilities, find them elsewhere.* Unless the change is a simple transaction, the public partner may need to engage financial and legal advisors to assist it to assess the change.
3. *Ensure that the private party has provided all information that the public partner needs to assess the change.* Private parties' proposals for changes in ownership or control are often developed without any consultation with the public partner. The private party then provides the public partner with a simple explanation of the proposal and requests the public partner's consent. Often the information provided by the private party is insufficient for the public partner to assess how the change will affect the project's risk profile. If it requires

further information, the public partner should request that the private party provide this information to enable it to assess the proposal.

4. *Identify who has ownership or control of the private party before and after the change.* In some cases, this is a simple question; however, where the investors use complex ownership structures, it may be difficult to identify which parties fall within the definition of ownership or control in the PPP contract. The public partner may require legal advice in relation to these definitions.
5. *Assess the impact of the change.* The public partner should assess how the change in ownership or control will affect the risk profile of the project. Possible risk impacts include:
 - If the project is dependent on technology or know-how provided by a particular investor and that investor seeks to exit the project by selling its interest, there is a risk that access to the technology or know-how will be lost. In this situation, the public partner should request evidence that the private party will continue to have access to the necessary technology or know-how after the investor has exited the project.
 - The new investor may have less financial capacity than the outgoing investor. In this situation there is a risk that the new investor will be unable to make any planned or unexpected but necessary future contributions of equity to the private party. In this situation, the public partner should request evidence of the incoming investor's financial capacity.
 - The identity of a new investor may create public interest risks for the government. For example, it may be unacceptable to the government and the public for a person with a criminal record to gain control of the private party and be in a position to influence the management of services provided to the public on behalf of the government. The PPP contract may allow the public partner to reject any such proposed change in control.
6. *Consult with other government stakeholders if necessary.* The public partner should consult with any other relevant stakeholders within the government. In some cases, a single investor will be selling out of or buying into two or more of the governments' PPP projects at the same time. If the relevant contracts are managed by different public partners, those public partners should consult with one another to ensure they take consistent approaches in assessing the issues raised by the change.

f. Renegotiation

Although PPP contracts typically contain a number of processes for managing changes, such as those described above, these processes are not always suitable for making all of the necessary or desirable changes that might be proposed during the life of a PPP contract. If a necessary or desirable change cannot be implemented through an existing process within the PPP contract, it may be necessary for the public partner to renegotiate the contract with the private party. In good international practice, renegotiation differs from a modification in that renegotiation is an agreement to change

the terms of the contract, whereas a modification is a change in the infrastructure or the services that is implemented through a process set out in the contract.

While some renegotiations are efficient and can improve project outcomes for the government and the community, many renegotiation requests made by private parties are opportunistic and should be avoided by the public partner. The risks associated with opportunistic renegotiations include the following:

1. Renegotiations are carried out bilaterally, without the positive effects of competitive pressure. It places the private party in a strong bargaining position and makes it difficult for the public partner to achieve good outcomes from renegotiation.
2. Competitive bidding for future PPPs may be distorted, as bidders may submit unrealistic bids with the expectation that they can renegotiate for an improved deal after signing the contract.

Renegotiation of a PPP contract should not be regarded by a public partner as a way of circumventing ordinary government processes. If the public partner believes that a renegotiation is possible within the legal framework and is in the best interests of the project, it should:

1. Carefully assess all of the impacts of the proposed changes in a manner as consistent as possible with the government processes that would apply if the changes were proposed as a new project. This should include comparing renegotiation to other options for achieving the same outcome and carrying out the relevant feasibility, affordability, and due diligence tests that would ordinarily be conducted in evaluating a new project, adjusted as necessary for the circumstances of the renegotiation.
2. Seek expert legal advice on the drafting of the changes to the PPP contract.
3. Consult with relevant central agencies, particularly in relation to the financial impacts of the renegotiation.

It is recommended to take into consideration EU principles as stipulated in its Directive on Concession Awards, Article 43, which includes the following criteria for allowing renegotiation:

1. The modifications, irrespective of their monetary value, have been provided for in the initial concession documents in clear, precise, and unequivocal review clauses and do not alter the overall nature of the concession.
2. Additional works or services by the original concessionaire are necessary and cannot be provided by a new concessionaire for valid economic and technical reasons, and procurement of a new concessionaire would impose “significant inconvenience or substantial duplication of costs” on the contracting authority.

g. PPP price adjustment

It is nearly impossible to write a PPP contract that can foresee with certainty all material changes to the delivery of a service beyond five or ten years. In signing a PPP contract, all parties essentially

agree at the outset that there may be changes in the conditions within which a PPP project operates and that these are likely to affect the costs that a private service provider must bear. Therefore, some predictable procedures should be agreed upon in advance in the PPP contract for how instances of any possible adjustments to PPP prices and tariffs should be requested, reviewed, and decided.

Price adjustment techniques are models for making predictable decisions about whether and how any changes should be made to a PPP contract's prices or tariffs in response to specific changes in the surrounding conditions. These changes in conditions usually result in changes (i.e., increases) to the operating costs or the investments that a private partner must fund. The key decision about which price adjustment technique a PPP project should adopt depends upon what types of performance the government would like to incentivize from the private partner, such as more efficient operations or increased investments.

The two main options of setting and adjusting prices for long-term PPP projects are rate of return regulation or price cap regulation. Each technique provides different incentives for the private partner to either make new investments in the project or to improve the operating efficiency of the project. Neither technique is necessarily superior to the other. Rather, each should be applied to meet the unique needs and priorities of the project or of the given infrastructure sector and the specific PPP project.

In practice, most large, capital-intensive PPPs prescribe a variant of the price cap technique, and the review period is for the entire 20+ years of the PPP project's life. Prices are often automatically adjusted according to changes in the agreed inflation rates, world energy price indexes, foreign exchange rates, etc. This protects private investors and their lenders from the "regulatory risks" that a local regulator or the public partner may decide, such as for political reasons, to agree that the private partner's costs are increasing or that new investments (such as renewing and replacing medium-term assets) should be made, while also requiring that prices should not increase, in hopes of making the services more affordable to local consumers.

Rate of return regulation

In rate of return regulation, the public partner must first review all of the assets that the PPP project company has invested in and determine if they are "used and useful." Second, it reviews the operating expenses of the PPP project and determines if they are all "prudent and necessary." The main decision the monitor must make focuses on deciding what the service provider's return on capital should be. Finally, the prices the private contractor charges are adjusted to meet the new revenue requirement that provides this approved rate of return.

