NCSL Foundation Partnership
Public-Private Partnerships (P3s or PPPs) for Transportation

Transportation PPP Partners Project Educational Session

Hosted at the NCSL Fall Forum

December 11, 2009

San Diego, CA

Meeting Summary

Compiled by NCSL
February 10, 2010

Executive Summary

The NCSL Foundation Partners Project on Public-Private Partnerships (P3s/PPPs) exists to link legislators, legislative staff and interested private entities to analyze legislators' needs and to develop nonpartisan, balanced, useful materials to aid legislators' decision-making regarding PPPs in transportation, both in their respective states and as they consider state-federal relationships.

One purpose of this 18-month Project is to develop and offer educational sessions. This session at NCSL's Fall Forum in San Diego built on previous meetings of the working group in April and July. The information gathered in these meetings will inform the group in its ongoing analysis, with the end goal of developing a "toolkit" of useful resources for legislators considering transportation PPPs.

The session began with opening remarks from the project co-chairs, *Representative Terri Austin of Indiana* and *Representative Linda Harper-Brown of Texas*. This was followed by an in-depth presentation on the **UK PPP Program: Policy Background and Implementation** by *Edward Farquharson (Project Director, Partnerships UK)*, in which he described the institutional arrangements, projects and lessons learned of the established PPP program in the United Kingdom. The session ended with a business meeting, including a review of the draft "toolkit" report and the tentative scheduling of the next two Partners Project events: a joint summit with the United Kingdom Trade and Investment Office of the British Consulate General (March 2010) and a Partners Project meeting at the NCSL Spring Forum (April 2010).

NCSL thanks all of the public and private sector participants in the Partnership Project for their contributions to this event and to the ongoing work of the Project.

Contents

More information about this meeting, including PowerPoints, is at http://www.ncsl.org/?tabid=19354

More information about the NCSL Foundation Partnership for PPPs for Transportation is at http://www.ncsl.org/?tabid=17528

Information about previous meetings, including PowerPoints, is at http://www.ncsl.org/?tabid=17216 and http://www.ncsl.org/?tabid=18016

[1] As of December 9, 2009, Partnerships UK was merged into Infrastructure UK, a new body of HM Treasury.

Opening Remarks, Introductions and Review of Past Work

Speakers
- Representative Terri Austin, Indiana (*Project Co-chair*)
- Representative Linda Harper-Brown, Texas (*Project Co-chair*)

Opening Remarks by Representative Terri Austin, Indiana

In her opening remarks, Representative Austin welcomed everyone to this educational session and introduced herself as one of the co-chairs of the NCSL Transportation PPP Partners Working Group. She reviewed the session agenda, including the review of the draft "toolkit" report.

Representative Austin described how NCSL formed this working group of state legislators, legislative staff and representatives of private sector entities to assemble reliable information and to identify effective tools for considering PPPs (or not). This group has worked for 18 months, analyzing legislators' needs and hearing a variety of invited experts. It has developed nonpartisan, balanced and absorbable materials to aid the legislative process both in their respective states and in considering state-federal relationships. Representative Austin thanked everyone who has been involved in this endeavor for their time and expertise.

Representative Austin also thanked the sponsors of the NCSL Transportation PPP Partners Working Group: The NCSL Foundation for State Legislatures, AAA, the American Federation of State, County and Municipal Employees (AFSCME), the American Road and Transportation Builders Association (ARTBA), the American Trucking Associations (ATA), the Americans for Transportation Mobility Coalition (U.S. Chamber of Commerce), Macquarie Capital, The Reason Foundation and Transurban.

Opening Remarks by Representative Linda Harper-Brown, Texas

Representative Harper-Brown welcomed everyone to today's session. She stated that the "toolkit" report will be helpful to legislators in Texas; the Partners Project meetings certainly have been, and she hopes they will be helpful to other states as well. She then facilitated introductions of all of the meeting participants, which included legislators and legislative staff from Guam, Indiana, New Hampshire, New York, Minnesota, Oregon, Pennsylvania, Texas, Washington, NCSL staff, representatives of private sector entities and other interested parties.

