



Japan Local Government Centre, London

Monthly Report May 2010 (Germany) – The Situation of PPP projects in Germany

Since 1992, investment by local government has declined steadily, and this continued well into the new millennium. In 2004, the level of investment in public works and buildings and the acquisition of assets had fallen by 32% in the Western areas compared to 1992 levels; and by 52% in the Eastern areas. Indeed the total sum of depreciation of assets exceeds investment, meaning that local authorities are disinvesting. Over time, this will lead to a decrease in local government assets, and at the same time to aging of the existing infrastructure.

The reason for this decrease in investment is evidently to be found in the financial deficit many local authorities are running. Own revenue is decreasing, subsidies for investment are not forthcoming, and new credit hard to find. If local authorities still have assets to sell, very often this is a means to reduce deficits rather than in order to invest. In this situation, the federal government, some *Länder* and the private sector, especially the construction industry and the banks, promote the concept of 'public private partnerships' as a means to realise investment projects which otherwise would not materialise at all. The federal government as well as those *Länder* which are in favour have established task forces and commissioned feasibility studies to show the way. The federal government PPP task force was established at the Federal Ministry of Transport, Building and Urban Development in 2004 and continued until February 2009. In November 2008, a company was founded by two federal ministries (the above mentioned and the Ministry of Finance) together with 10 *Länder*, 82 local authorities and more than 70 private businesses. Under the name of 'Partnership Deutschland', this company provides independent advice for the public sector on planning for, establishing and managing PPP projects. However, the PPP database which tries to give an accurate picture of PPP projects in the whole country is still located at the Federal Ministry of Transport, Construction and Urban Development.

The current approach to PPP-projects is to consider the whole lifetime of a project, from planning through construction as well as the running and management, up to its becoming obsolete and its eventual demolition. By using this method, the aim is to optimise running costs, which over the lifetime of a project can be much higher than the initial investment. This is particularly true in the case of alterations and renovations.

There are two scenarios where PPP projects can be successful.

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- 1) Cases where new financial streams can be opened for a new service or facility, which citizens and/or businesses are willing to pay for. For example, if for a new road tunnel a fee can be levied, and it is used according to projections, then the necessary funding is secured. In such a case the problem is less of an economic but rather of a political-legal nature. In reality there are not many circumstances where such a model is feasible.
- 2) The second case concerns the updating and modernising of existing infrastructure, which is still needed in future. In these cases it is important that subsidies and transfers for investment purposes can be used for PPP projects. However, it is not only about the initial investment, but also about the running costs – and if the local authority cannot support these costs, then there is a problem.

In the first half of the last decade a large number of PPP projects were schools, as was ascertained by the first large-scale PPP-study conducted by the German Institute for Urban Affairs (DifU) in 2005. After another four years, a new study was conducted in 2009 by questioning all cities over 10 000 inhabitants, and a representative sample of smaller cities, as well as all counties, and the federal and *Länder* governments were also included. This questionnaire showed that currently 101 PPP projects are in progress in local authorities; some larger cities may have two or three projects running at the same time, while smaller local authorities will normally only deal with one at a time.

Of all the PPP projects that can be classified as 'infrastructure PPPs', 28% were schools, and 27% fall under sport, leisure and tourism. A further 15% are general administrative buildings, and 10% transport infrastructure.

The study detected a certain slow-down in the PPP market. The number of finished projects was 11 in 2008, the same number as in 2007. The reason for the slow-down is mainly seen in the recognition that PPP is not a method to finance infrastructure when otherwise finance is scarce, but instead a way of maximising resources and achieving efficiencies by considering the whole life-span of a project. Furthermore, the improved financial situation of local authorities in 2007 and 2008, until the crash struck, may have led some authorities to return to traditional procuring methods. Then, when the financial crisis had developed, local authorities were quickly preoccupied with planning for the investment projects based on the economic stimulus package funded by the federal government. And finally, banks and the private sector are becoming much more cautious in the pursuit of PPP, so the climate surrounding PPP has changed considerably.

The people dealing with PPP projects in local authorities express overall satisfaction with development, process and outcome of PPP projects. Satisfaction ratings and the fulfilment of criteria regarding efficiency and quality are closely connected – in most cases the criteria were met, but there are also cases of exceeding as well as falling short of expectations.

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Interestingly enough the achievement of agreed quality standards proves to be a bigger problem than achieving economic efficiency. Also, a quarter of projects experienced serious problems during at least one stage. In particular the drafting of contracts, the identification of risks and the necessary weighting of risks can be big challenges.

For the successful implementation of PPP projects a number of factors have to be considered. According to the people responding to the research, the most important are: thorough planning for needs and judgement of existing capacity, meticulous execution of feasibility study and planning, good project management and functioning communication between all partners involved. The main risks are named as incomplete contracts, insufficient flexibility to incorporate changes in projected targets and outcomes, and the loss of control in the public sector.

At the local authority level, the volume of PPP projects currently planned and progressing for the next five years is ca. 8.4 billion Euros, and another 5.8 billion Euros are spent on PPP projects by the federal and *Länder* governments.

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