In practice, fixing the rate of return a private service provider earns has been an effective method of incentivizing the private investor to proceed with making new investments in long-term assets. Investors are nearly assured that if they make these new long-term investments, they will earn a

fair return on it. Rate of return regulation has not, however, been a very effective way of encouraging operating efficiency by private partners. In practice, it has been difficult for regulators to force companies to either cap or to reduce their operating expenses when their rate of return is also fixed.

Price-cap regulation

The second major technique for managing price adjustment issues for PPPs is price-cap regulation. Unlike rate of return regulation, price-cap regulators first fix the maximum price(s) that the private service provider may charge during a given test period, say five years. The public partner allows the private service provider to earn and keep whatever returns it achieves from their efficiency improvement for that five-year period. In practice, this has been an effective way of incentivizing private service providers to improve efficiency and reduce any excess operating expenses. However, this technique has not necessarily encouraged private service providers to make new investments in areas like system reliability and security. While a price-capped private partner would choose to invest in a new asset that reduced operating costs, such as a new automated remote meter-reading (ARM) system to replace more expensive human meter-readers, it would be reluctant to invest in new assets that do not directly reduce operating costs, like back-up systems and added security, unless clearly required to do so by the PPP contract and by its monitor. Under the price-cap technique, monitors often need to be more vigilant in their efforts to make sure private service providers are not being overly aggressive in reducing their operating costs at the expense of the technical quality and reliability of their service.

When prices are capped for a given test period, such as five years, they are pegged to a common retail price index (RPI), minus an efficiency factor X. The X-factor is the single most important decision that the PPP regulator makes. It represents the annual rate of improvements in operating efficiency that the regulator believes the company can reasonably make. For example, if the inflation rate for a five-year revenue period remains constant at 10 percent per year, and the regulator believes that the service provider can reasonably improve its efficiency by 3 percent per year, then the service provider is allowed to raise its prices by 10 percent less 3 percent, or 7 percent per year. In other words, the private service provider must reduce its operating costs by at least 3 percent each year just to maintain the same level of profitability. What often happens in practice, however, is that at the start of the review period when the X-factor is first announced, private service providers will work hard to reduce their operating costs by more than the X-factor because of the incentive to maximize their profitability during the remainder of the five-year review period.

Appendix 3. Engaging advisors during the contract management stage

Public partners require a wide range of skills and capabilities to manage a PPP contract. It is usually the case that the public partner does not have the full range of necessary expertise in-house. In addition, the contract management workload is highly variable, and it is inefficient for the public partner to continually employ a contract management team that is large enough to manage the infrequent busy periods. To fill these capability and capacity gaps, the public partner may need to hire a range of advisors from time to time to assist with contract management tasks.

Appendix 3 of the PPP Manual Phase 1 contains general guidance on planning and managing the procurement of advisors. That guidance also largely applies to the procurement of advisors to assist with contract management, but the public partner should also consider the following:

1. During contract management, the background knowledge of the advisors who worked on the project during the earlier phases can be very valuable.
2. Conversely, in a dispute situation, it may be in the public partner's best interests to seek advice from advisors who have had no previous involvement in the project. For example, if a dispute arises in relation to the legal interpretation of the contract, there is a risk that the lawyers who originally drafted the contract for the public partner may not provide objective advice on the dispute as they may feel obliged to stand by their drafting of the contract. If the public partner seeks advice from a different legal advisor, that advisor may provide more objective advice in relation to the dispute.

Potential roles of advisors during contract management

The potential roles of advisors during contract management, and the scope of their roles, will vary depending upon the issues that arise during the term of the PPP contract. Table 2 sets out a list of possible tasks on which advisors can assist the public partner. The public partner should ensure that the contract management team has access to funds to hire advisors for these and other purposes over the term of the PPP contract.

Table 2. Possible advisor roles during contract management

<i>Task</i>	<i>Legal Advisor</i>	<i>Financial Advisor</i>	<i>Technical Advisors</i>
Using the base case financial model		<ul style="list-style-type: none"> Can advise on the use of the base case financial model during contract management 	
Developing and using a payment model		<ul style="list-style-type: none"> Can develop and advise on the use of a payment model for calculating or validating the payments, deductions, and adjustments required under the PPP contract 	
Government-initiated modifications	<ul style="list-style-type: none"> Can advise on the contractual modification process 	<ul style="list-style-type: none"> Can advise on the financial impacts of modifications 	<ul style="list-style-type: none"> Can assist in developing the output specification and performance standards for the modification
Private party-initiated modifications	<ul style="list-style-type: none"> Can advise on the contractual modification process 	<ul style="list-style-type: none"> Can advise on potential cost savings from modifications 	<ul style="list-style-type: none"> Can assist in reviewing technical aspects of the proposed modification
Resetting events	<ul style="list-style-type: none"> Can advise on the contractual process for the resetting event and any consequential contract amendments 	<ul style="list-style-type: none"> Can advise on the financial impacts of resetting events, such as a change in contractual payments following market testing of services provided by the private party 	<ul style="list-style-type: none"> Can advise on the technical aspects of resetting events, such as by reviewing designs for any proposed expansion of the infrastructure as a result of a trigger for increased investment being achieved
Refinancing	<ul style="list-style-type: none"> Can advise on the refinancing provisions in the PPP contract 	<ul style="list-style-type: none"> Can assist in reviewing the private party's refinancing proposal and calculating any refinancing gains 	
Changes in ownership or control	<ul style="list-style-type: none"> Can advise on the relevant clauses in the PPP contract and the ownership structure of the private party 	<ul style="list-style-type: none"> Can advise on whether any change may compromise the future financial stability of the project 	

<i>Task</i>	<i>Legal Advisor</i>	<i>Financial Advisor</i>	<i>Technical Advisors</i>
Dispute resolution	<ul style="list-style-type: none"> Can advise on the dispute resolution process in the PPP contract and on any legal issues that are in dispute 	<ul style="list-style-type: none"> Can advise on any financial issues in dispute 	<ul style="list-style-type: none"> Can advise on any technical issues in dispute
Government review and approvals during the construction and operations phases	<ul style="list-style-type: none"> Can advise on any legal matters that must be reviewed or approved by the public partner 	<ul style="list-style-type: none"> Can advise on any financial matters that must be reviewed or approved by the public partner 	<ul style="list-style-type: none"> Can advise on any technical matters that must be reviewed or approved by the public partner
Ensuring compliance with the hand-back conditions			<ul style="list-style-type: none"> Can assist in the technical audit of whether the infrastructure is expected to meet the hand-back conditions
Ensuring continuity of operations after hand-back	<ul style="list-style-type: none"> Can provide legal advice on options to ensure continuity of operations after hand-back 	<ul style="list-style-type: none"> Can provide financial advice on options to ensure continuity of operations after hand-back 	<ul style="list-style-type: none"> Can provide technical advice on options to ensure continuity of operations after hand-back