UK PPP Program: Policy Background and Implementation[2]

Presentation by Edward Farquharson
Project Director, Partnerships UK[3]

Representative Linda Harper-Brown of Texas welcomed and introduced Edward Farquharson.

Edward Farquharson began his presentation by expressing his thanks for the privilege of being at this meeting and the opportunity to share some of the lessons and mistakes that have been made with PPPs in the United Kingdom. The presentation will address the scope and reach of PPPs in the UK. In response to the NCSL Partners Project draft "toolkit" report, the presentation will also review

[2] NCSL especially thanks Edward Farquharson for his feedback on this presentation summary.
[3] As of December 9, 2009, Partnerships UK was merged into Infrastructure UK, a new body of HM Treasury.

institutional arrangements and processes that have been used in the UK; this is still a work in progress. Finally, the application of PPPs in the transport sector in the UK will be addressed.

PPP Policy Objectives

The first point is that the public sector must be very careful about *why* it would engage in PPPs. We must understand our policy objectives and what we are trying to achieve. In England, the key driver is **value for money**. PPPs are considered a procurement method, and it only makes sense to use the PPP method if it yields improved value-for-money procurement of public services.

PPPs were originally thought of only as a financing tool, but that is not the only benefit. The value-for-money benefit is key. There is also an accounting benefit, in that PPPs give the public sector an opportunity to finance infrastructure for some types of public service without impact on the public balance sheet. This is an issue in the EU, where there are rules about public debt limits. This may be a false profit, however, and may achieve an accounting benefit without actually delivering value for money.

Another policy driver for PPPs that economists like is **contestability in delivery of public services**. This means that, if you can do the same thing in two different ways, you create a competitive process that can drive change. For example, when the private sector got involved with prisons in the UK, we found that we could design and build prisons in a completely new way. Now, whenever prisons are built, we apply some of those principles. So, though only 9 of 160 prisons in the UK are PPPs, the impact has been felt across the whole public service area.

PPPs can also serve as **an antidote to short-termism** in both public and private sectors. It creates a new perspective when the operations and maintenance costs over the life cycle are taken into account. When you enter a long-term PPP arrangement—and many in the UK are availability-based, where the public authority rather than the user is paying a fee for the service—you need to think through the duration of that contract. With a PPP, the long term impacts can't be avoided; it hits you right between the eyes, even before signing the contract.

Other policy drivers for PPPs in England include **reform and modernization** of public services and **improved transparency of costs** of public service delivery.

In the UK, the crucial difference between privatization and PPPs could have been made clearer to the public earlier on. In PPPs, public accountability is retained; if something goes wrong with a PPP, you still complain to the government.

The UK PPP Program

The UK's PPP policy—known as the Private Finance Initiative (PFI)—was officially launched in 1992 by a conservative administration, but it only really took off when the Labor Party came to power in 1996-1997. The Labor Party came to power with a large social infrastructure investment agenda, especially in schools and hospitals. While Labor was in opposition, they were not particularly in favor of PPPs (it sounded too much like privatization), but once they got into power, they saw that this was one method for delivering social infrastructure more quickly and effectively. PPPs have stayed active since then and are now considered stable investment vehicles for financial institutions. (Perhaps we got too enthusiastic in 2003, when the capital value of projects that year exceeded £16 billion; one lesson learned there was that there is a size of project under which PPPs don't work well.)

Transportation projects are still the largest sector by value of the net capital investment, but smaller than education and health by number of projects, because transportation projects are big and use a great deal of capital. For example, this category includes the huge London Underground project.

Many of these projects use an availability payment model. This is an important distinction: We are contracting for a service, not for an asset. The asset provides the service. It is important to make the public understand that we are contracting for outputs, not inputs—the resulting service, not the thickness of concrete and so on. And outputs are only part way to what we really want, which is *outcomes*. We are getting better at defining outcomes in PPP contracts and at distinguishing between the public sector as a commissioner of services and the private sector (or even third sector or at times other public bodies) as a provider of services.