Appendix 4. Relationship management

PPPs, by their very nature, typically span a long time frame; involve complex relationships between the various parties involved; and include many stakeholders, among them private partner, subcontractors, lenders, investors, end users, regulators, other arms of government, and the wider community. Effective relationship management can help mitigate or minimize a range of project risks. For example, the risk of local residents or operational staff (such as doctors and nurses in a hospital project) objecting to the project can be reduced if the public partner properly informs them of the project's objectives, impacts, and benefits. Furthermore, relationship management ensures that the private party better understands the public partner's project objectives and concerns and is more responsive when issues arise. Finally, relationship management provides comfort that the parties can resolve issues effectively and work towards mutually beneficial outcomes. The objectives of relationship management are to ensure that:

1. The public partner has an effective partnership with the private partner based on transparency, openness, mutual respect and co-operation.
2. The public partner has effective relationships with other stakeholders involved in the PPP so that these relationships assist in the achievement of the project outcomes.

a. *Key factors in relationship management*

The key factors for establishing a good relationship between the public partner and the private party and other project stakeholders include:

- *Mutual benefit*. The public partner and the private party must approach the project as a mutually beneficial arrangement.
- *Understanding of objectives*. The government stakeholders in the project, on the one hand, and the private party and other consortium members on the other, must appreciate each other's objectives and those they have in common.
- *Trust*. Trust can only be built up over time. It is fostered by both parties seeking to achieve mutual benefit through open and transparent communication and timely completion of obligations, and it involves a consistent approach to doing business with "no (unpleasant) surprises."
- *Open communication*. Open communication is a key to maintaining a good relationship. It fosters a spirit of cooperation and helps align the parties interests. Open communication does not mean the parties must share all information relating to the project. However, a party should share an information if no good public interest, commercial, or legal reason suggests it not be shared and if sharing the information will enhance the relationship.

Effective relationship management starts with a collaborative, rather than an adversarial attitude. If either party starts with an adversarial attitude, it may force the other party to adopt the same tactics, compromising the long-term interests of both parties. To establish a collaborative working relationship, the public partner should consider arranging externally facilitated relationship-building workshops attended by the contract management team and key representatives of the private party and its consortium partners. These workshops are particularly valuable soon after contract signing, but they can

be undertaken throughout the term of the contract. The content of these workshops should include understanding one another's objectives in the project; learning about the other party's key risks in the project and their plans for managing and mitigating these risks; identifying the roles of individuals representing each party; and specifying the practical forms, purposes, and channels of communication between the parties that will be necessary for successful project outcomes.

Continuity and personal commitment are also important in a relationship. The public partner should therefore aim to limit staff turnover in its contract management team and should institute good succession practices (see Appendix 6 of this Manual).

b. Managing the relationship with the private party

The relationship between the public partner and the private party begins during the tender phase and progressively develops from the time the contract is signed. The relationship should be championed at senior levels in both organizations. Senior management attitudes and actions will signal to other staff how they should treat the relationship.

The public partner should recognize the importance of the commonality of interest involved in a PPP project. The contractual risk transfer, the output specification, and the payment mechanism are important contributors to this commonality of interest, as they align the private party's commercial interests with public partner's project objectives.

The public partner and the private party should strengthen their relationship by sharing relevant information where there is no public interest, commercial, or legal reason for not doing so. The public partner should ensure that the private party's management hear criticisms and find out about issues directly from their public sector counterparts rather than through indirect channels. Concerns about the wider relationship should be discussed frankly, whether they relate to contract performance, progress, or people. If these points are not observed, the risk is serious that problems will worsen. Both parties should avoid being defensive about criticism. The focus should be on providing and seeking information with a view to improving the relationship over time rather than unnecessarily apportioning blame.

The public partner's contract management team should analyze all information received from the private party. Where relevant, the information should be incorporated into the Contract Administration Manual or other contract management tools.

The public partner should consider creating an issue register outlining outstanding issues between the parties, allocating responsibilities, setting timelines, and recording each issue's current status. Ideally, the public partner should share the issues register with the private party through an electronic knowledge management platform (see Appendix 6 of this Manual for general information on knowledge and information management). The public partner may also retain a separate internal issue register for the project that lists issues the public partner does not need to or wish to share with the private party. The public partner should set up the issues registers so that issues can be sorted and filtered in different ways

(for example, by the date the issue was raised, by the target date for resolution, and by the status of the issue).

While good communication should avoid excessive formality, the public partner should take particular care to document verbal communications where it may be necessary to retain an agreed record of what was said. For example, if it is verbally agreed that each party will consider a proposed minor variation to the output specification, a written record of the discussion is critically important to clarify that no party has yet committed to the variation.

Appropriate practices for documenting verbal communications include the following:

1. For informal discussions, the public partner should record the key outcomes and action points and provide this to the private party as confirmation of the discussion.
2. For formal meetings, the public partner or the private party should prepare minutes of the meeting, circulate these to all attendees, and obtain confirmation that the minutes are accurate.
3. The public partner should add any pending matters to its issues registers where appropriate.

The written record or minutes should be prepared or reviewed by a person with a strong understanding of the context of the discussions before being circulated to the other party. The potential consequences of a document being prepared without this input can include the following:

1. The document may summarize the discussion using accurate statements but omit important details that may be disputed in future.
2. The document may inaccurately reflect discussions, which may undermine the public partner's future position, result in a take-back of risk allocated to the private party, or cause unnecessary conflict through use of inappropriate or incomplete wording.

The documents created as a consequence of verbal discussions, as well as other informal communications between the parties such as emails, should be stored in accordance with the public partner's information and document management strategy (see Appendix 6 of this Manual).

Managing the relationship with the private party can be particularly challenging if a dispute arises. Appendix 7 of this Manual provides further information on managing disputes, including techniques to manage disputes without undermining the broader relationship with the private party.

c. Appropriate communication channels and forums

A PPP contract often identifies one or more formal points of contact between the public partner and the private party. For example, the contract may state that the head of the public partner is authorized to issue formal notices under the contract to the private party. However, to ensure a good relationship is maintained, a number of other contact points may be needed.