National Audit Office Review

The UK National Audit Office (NAO)—equivalent to the U.S. Government Accountability Office (GAO)—reported to the House of Lords on the PPP experience earlier this year. The NAO conducts performance audits of PPP projects. The NAO's responsibility is to report to Parliament and represent the taxpayers' interests to Parliament. This is important because it provides a feedback loop, by conducting a disinterested but expert analysis of PPPs—compared to the many interested parties who assess PPPs to prove a point. (*Source: National Audit Office, Private Finance Projects: A Paper for the Lords Economic Affairs Committee, 2009.*)

The NAO has shown that **PPPs can deliver benefits but are not appropriate for every project**. Also, while PPPs **generally are providing what they promised**—including real risk transfer—they will not provide much *more* than what was promised. However, risk transfer only really exists if the public sector can stand up to the private sector when something goes wrong.

The NAO also found that it is **important to establish the benefits of PPPs** to justify the higher financing cost. Any value for money analysis is based on assumptions, and needs to balance qualitative with quantitative analysis using a common-sense approach. Also, **competitive tension** is an important value for money driver with PPPs, though note that the *quality* of competition is as important as the number involved. You don't necessarily want lots and lots of companies competing, especially at the closing stages of the tender process; you want high-quality companies competing.

Other findings of the NAO included that **institutional incentives may drive use of PPPs**, **PPP evaluation tools need more development** and **PPPs require very careful management**. On this last point: There is often an obsession with "doing the deal," but this is only the beginning; then there is the rest of the project's life during which the public service is actually delivered. Gearing up for long-term contract management—and building the necessary resources and skills—is often overlooked by the public sector.

PPP Activity in the European Union

PPPs have been an active area of investment across the European Union (EU), even during the financial crisis. There were 385 deals between 2007 and 2009, with 442 more, currently in the pre-approval stage, and 486 in tender. From 2007 to 2009, the UK was the top country in the EU for PPPs by number of closed deals (178) and by value (more than €18 billion). Portugal has a high value of PPPs but relatively few projects, because they have focused largely on high-value transportation projects. (*Source: DLA Piper, European PPP Report, 2009.)*

PPP challenges in the EU include: **liquidity shortages and recognition of illiquidity risk** and c**hallenges to existing risk allocation models.** Trends include m**ore availability-based, social infrastructure projects** and the **development of common approaches to common problems** (for example, through the European PPP Expertise Centre, or EPEC, which exists as a source of information for public sector PPP units). Another trend to consider is the **role of the European Investment Bank** (**EIB**), which has been an important source of long-term finance and therefore stability in the market. During the financial crisis, their rates didn't change that much, which begs the question as to whether there is an important role to be played in *any* market by a public source of finance. In response to the credit crisis, the UK also established a long-term financing facility within HM Treasury to lend alongside the banks on identical terms to provide an additional source of confidence to the market. It has only had to lend to one project so far, so it appears to have created the confidence for those banks willing to lend during the credit crunch that projects will close.

Institutional Issues: The Case for a Central PPP Unit

There is a strong case to be made for a central, public sector PPP unit. First, there are **common issues across projects**; about 80 percent of contractual terms in PFI-type PPPs in the UK are common across sectors, and having a central unit helps avoid a "silo" problem. A central unit also provides **institutional memory** and helps address the **asymmetry of private and public sector PPP skills**. PPPs are complex, and PPP skills are scarce and expensive. The goal is to make the public sector an "intelligent client"—not just in entering into PPPs, but in how they go about appointing and managing good legal, financial and other transaction advisors. The public sector needs to have sensible budgets for transaction costs, or else PPPs will cost a lot more in the long term, as the public sector enters into undesirable deals.

The roles of a central unit, as demonstrated by Partnerships UK, are:

- **Policeman/scorekeeper**, to approve any departures from a standard contract and ensure consistency of risk allocation across the program and, in the case of Treasury-based units, to record any long-term liabilities;
- **Friend/counsel**, to hold the hand of the project team (often as a member of the Project Board), troubleshoot and follow closely the advice that legal, financial or other advisors are giving;
- **Analyst/strategist**, to review and help to develop policy, and take the programmatic rather than project view.

Other roles of the public sector are to **shape the market** (for example, by bringing new suppliers into the market) and to **develop methodologies** such as Value for Money analyses.