In most PPPs, the relationship between the parties operates at a number of different organizational levels. Working relationships between the parties should be conducted between peers. Communication channels

therefore tend to run “horizontally” between people at equivalent levels in each organization. The head of the public partner’s contract management team may communicate with senior management of the private party infrequently—but at regular intervals—on strategic matters. The contract management personnel who report to the head of the contract management team, and their private sector equivalents, may communicate frequently on operational matters.

The public partner should identify and define the roles of the contract management team members in communicating with the private party when it is developing the structure of the contract management team. See Task 15 of the PPP Manual Phase 3 for more information on setting up the contract management team.

For horizontal communication between the parties to function effectively, the public partner should:

- *Establish protocols with the private party for these communications.* Where necessary, these protocols should also provide for consultation between the parties in relation to communications between either of them and third parties. For example, it may be appropriate for the parties to consult each other on the content of any public communication in relation to the project. In the case of larger projects with significant public profiles, the parties should have regular formal meetings to discuss public relations.
- *Ensure that the individuals responsible at each level have appropriate skills.* If skills are not properly matched at a particular level, the effectiveness of communication at that level may be compromised. If the head of the public partner’s contract management team believes there is a skills mismatch at a particular level, staffing should be reevaluated or communication channels with the private party altered to correct this problem.

The PPP contract should provide for regular formal meetings between the parties at appropriate levels. The arrangements typically put in place for the operational phase of a PPP contract include:

1. Weekly operational meetings;
2. Monthly operational management committee meetings to review operational performance;
and
3. Quarterly meetings of senior representatives of the parties to discuss strategic issues.

See Box 8 for further information on who should attend these meetings.

Box 8. Who should attend meetings between the parties?

It is important that the appropriate representatives of the parties attend the interparty contract management meetings. If the appropriate representatives do not attend, issues may be overlooked, communication between the parties may be compromised, and any required decisions may be delayed or made without a full appreciation of the consequences.

The appropriate representatives of the public partner will depend on the nature of the project, the composition of the contract management team, the purpose of the meeting, and the current status of the project. The public partner should use the following principles as a guide when determining who should attend meetings:

- *Weekly operational meetings should be attended by representatives with direct knowledge of the day-to-day issues in the project.* For the public partner, this will usually be the contract management team member responsible for day-to-day monitoring of the private partner's performance. If another government agency has significant involvement in the project (for example, as a user of the infrastructure), that agency should also be represented at operational meetings. The private sector representatives should usually include, at a minimum, the private partner's operations manager and a representative of any key subcontractor (for example, the operations and maintenance subcontractor) responsible for day-to-day operational issues.
- *Monthly operational management committee meetings to review operational performance should usually be attended by the head of the contract management team, unless the team is very large and another senior team member oversees operational performance.* The contract management team member responsible for day-to-day monitoring of the private partner's performance should also attend. If another government agency has significant involvement in the project (for example, as a user of the infrastructure), a management representative of that agency should also attend operational meetings. The private sector representatives should usually include, at a minimum, the private partner's chief executive and a management representative of any key subcontractor (for example, the operations and maintenance subcontractor) responsible for day-to-day operational issues.
- *Quarterly meetings of senior representatives should usually be attended by a senior executive of the public partner, supported by the head of the contract management team.* If another government agency has significant involvement in the project (for example, as a user of the infrastructure), a senior executive of that agency should also attend these meetings. The private sector representatives should usually include, at a minimum, the private partner's chief executive and senior executive representatives of any key subcontractor (for example, the operations and maintenance subcontractor) and of the investors and lenders.
- *In some cases, the attendees at particular meetings are specified in the PPP contract.* If the contract specifies who is to attend a particular meeting but it would be beneficial for other people to also be present at the meeting, the public partner should consider asking the specified invitees whether those other people can attend as observers for all or part of the meeting. For example, if the contract specifies that a meeting is to be attended by representatives of the public partner, the private party, and the investors, but it would be beneficial for the lenders to also be aware of progress reports presented at the meeting, the public partner should propose to the private party and the investors that they also invite the lenders.

If the PPP contract does not already require such meetings, the public partner should seek the private party's agreement to conduct them. Another common practice is to conduct periodic field visits to the project. These can be beneficial both for relationship management and as an additional form of monitoring of the private party's performance.

To ensure consistent communication through the various horizontal communication channels, it is essential that there are consistent “vertical” internal communications within the public partner. This ensures that the head of the contract management team and its team members have a common understanding of the status of the relationship and are delivering consistent messages to their private sector counterparts. If this is not done, differences in perspective may create or mask problems in the relationship. For example, the head of the contract management team may regard the relationship as successful, unaware of significant friction between junior contract management personnel and their private party equivalents.

The public partner and the private party should also use their internal vertical communication channels as escalation paths when specific issues must be considered or decisions made at a higher level within each organization. Escalation paths should be understood and used appropriately so that problems are resolved early.

The public partner should also consider regular communication with the private party’s investors, its lenders, and its construction and operations and maintenance contractors, where this is not already set out in the contract. For example, it may be appropriate to invite representatives of the investors and the operations and maintenance contractors to attend performance review meetings on a regular basis.

When communicating with investors, lenders, and contractors, the public partner should ensure that confidentiality and privacy obligations are observed. Particular care should be taken when communicating with an investor that is not the sole owner of the private party or with a lender that is not the sole debt financier.

d. Relationships with the community and broader stakeholder groups

Appropriate consultation and communication with stakeholders is an important component of good governance. A PPP project will often involve or affect a large number of parties, and the interaction between the public partner and the stakeholders can be complex. Finding an appropriate way to involve the different kinds of stakeholders is a delicate matter, as the public partner has to carefully manage each stakeholder’s expectations, interests, and concerns.

The public partner should develop consultation and communications plans that detail how it will manage relationships with the community and broader stakeholder groups. These plans should be documented or referred to in the Contract Administration Manual (see Appendix 1 of this Manual).

In developing its consultation and communications plans, the public partner should consider the following:

- The project stakeholders (see Box 9 for examples in particular types of PPPs);
- The objectives of each stakeholder;
- The stakeholders that must be part of the governance framework for the project and how best to accommodate them within this framework;
- The appropriate contacts within the stakeholder group;

- The matters that each stakeholder should be consulted about;
- The likely involvement and role of each stakeholder;
- Information that should be provided to each stakeholder;
- Whether the stakeholder arrangements have been discussed and agreed to with the stakeholders;
- Methods of documenting the stakeholder arrangements;
- Personnel within government who should be asked for input into the stakeholder communication and consultation plans;
- Need for a public communication process.

Box 9. Examples of key stakeholders

In hospital PPP projects, the stakeholders other than the public partner may include the national health administration, the medical staff (such as doctors and nurses), the hospital administration staff, the local residents, future patients, and environmental groups.

In road PPP projects, the stakeholders other than the public partner may include the relevant local governments, the landowners, the local residents, the rail authority if the project crosses a rail line, and the bodies in charge of water, gas, and electricity infrastructure.

Some projects may be of such significant interest to the community and to parties such as other governments, that the contract management team must be equipped to provide public information and provide site tours. The public partner should also consider establishing a project website as a means of communicating with a wide audience.

Many PPP projects have a range of government and/or municipal stakeholders. These stakeholders may include departments of the public partner that are not directly responsible for the management of the contract, or other government agencies that perform central government functions (that is, central agencies) that influence the decision-making process and are usually part of the governance framework. The public partner should distinguish between stakeholders that must be part of the project's governance framework during the contract management phase and those that do not need to be part of that framework. (See task 15 of the PPP Manual Phase 3 for further guidance on setting up a governance framework.) In developing the governance framework, the public partner should consider whether establishment of a reference group to enable effective communication and consultation with other government parties who have a strong interest in the project but are not directly involved in the decision-making process may be warranted.

Even if the private partner has, under the PPP contract, taken the risk associated with dealing with a particular stakeholder, the contract management team can play a role in informing that stakeholder about the project and ensuring that they do not unnecessarily slow down the project. For example, where the private partner is responsible for obtaining a permit from another government agency, the contract management team can ensure that the other government agency fully understands the project and the context in which the private party is seeking the permit. However, the contract management team should

not provide any assurance to the private partner that the permit will be granted, as this decision is the responsibility of the other government agency.

Appendix 5. Contingency planning and managing critical events

In a PPP, the majority of the risks affecting the project are transferred to the private party. The private party, therefore, will generally bear the financial consequences of unexpected events affecting the project. However, the public partner could face several residual risks, such as:

1. The public partner retains ultimate accountability to users and the community for the risk of service delivery failure by the private party.
2. If the private party fails to deliver services as required under the contract, the public partner may face significant reputational damage, and the failure may inconvenience users and possibly other third parties.
3. If an unexpected event is classified as a force majeure under the PPP contract, this may relieve the private party of its obligation to provide services, but the public partner may be compelled or subject to strong pressure to ensure the public or other third parties are not inconvenienced.

Therefore, the public partner must undertake contingency planning to mitigate these risks. The objectives of contingency planning and managing critical events are to:

1. Establish appropriate plans so that the public partner is prepared to respond to any unexpected events that occur during the life of the PPP contract.
2. Respond effectively and mitigate risks to the public partner and users when critical events occur.

a. Planning ahead for potential step-in, default, termination, or force majeure

The PPP contract will include specific processes for managing some unexpected events. These processes typically include:

1. *Step-in processes*, allowing the public partner to take over some of the private party's responsibilities under the PPP contract.
2. *Default processes*, allowing the public partner to require corrective action by the private party in certain circumstances in which the private party has not performed its obligations under the contract.
3. *Termination processes*, allowing a party to bring the contract to an end prior its planned expiration in certain circumstances.
4. *Force majeure processes*, under which the private party can be excused from performing obligations if it becomes impossible to perform those obligations due to certain events outside the control of the parties.

The public partner should develop a contingency plan to assist it in managing these processes should the need occur. While the public partner cannot identify and plan in detail for every possible situation that might arise, the contingency plan should focus on the key requirements and actions necessary to respond to a broad range of different events. Issues to consider in developing a contingency plan include:

1. Events that can trigger the government's step-in, default, and termination rights or a force majeure.
2. The contractual conditions that must be satisfied before the step-in, default, or termination rights can be exercised or if a force majeure exists under the contract.
3. The roles and responsibilities of the public partner's personnel responsible for activating and exercising the relevant rights in the contract. Additional considerations are given to whether these personnel understand their roles and responsibilities, if they have appropriately delegated authority for their roles and responsibilities, and the limits within which the public partner's rights are exercisable.
4. Required resources to implement the contingency plan (access to sufficient skilled personnel to enable it to effectively exercise its rights, measures to mobilize the resources and personnel). For example, if the private party abandons the project site and the public partner steps-in, the public partner may immediately need to hire a security company to secure the site.
5. Required internal authorizations before exercising the public partner's rights.
6. Obligations and liabilities that may be incurred in exercising the public partner's rights, including whether adequate insurance is in place. For example, if the public partner steps in to a road PPP, taking over responsibility for the operation and maintenance of the road because the private party has not been properly performing its maintenance obligations, the public partner may be liable to road users for injuries or accidents caused by the road being inadequately maintained.
7. Information requirements for implementing the contingency plan. These information requirements should be considered when developing the public partner's knowledge and information management strategy, discussed in Appendix 6 of this Manual.
8. Required communication to activate and implement the contingency plan. A proactive communication strategy can prevent the public partner becoming inundated with incoming queries from concerned end users, the public and the media.
9. Ways for the public partner to access any additional funding required to activate the contingency plan.
10. Methods for the public partner to engage advisors at short notice if this is required.
11. Ways the public partner can "step-out," if it needs to step-in, and whether step-out is possible or feasible in this project; if the public partner cannot step-out, whether it can (from both legal and practical perspectives) retender the project.
12. Availability of the contingency plan to the people who need to invoke it.

The public partner should bear in mind that the plan will be activated at short notice in circumstances in which the contract management team may be under significant pressure. Consequently, the plan should be short, clear, easily understandable and easily available. Generally, it is not possible to fully test a contingency plan. However, the public partner should consider "walking through" a range of scenarios as a means of testing the plan's validity.

b. Responding to unexpected events

If a significant unexpected event triggers a contingency plan, it may be necessary for the contract management team to take action without having the opportunity to fully consider the issues identified in the contingency plan. For example, if an event occurs that threatens the health and safety of the public, the public partner (possibly in conjunction with the private party) may need to take action to remove that threat without having an opportunity to fully consider the implications of this action under the PPP contract.

Once the immediate need for action has been met, the contract management team should promptly review the contingency plan to identify the actions that should be taken. The identified actions should be documented in a response plan. The public partner may need to engage advisors at short notice to assist it in identifying the actions to be taken.