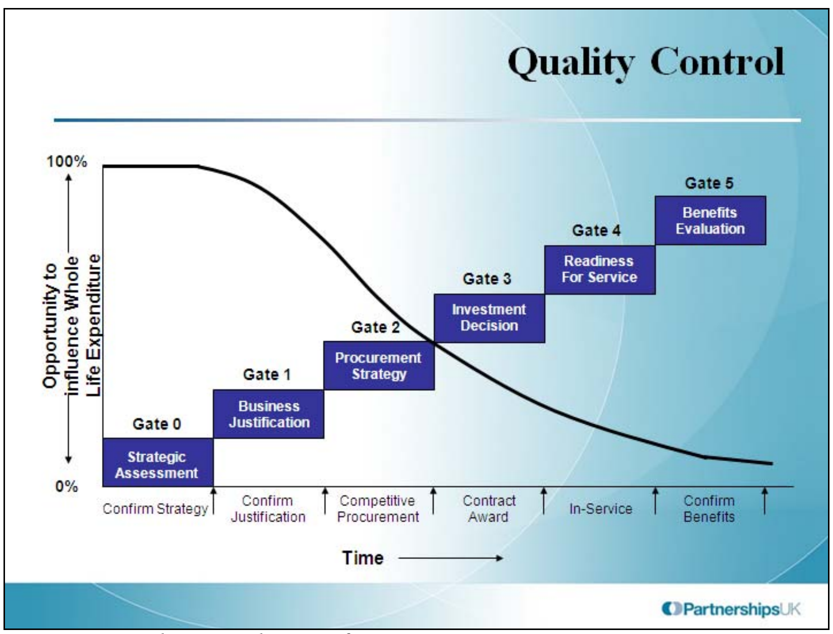
A PPP unit requires a range of expertise and a blend of public and private cultures. If it was all ex-investment bankers, a unit might not be able to communicate so well to its public sector clients. Partnerships UK employs approximately 70 mid- to late-career level specialists in procurement, project management, law/contracts, finance, public accounting, commercialization of public assets and sector-specific expertise. These specialists are drawn from the private, public and third sectors, and while they are not acting as transaction advisers, they know how to manage them.

UK Public Sector PPP Institutions

UK public sector PPP institutions have included HM Treasury (to develop policy), Partnerships UK (for implementation), Local Partnerships (which brings together central and local government, supporting local government PPPs), Local Government Association (similar to NCSL), devolved government PPP policy units, Partnerships for Schools (to deliver the sector-specific schools program), sector department private finance units and auditing bodies such as the National Audit Office. Local Partnerships and the Local Government Association are important because many decisions are made locally, not centrally. As of noon yesterday, it was announced that the PPP delivery expertise of Partnerships UK would be folded into a new HM Treasury body to be called Infrastructure UK. This would bring together the policy team and the infrastructure finance unit in Treasury and enable a more holistic and longer term approach to be taken to infrastructure policy and delivery. It would also have a wider role in looking at further key economic, as well as social, infrastructure investment needs such as energy and high speed rail and examine further ways to mobilize long term institutional sources of finance.

Delivery Processes

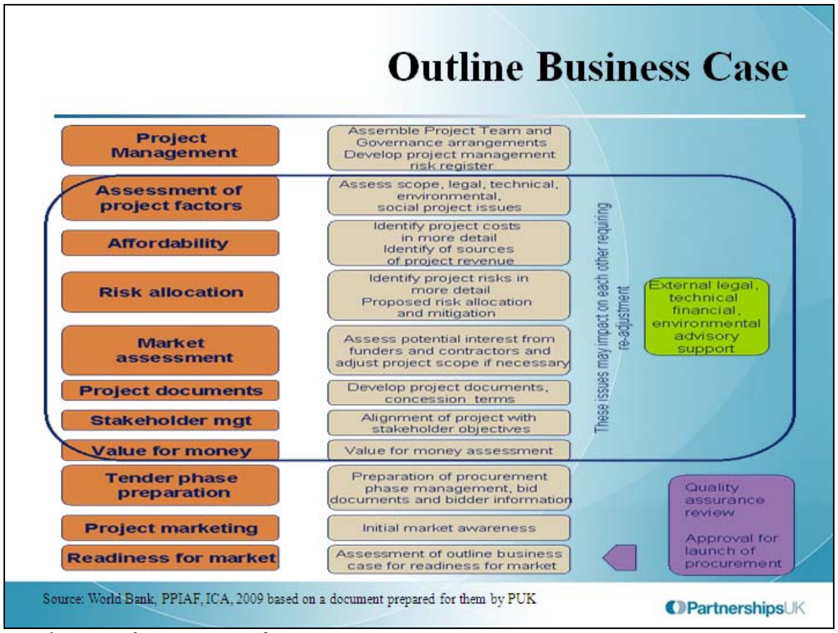
The UK has implemented quality control "checkpoints" for *all* procurement. The "gateway" quality control process—wherein certain conditions must be met at each "gate" for the process to move forward—is one we now swear by.