If the unexpected event has disrupted the delivery of services by the private party, the public partner should consider the following questions in developing its response plan:

1. How will the private party restore services, consistent with the output specification?
2. What will be the time periods or targets for stabilizing or restoring critical components of the services?
3. During the period of service interruption will replacement services be provided by the public partner or the private party (to the extent that it is able), or will a combination of these solutions be used? For example, if the heating, ventilation, and cooling system in a PPP hospital suffers a critical failure that will take several days to repair, the public partner will need to consider whether patients should remain at the hospital, notwithstanding the fact that the air temperature and quality in the hospital may be outside normal ranges, or whether some or all of the patients should be transferred to alternative hospitals.
4. What resources will be required to restore delivery of each critical component of the services, and how will these resources be mobilized?
5. What temporary service specifications and service level targets should be set for each critical component of the services during the response period, and what relevant stakeholders should be informed that these specifications and targets will apply during the response period? In some cases of temporary operating conditions, acceptable service specifications and service levels may be less stringent than those imposed on the private party in the relevant PPP contract.
6. What information is required to implement the response plan?

Appendix 6. Knowledge and information management and succession planning

Over the life of a PPP contract, a great deal of knowledge will be gained by the public partner's contract management team, and many documents will be produced. To get the best possible outcomes from the project, this knowledge and these documents must be retained and accessible. The objectives of knowledge and information management and succession planning are to:

1. Ensure that information held by the public partner in relation to the project is up to date and accurate and can be easily retrieved when it is required.
2. Ensure that information and documents are submitted and transferred between stakeholders in the appropriate form and at the appropriate time.
3. Ensure that changes in the membership of the contract management team do not result in loss of project knowledge.

a. Knowledge and information management

In establishing its knowledge and information management tools and processes, the public partner should consider the information necessary to manage the PPP contract properly and the appropriate tools for managing contractual information, the extent to which these tools be shared with the private partner, and how the tools and processes should be managed. To effectively manage knowledge and information, the public partner should establish:

1. Appropriate tools and processes (discussed in detail in Appendix 1 of this Manual):
 - a. An electronic document management system for storing electronic documentation related to the project;
 - b. A filing system for hard copy records;
 - c. A system for recording and analyzing data related to the performance of the private partner, and for producing reports as required; and
 - d. A workflow management system that records the tasks the contract management team is responsible for in managing the contract and that automates key processes, such as the receipt and approval of reports from the private party.

The public partner should also develop policies and procedures for using these tools. If the public partner has existing policies and procedures related to managing information, records, and documents, these should be used as a starting point in developing consistent contract management information processes. The policies and procedures should either be included or cross-referred in the Contract Administration Manual.

2. An appropriate culture.

The public partner's contract management team must have a culture that respects adherence to established processes, tools, and systems; otherwise, the mechanisms designed to manage knowledge and information will have limited success.

b. Succession planning

Given the long term of PPP contracts, the membership of the public partner's contract management team is likely to change several times through the project life cycle. New team members will take considerable time to become sufficiently familiar with the project to be effective in their roles. Therefore, the public partner should establish a succession plan for key personnel to manage personnel changes efficiently. For example, it should:

1. Identify who is capable of filling key roles in the contract management team if the current team member becomes unavailable;
2. Aim to limit concurrent departures from the team;
3. Ensure that the retained team has a good mix of new and old members; and
4. Ensure that its Contract Administration Manual and knowledge and information management systems support succession planning by enabling new team members to quickly become competent in their roles.

The succession plan must be sufficiently flexible to allow for:

1. The possibility that contract management team members choose to leave their positions prematurely or are absent on leave for significant periods of time;
2. The need for incoming personnel to complete any appropriate training;
3. The possible need to replace unsuitable staff;
4. The likelihood that roles and workloads will change over the term of the PPP contract.

Appendix 7. Dispute Resolution

PPPs are large and complex projects in which differences may emerge between the parties and become disputes. The objectives of dispute resolution are to:

1. Identify genuine disputes and not assume a dispute exists whenever an issue arises in the project.
2. Resolve disputes efficiently and effectively using an appropriate dispute resolution process.
3. Enable the project to continue while disputes are being resolved.

By adopting good practices in managing and resolving disputes, the public partner ensures that the relationship between the parties is preserved and the risk that disputes can cause additional unnecessary damage to the project is minimized.

a. Understanding what is and is not a dispute

A range of issues are likely to arise over the life of a PPP contract. Some issues can significantly affect one or both parties. For example, the private party may be significantly delayed in completing construction, the public partner may fail to make land available when it is required, or the design of the infrastructure may prove to be inefficient for users. These issues can cause tension between the public partner and the private party.

Public partners and private parties who are unfamiliar with the long-term relationship perspective in PPPs can sometimes assume that any significant issue between the parties is, by its nature, a dispute. This can lead to an adversarial mindset in which the parties no longer focus on long-term outcomes that are beneficial to both parties. This results in poor value for money outcomes.

A dispute only exists where there is a difference of opinion or position between the parties as to what one of the parties is obliged to do or entitled to do under the contract. This can be in the form of a dispute on a question of law (for example, what is the legal meaning of a clause of the contract?) or a dispute on a question of fact (for example, what has occurred or who has caused a particular event, and what are the consequences under the contract?). Most issues that arise in a PPP do not, in fact, involve any dispute and should be managed within the framework of the PPP contract. For example:

1. If the private party is significantly delayed in completing construction, there are processes for dealing with this in the PPP contract (see the asks performed during construction phase in Chapter 1 of this Manual). No dispute exists, necessarily, although a dispute may arise if the parties have different opinions as to the cause of the delay and the different causes have different consequences under the contract.
2. If the public partner fails to make land available when it is required, it should also be dealt with through processes within the PPP contract. The contract may require the public partner to compensate the private party. Again, no dispute exists at this point, although a dispute may arise if the parties have different opinions as to the amount of compensation payable under the contract.

3. If the infrastructure design proves to be inefficient for users, the public partner must determine whether this is because the private party has failed to meet the output specification or because the private party has met the output specification but the specification does not provide a good design outcome for users. In the former case, the public partner should use the contractual mechanisms to require the private party to meet the output specification. In the latter case, the public partner has received what it asked for in the contract but must now consider whether a modification is justified to deliver a better outcome for users.

In each case, the issue may naturally cause tension between the parties, but they are not necessarily in dispute, and they should continue to work cooperatively within the framework of the PPP contract. In most cases, no dispute will occur, even though the issue may be challenging for the parties to deal with.

Public partners should therefore analyze issues that arise during the life of a PPP contract and identify whether those issues can be managed within the contractual framework. The public partner should not assume that a dispute exists until it has established that there is a difference of opinion or positions in respect of a question of law or of fact.

b. Good practice in dispute resolution

In a well-planned and well-managed PPP, disputes between the parties should be infrequent. Effective relationship management (see Appendix 4 of this Manual) and careful monitoring and response to noncompliances and defaults by the private party (see tasks performed during the construction and operations phases (Chapters 1 and 2, respectively) in this Manual) are key to addressing issues before they develop into disputes. Should any dispute arise, the public partner should:

1. *Deal with the dispute as early as possible and at the appropriate level within the private partner, so that the dispute can be resolved quickly and effectively.* Care is needed to ensure that issues are resolved at the correct level. The solution should be critically considered by someone who has an understanding not only of the immediate context of the dispute but also of the broader possible consequences of the solution adopted.
2. *Engage in dialogue with the private party to share perspectives on the issue and determine whether a difference of opinion or position exists between the parties that can only be resolved through dispute resolution.* In many cases, a detailed investigation of an issue and sharing information between the parties can resolve their differences and identify an appropriate resolution.
3. *If a dispute does in fact exist, promptly deal with it through an appropriate dispute resolution process.* The parties should not allow disputes to unnecessarily drag on unresolved, as this will further damage the relationship.

A variety of dispute resolution processes exist, ranging from negotiation between the parties; through alternative dispute resolution mechanisms such as mediation, conciliation, and seeking an opinion from an expert or a dispute board; to formal processes such as arbitration and litigation. PPP contracts typically specify which of these processes are to be used to resolve disputes between the parties. In some cases,

the public partner, either alone or jointly with the private party, may be able to select the dispute resolution mechanism from one or more options. The best option to choose will depend upon the nature of the dispute. The matters described below should be considered in choosing the dispute resolution mechanism. If the contract does not provide a dispute resolution mechanism, the parties may be able to agree ad hoc on a mechanism; however, this might not be the case if the parties see different dispute resolution mechanisms as being more favorable to their position.

Mediation of PPP disputes

Mediation requires both sides to agree to appoint a qualified official, independent of either of the two parties, who is knowledgeable about PPPs in general and about the given infrastructure sector in particular. In practice such mediators often have legal backgrounds as lawyers or even former judges. It is common that both sides will request that the mediator be independent of all national and political pressures, and therefore not be a national of the host country government nor of the home country of the lead private service provider or its investors. The mediator hears both sides' testimonies and then issues a recommended solution. However, the defining characteristic of mediation is that neither side is legally bound to accept the mediator's finding.

Typically, the mediator will spend a reasonable amount of time (usually a day or less) hearing the summarized versions of the dispute from each side and will then issue a recommendation. The recommendation may come out in favor of one party or the other, or it may suggest sharing the costs of the remedy or the risk event in question. The key to the success of mediation of a PPP is that it should be done quickly and without significant expense for either party. Moreover, the recommendation of a qualified mediator should be seen by both sides as being close to what any binding arbitration or litigated outcome in a court would decide. Thus, for mediation to be successful, both sides should believe that they can either accept the recommendation of a qualified mediator, which can be issued within a period of weeks and for relatively low cost, or they can spend many months (or often years) and significant financial resources in legal fees and court costs to arrive to the same decision, but now a binding one. If one or both sides decide not to accept the mediator's recommendation, the next form of dispute resolution may be attempted: binding arbitration.

Binding arbitration

Under binding arbitration procedures, both sides agree to appoint a single arbitrator or a panel of arbitrators to hear their case. Such arbitrators and their organizations should be agreed to and stipulated within the PPP contract itself. For example, during the past ten years the World Bank's International Center for the Settlement of Investment Disputes (ICSID) has become very experienced in hearing and resolving the unique disputes of PPP contracts in nearly all infrastructure sectors and subsectors.

Unlike mediation, where both parties agree that they are free to ignore the recommended solution of the mediator, arbitration is usually classified as "binding," meaning that both parties commit in advance that they will accept and abide by the decision of the arbitrator. In this sense, arbitration resembles an official court of law. However, for PPPs, arbitration has the advantage that it can still be significantly quicker and

cheaper than going through official litigation procedures required by courts. Arbitration panels can be set up in a matter of a few weeks or months. Additionally, arbitrators may be selected who already understand the technical, operational, and even contractual issues of sectors such as roadways, solid waste facilities, airports, water plants, etc., unlike most civil court justices. Additionally, worldwide most civil court systems are overwhelmed by the volume of cases already before them and the mounting number of requests for new civil cases to be heard.

Litigation

Participants in a PPP dispute may also try find resolution through formal litigation in courts of law. However, this tends to take the longest time of any method for resolving a dispute and may impose significant expenses on all parties, including the “winner.” For PPPs that involve foreign investors and lenders, the dispute resolution mechanisms of the PPP contract almost always require that the law of a third country or other applicable law be relied on in litigating any disputes.

Contract termination

The final option for ending a PPP dispute is to seek termination of the PPP contract. All PPP contracts should specify in detail the procedures for contract termination. Contract termination must be formally sought or requested by one of the parties. PPP contract termination should have very detailed procedures for how all the accumulated costs of the project, including past investments, outstanding project-backed loans, and current inventories of assets will be allocated and recovered. Generally, in larger PPPs with project-backed financings, lenders require that if the government seeks termination for any reason other than nonperformance, it must pay the full amount of the lenders’ outstanding loans plus additional fees (covering their “loan prepayment risks”). In addition, project-backed lenders generally insist on asserting their own “step-in rights” for PPPs. This means that if an SPV’s private service provider’s operating contractor fails to perform, rather than terminate the contract, the lenders may first step in and take over the project and appoint their own new management team and operating contractor to successfully operate the project and thereby pay off all outstanding project loans.

PPP contract terminations are expensive for all sides involved, which is why they are relatively rare in large, capital-intensive PPPs. Almost all sides find it more cost-effective to try to restructure and renegotiate these deals and to share the costs of revising these contracts rather than cancel a PPP contract.