"Gateway" quality control process for PPP procurement.

For PPPs, the two most important "gates" are: 1) Before you launch the project on the market: are all of your ducks in a row? Otherwise, if you have to go back and do something else, it discourages the market and loses credibility for the public sector, and 2) before signing the contract. After all, as you move through PPP process, it gets increasingly expensive to change your mind, so it makes sense to check you have taken the right actions at the right time.

The business case must be carefully outlined, the requirements clear and the contract fairly well developed, before taking a project to the market and entering into the competitive procurement phase. The project must be *deliverable.* If Partnerships UK is not satisfied with a business case for a given project (in its role of reviewing projects for the Project Review Group and therefore the allocation of central government funding support for the availability payments), the project goes back to be further developed rather than going to market.



Outlining a business case for a PPP project.

Project Governance

A **Project Board** (including the project owner and key stakeholders) is usually created to oversee development of the project and the **Project Management Group** (including the project team director and functional heads in the project), led by a project director, carries the project through on a day-to-day basis, with the assistance of legal, financial, technical and environmental advisors. One mistake the UK made early on was to think that carrying the project through could just be an addition to the project director's other day job. In reality, carrying the project through is a full-time job and requires time and expertise. Getting the initial government process going right takes you about 80 percent of the way.

Value for Money Assessment[4]

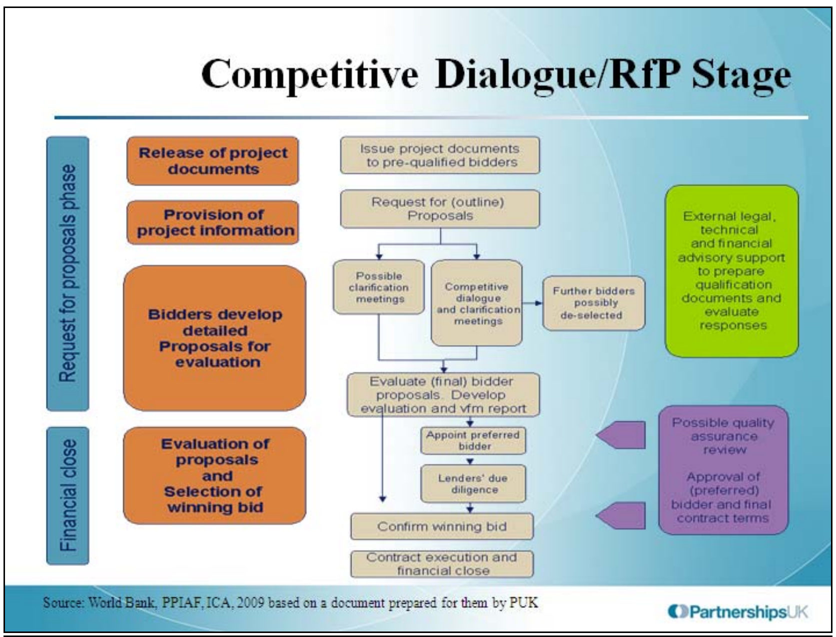
In the UK, a Value for Money (VfM) assessment takes a **three-stage approach** (program, project and procurement level), embeds an **evidence-based approach** and **balances qualitative and quantitative assessment**. On this last point: There is much leeway to manipulate the numbers for a public sector comparator, because it is based on assumptions. The UK has decided to use a more consistent and simplified approach, where you feed in numbers to a standard and less manipulable analytical tool to provide an approximate but more consistently derived quantitative comparator. This generic analysis is balanced by the qualitative assessment, which looks at a project's **viability** (outputs, scope, flexibility, equity, efficiency, accountability), **desirability** (cost/benefit) and **achievability** (market interest, competition, time scales). Viability cannot be at the expense of labor conditions, and a project may be undesirable if it is so complicated that it will cost a great deal to implement (e.g., small deals).

[4] The UK guidance on VfM assessment is available at http://www.hm-treasury.gov.uk/ppp_vfm_index.htm

Deliverability, overall, must be looked at. Essentially this is the checklist to determine whether the project is ready for tendering and includes: clarity of requirements and scope; appropriate risk allocation; indication of commercial interest; project information and contract terms prepared; affordability; expected accounting treatment determined; project team/processes in place; suitability of proposed advisers; indicative timetable; value for money properly assessed; commitment of stakeholders/users; approvals/appropriate powers confirmed, and; commitment of sponsors/users.

Competitive Dialogue and Request for Proposals Stage

The **competitive dialogue process** is meant to create a real dialogue under competitive conditions. The goal is to get to a point where you have reasonable comparability among bidders. They understand what you want, and you understand and are confident of their ability to deliver the project.



The competitive dialogue and request for proposal stage of PPP procurement.

Regarding bid evaluation, around the world, many procurement rules don't allow any form of dialogue after pre-qualification and, when evaluating the bids, anything except single parameter bidding, where decisions are made solely on cost. The challenge in this alternative, competitive dialogue approach and the use of multiple technical and cost evaluation criteria, is that it may inject an element of subjectivity. For more complex projects however it will usually lead to a better long term decision.

Robust processes can be used: the process by which the bids are evaluated generally involves creating different teams that look at each aspect of the bid (technical, etc.) and a well documented and auditable decision making trail Each team looking at different aspects of the bid is not, for example, allowed to know about the price.

It is a requirement under European Union procurement law that you set out at the beginning what the evaluation process will be. However, there is some debate about how much information about evaluation criteria you share. If you share too much, you might get "gaming" and bidders crafting proposals just to meet those criteria. In general, broad criteria will be published, but there is no consensus on this.

Lessons Learned about the PPP Process

Lessons learned include:

- **Communicate strong central sponsorship and stable long term policy commitments** if changes are to be made across markets.
- Have a view about **what you want the market to look like** in 5 – 10 years' time.
- **You generally get one shot at crafting the overall policy**. It is difficult to change things later.
- **Have a mix of both mandatory procedures and support.** There is no point in having hard rules unless there are support mechanisms to go with it for procuring authorities.
- **Standardize the contracts, but not too soon.** In the UK, standardized contracts came too late, because we thought something wonderful would come out of all of these different approaches. But don't create a standardized document too soon, before it has been market-tested (the UK is on the fourth iteration of its standardized PFI contract). A standardized contract doesn't mean one where none of the drafting can be changed (though some countries use such an approach). The UK uses an "exegetic document," expressing "we strongly believe that risk allocation in this area should be like this," and "this is the language required" in some areas, while in other areas it raises an issue but leaves flexibility for the procuring agency.
- **Use independent assessment and a pass/fail control point—**a "kite mark" to reassure the bidder market.
- **Engage in a rigorous use of the business case**, which allows you to do various adjustments (not a strictly linear process).
- **Project governance** is key.
- **Scrutinize the deliverability** of a project before real engagement with the market.
- **Scrutiny can prevent bad projects going to market**, but cannot create good ones.
- There is a need for a **skilled, properly resourced project delivery workforce**.
- Program delivery platforms are very useful where you have **large numbers of similar projects** and therefore where standard processes can be used and the public authority can be specialized and skilled up.
- Pay proper attention early on to preparing for the **operational phase of projects**.

Examples of UK PPP Projects in the Transportation Sector

UK PPP projects in the transportation sector have included **design-build-finance-operate** (DBFO) **roads** (one toll road, shadow tolls, availability payments and hybrid models); **DBFO street lighting** (a relatively simple sector on which to use a PPP, in which performance is easily measured using a light meter); **DBFO road maintenance**; **DBFO light rail**; **the London Underground**. Other examples of different forms of successful transport PPPs include the **Channel Tunnel Rail Link** (a high speed rail project); **London Luton Airport**; **Highways Traffic Control**; and the **Oyster Card** payment and ticketing system for the London Underground.