Dispute management strategy

If the private party initiates the dispute resolution process, or the public partner is considering doing so, the public partner should assess the potential costs, risks, and benefits of the dispute resolution process specified in the contract and develop a dispute management strategy that, to the extent possible, protects value for money. In developing its dispute management strategy, the public partner should consider the following:

1. *The likely cost of the dispute resolution process*, both the costs paid to the decision maker (for example, court fees in the case of litigation or the arbitrator's fees in the case of arbitration) and the public partner's likely costs for legal advice, technical advice, and management time in relation to the dispute. The public partner should ensure that it has a sufficient budget to manage the dispute and should weigh up the costs and benefits of proceeding with the dispute, compared to other options such as settling with the private party without a formal dispute resolution process (such a settlement may amount to renegotiation; see Appendix 2 on change management in this Manual).
2. *Existence of clear rules for the process and their appropriateness for the nature of the dispute*. The public partner should have a clear understanding of the process by which the dispute resolution mechanism will reach a conclusion. The process should be free from significant opportunities for delaying tactics and other behavior by which one party seeks an unmerited advantage. The public partner should be prepared for the possibility that the private party will use such opportunities if they exist.
3. *The decision maker's skills and knowledge are suited to understanding the dispute*. Often disputes are decided by people with legal training (judges in the case of litigation, experienced lawyers in the case of many arbitrations). If a dispute relates to a question of law, such as the correct legal interpretation of a clause in the PPP contract, a person with legal training is likely to be well suited to resolving the dispute. However, if the dispute concerns a technical question of fact, such as whether the condition of a road meets the output specification, a legally trained decision maker may not understand the complexities of the issue and (even after hearing from expert witnesses) may have difficulty reaching an appropriate decision.

In some projects, a dispute resolution board or expert panel is created at the outset of the contract. The members of the board or panel are regularly updated on the progress of the project. As a result, this body develops a strong understanding of the project and is typically available at short notice to quickly resolve disputes.

The public partner's dispute management strategy should take into account the skills and knowledge of the decision maker and present the public partner's case in an appropriate way to ensure it is understood by the decision maker.

4. *Length of time to get an outcome*. Different dispute resolution mechanisms will take different lengths of time to produce an outcome. It is generally the case that the longer it takes to reach an outcome from a dispute, the greater the damage to the relationship and the greater the negative impact on project outcomes. Public partners should prefer dispute resolution mechanisms that promptly resolve disputes. If the process will take a long time to reach an outcome, the public partner will need to prepare for this. For example, it may need a communications plan to keep key stakeholders informed of the process.
5. *The binding outcome on the parties*. Many dispute resolution mechanisms, such as litigation and arbitration, are binding on the parties. This means that the outcome of the dispute determines the parties' legal rights and obligations. Other dispute resolution mechanisms are nonbinding. For example, the findings of a dispute resolution board are usually nonbinding. This means that the parties are under no obligation to comply with those findings.

A key advantage of a nonbinding outcome is that it gives the parties scope to agree on a somewhat different outcome after receiving the findings. This can be beneficial if the parties still have a relationship in which a degree of cooperation is possible. They may agree to adopt the majority of the findings subject to some changes thus providing a better outcome for both parties over the remaining life of the PPP contract.

The disadvantage of a nonbinding outcome is that there is no certainty that the dispute resolution process will resolve the dispute, particularly if the relationship between the parties is poor.

The public partner's dispute management strategy should take into account whether the outcome is binding and, if not, plan for the possibility that the initial dispute resolution process may not resolve the dispute unless a further step (such as litigation or arbitration) occurs.

6. *Possibility of enforcing the outcome.* Even if the outcome of a dispute resolution mechanism is binding, there remains a question as to whether the outcome can be enforced. For example, if the outcome of the dispute resolution is that the private party must pay the public partner a sum of money, what enforcement process ensures the public partner can obtain that payment if the private party refuses to pay?

The public partner's dispute management strategy should take into account whether the outcome can be enforced and, if not, plan for the possibility that any binding outcome will nevertheless be of little value.

7. *Rights of the parties to appeal the outcome.* In some dispute resolution processes, the parties only have limited rights to appeal the decision, even if they think the decision was incorrect. If this is the case, the public partner's dispute management strategy should take into account the possibility that the outcome may be incorrect but that an appeal will not be possible.
8. *The dispute resolution mechanism provides an outcome in the interests of both parties.* Some dispute resolution mechanisms, such as litigation and arbitration, focus on the legal rights and obligations of the parties and cannot focus on alternative outcomes, even if an alternative outcome is in the interests of both parties. Other dispute resolution mechanisms, such as dispute boards, can look beyond the parties' legal rights and obligations and make recommendations that are in the interests of both parties or that are "best for project" solutions.

For example, if there is a dispute as to whether the private party has complied with a particular requirement in the output specification, a dispute board might agree that the private party has not complied, but it might also find that the particular requirement in dispute has no impact on the project outcomes and that it is not practical for the private party to comply; hence the parties should continue the project as if that requirement did not exist.

In these circumstances, the public partner's dispute management strategy should examine what the best outcome for both parties might be under the dispute resolution mechanism.

9. *Disclosure practice in conducting the dispute resolution process.* Litigation is typically a public process, with the proceedings open to scrutiny by the community and the media. This provides transparency; however, in a PPP project, the parties may want to resolve a dispute without any unnecessary controversy. The parties can often better protect their reputations and preserve their relationship by conducting a private dispute resolution process, such as arbitration.

If the parties choose a private dispute resolution process, the public partner can consider disclosing details of the final outcome (in addition to any public release of the decision by the decision maker, such as publication of an arbitral award), provided the disclosure does not breach any confidentiality undertaking to another party. This provides an added level of transparency.

The public partner's dispute management strategy should take into account whether the dispute resolution process is a public or private. If it is a public process, the public partner should be prepared for potential media exposure and public debate and should develop an appropriate public communications strategy.

c. Continuing the project while a dispute is being resolved

Even though a dispute exists it does not mean that the parties are freed from the contract and should not proceed with the project as planned. The parties should continue to meet their contractual obligations during the dispute resolution process, without prejudice to their subsequent compensation following the final decision regarding the dispute. Continuing the project while a dispute is being resolved can be challenging, as individuals on each side of the contract may have been involved in the events giving rise to the dispute. To the extent possible, the public partner should separate management of the dispute from other contract management activities. The public partner should consider:

1. Ensuring that any meetings and other interaction with the private party in relation to the dispute are distinct from the normal contract management meetings and other interactions between the parties;
2. Appointing to the contract management team a new member with appropriate skills to be responsible for managing the dispute, allowing the other members of the contract management team to continue their normal roles;
3. Reassigning individual contract management team members whose actions were a major factor in the dispute if their continuing involvement in the project may cause further conflict. These team members can be moved to roles in which they do not interact with the private party.