Lessons Learned about PPPs in the Transportation Sector

- A variety of PPP structures are available. Key themes include:
    - Robust risk allocation
    - Increased certainty of delivery and performance
    - An interest in the project's entire lifecycle, including operations and maintenance, drives good behaviors.
- Milestone payments can be used but may limit public sector remedies later on.
- Availability payments can assure long term performance but they have a cost.
- Transferring user/revenue risk can be problematic and may be inefficient,
- A key lesson is that *hybrid* arrangements combining say availability payments with some limited demand risk transfer can produce the most efficient and stable combinations: the Nottingham Tram project is a good example.

Representative Terri Austin thanked Edward Farquharson for his excellent, in-depth presentation and commented that the group will look at incorporating this into the "toolkit" report. She remarked that this information helps us realize that the U.S. is very much in its infancy with PPPs.

PPP Partners Working Group Business Meeting

The Working Group ended the session with a business meeting. Jim Reed facilitated the tentative scheduling of the next two Partners Project events: a joint summit with the United Kingdom Trade and Investment Office of the British Consulate General (March 2010) and a Partners Project meeting at the NCSL Spring Forum (April 2010).

For the remainder of the business meeting, the group offered detailed comments on the draft "toolkit" report, currently titled *Public-Private Partnerships for Transportation: A State Legislators' Toolkit.* Jim Reed of NCSL offered the group the opportunity to submit written comments on this draft by January 31, 2010. The comments will be incorporated into the next draft by NCSL staff, for review by the group at the NCSL Spring Forum in April. The final document will be released at the NCSL Legislative Summit in Louisville, KY, in July 2010.

Representative Terri Austin, Representative Linda Harper-Brown and Jim Reed of NCSL thanked all attendees for their participation.

Appendix A
Presenter Biography

Edward (Ed) Farquharson is the project director of Partnerships UK. Partnerships UK (PUK) was established in 2000 by Her Majesty's Treasury to support the public sector in pioneering and delivering PPPs.[5] Edward leads PUK's international work advising overseas governments on the establishment and implementation of their PPP policies and programs and is currently engaged on assignments in North America, Asia, Europe and Latin America. He has a background of over 25 years in debt and private equity finance in infrastructure businesses around the world including ten years with CDC Capital Partners (both London based and, before that, Southern Africa) where he led the infrastructure team responsible for developing an equity and debt portfolio of road, rail, airport and port projects. Prior to CDC, Edward was involved in developing limited recourse project financings at Morgan Grenfell, a leading UK investment bank, including the Dartford Crossing project for London's orbital motorway over the River Thames (the first UK PPP). Edward has an MBA from Manchester Business School and is an alumnus of London Business School and INSEAD, a graduate business school based in Fontainebleau, near Paris. He has a degree in Philosophy, Politics and Economics from Oxford University.

Appendix B
Question and Answer Session with Edward Farquharson

Question: How much is the Crown involved with local projects?

Edward Farquharson: Projects are owned by their procuring authority; however, they will usually depend on a central government source of funding to pay for a proportion of the availability payment (related to the capital element) known as a "PFI credit."

Question: What about making information from unsuccessful bidders public—the issue of proprietary information?

Edward Farquharson: There are processes for dealing with proprietary information. Companies will not present their proposals if they think you're going to share those with other bidders, so there are rules about respecting the confidentiality of each bidder's technical proposal. If you don't do that, you will not get technical proposals, and you will lack sufficient information to select among bidders. Proprietary information is an issue, but it cannot be an excuse for bidders not to provide technical proposals. The public sector needs that information, to know what each bidder's technical solution will be. When bidders are deselected, they are told why, and they have a right to be told why.

Question: How have you managed to avoid bid challenges?

Edward Farquharson: Firstly, procurement rules are set by the European Union. We are not just making them up as we go along.

In earlier stages of PPP development, one way to deal with challenges is to say that there will be a pipeline of projects; this reduces incentive to obfuscate the process, because bidders will be involved again with the next one. There is a self-interest.

[5] As of December 9, 2009, Partnerships UK was merged into Infrastructure UK, a new body of HM Treasury.

More complex process can raise this issue :the competitive dialogue process is quite complex; only three or four countries in the European Union use it. Conversely, one country where bid challenges are endemic—Greece—will not use competitive dialogue at all, but instead uses a very restricted process with very clear, limited and objective criteria for bid evaluation. There, if you ask the Minister of Finance why he is pursuing PPPs, he will say he's found a new procurement tool that is immune to bid challenges. That, to him, is the big win. So there may be some benefit in having a simpler process for nations in earlier stages and where bid challenge is a problem. But there is a possible cost in terms of a lack of sophistication in choosing the right bid for more complex projects as there is no scope for adjustment, so you will need to do your homework and very sure exactly what you want before going out to bid. In the UK, despite using competitive dialogue and multiple evaluation criteria, bid challenges are not common.

Question: What about unsolicited proposals?

Edward Farquharson: In the UK, unsolicited proposals are very uncommon. The first project I ever worked on was an unsolicited proposal to build a river crossing in east London in 1984. The government said, "Great idea! Now we'll have a competition." And we lost. No compensation.

Question: What is the involvement of local governments?

Edward Farquharson: In the UK, our approach has been that whoever has to live with a project for 30 years, should own it. In Victoria, British Columbia, or the UK, the procuring authority, many of which are at local government level, is very much the owner; otherwise, you get into trouble later when this deal isn't what they wanted.

Question: In my state, we have started with requests for information. Then we have chosen the best ideas and taken those to the next stages. We have told bidders that they would be reimbursed for some of their time and expense in putting together proposals on complex projects; in return, the state can use some of that information and bidders will not challenge the bid process.

Edward Farquharson: In the earlier days of the UK PPP program, we may not have been as rigorous about defining the project requirements before we started the competitive process. There was a tendency to leave things for later, which meant that the competitive process took much longer. Now, there is a draft contract out there early on; the bidders are sorted based on a fairly narrow set of requirements. Otherwise, there is a tendency to rely too heavily on the private sector to define what the public sector actually wants. The public sector needs to define early in the process what it wants in terms of outputs; what the private sector must define is *how*. So there is not as wide a range of proposals coming in.

Follow-up question: I may have misrepresented the request for information phase. It does tell them what we want in terms of outputs, and asks them how they would go about it.

Edward Farquharson: We would tend to start to do that in the market sounding process, which is pre-bid and not related to the procurement process at all. That gives us some ideas, and we are not bound by the bid process. We do not generally offer to compensate for the costs. The competitive dialogue process provides further opportunity for bidders to put forward ideas at a more detailed level. Again, it is not common practice to reimburse losing bidders. If you have a well-structured evaluation framework, you can use the competitive process to surface the good ideas.

Question: If we are putting design, build, operation and maintenance together, will that have the effect of eliminating our local contractors?

Edward Farquharson: Over time, contractors who can deliver more of the phases will be more competitive. Unless local contractors develop in that direction—i.e. as bid integrators and service providers, not builders—they will end up being sub-contractors to the companies that are at the front of this development. Lenders will also be a source of pressure as they will only back well capitalized and experienced bidders. Contractors will also be one of the main sources of risk equity, alongside some of equity provided by institutional players. (Although in PFI, 80 to 90 percent of the finance is by way of debt.)

Question: The lead bidder will deal with the debt market?

Edward Farquharson: Yes. In our market, the lead bidder tends to be the contractor, but can vary. We ask for a reasonably strong commitment from the bank when bidders submit their final bids, but we don't ask for committed finance, because there is not the capacity in the market to do that financial due diligence for all of these bidders on all of these different projects and it would increase costs.

Question: You said there are only a limited number of advisors in this business, so the same advisors must be working for both the public and private sectors. How do you deal with separation of duties and loyalties?

Edward Farquharson: Advisors are usually hired on a project-by-project basis. There needs to be a thin layer of expertise in the public sector so we know that the advisors are giving us good answers. We expect that they have worked with both sides, but for any given deal, they are only advising one side. It is actually beneficial to have advisors who know both sides, but it is important to manage them intelligently.