Abstract

In recent years, the needs for the development of infrastructure and the public facilities, as a very significant factor of economic growth, have equally increased in the developing and the developed countries. The public governments' budgetary allowances are mostly insufficient to allow keeping pace with these needs. One of the options in finding new ways to finance the facilities of public significance are private investments through a network of contract agreements, widely known under the term public-private partnership (PPP).

A public private partnership represents a contract agreement between a properly empowered local, regional or state authority and a private partner with a clear share of responsibilities and risks with the purpose of satisfying a given public need.

The paper gives an overview of PPP models and the most significant European Commission's documents related to the PPP. Further, the opinion of the responsible local authorities in the City of Rijeka related to the possibilities of implementing the PPP models in regard with the realization of public facilities projects is presented. Finally, an analysis of the opportunities for PPP model application to one of the foreseen buildings is given.

Keywords: public private partnership, models, local, regional and state authorities, private partner, PPP model application

Introduction and definition of public-private partnership

The term public-private partnership (PPP) has become politically and socially fashionable over the last decade. What are the main reasons for that? Private companies became more customer-focused trying to conquer the market. The consumers got used to it and have increased their expectations of privately delivered products and services, so as public services. The solution is in including the private sector in traditionally delivered public services to bring in the skills they have developed in meeting customer needs and developing value for money and work in partnership with the public sector to provide better services.

Another reason, even more important, for searching for new, alternative ways of funding for public services is an increased public demand. Local and public budgets are regularly insufficient for direct financing of those more intensive needs for investing in public services and quality infrastructure solutions. Therefore it became necessary to generate or improve models which will attract investing of private capital in public sector programmes or projects through contractual obligations network.
The expression “public-private partnership” is widely used but is often not clearly defined. One of many definitions describes the public-private partnership as a “contractual agreement between public and private parties, in which both parties will receive significant benefits, whereby the private party performs some public function on behalf of the public party for a specified time and within a negotiated framework of transferred risk and outcome-based financial rewards” [4].

Basically, PPP represents the untraditional way of providing public services and building infrastructure combining the best advantages from the public and private sectors, with emphasis on achieving improved value for money, i.e. improved services for the same amount of money.

There is no single definition of the PPP. Depending on the country concerned, the term can cover a variety of transactions where the private sector is given the right to operate, for an extended period, a public service, ranging from relatively short term management contracts (with little or no capital investment) through concession contracts (which may encompass the design and build of substantial capital assets along with the provision of a range of services and the financing of the entire construction and operation), to joint ventures where there is a sharing of ownership between the public and private sectors. Generally speaking, PPP’s fill a space between traditionally procured government projects and full privatisation. Governments stretching the definition for political reasons can cause further confusion. However, the exact definition of PPP is not as important as ensuring that both sides, as the other stakeholders in the project, understand what it encompasses.

Definitions diversities are followed by different PPP structures (which will be described in further text) and unstandardized nomenclature to describe the partnership process.

**PPP models**

The essence of public-private partnership lies in the share of risks. To ensure the success of a project, it is important to foresee, as realistically as possible, the risks related to certain components and phases of the project and allocate them so that the balance ensures the best value for invested resources. The ideal risk-sharing solution is the one in which each partner takes over the risks he can best manage and total costs are thus minimised.

Most literature on PPP identifies the following models (structures) for implementing PPP projects [4]:

1. Service contracts
2. Operation and management contracts
3. Leases
4. Concessions
5. Build-Operate-Transfer (BOT) contracts and variants

The outlined classification is based according to the level of private sector involvement, duration and level of risk and responsibility of private partner, as shown in Figure 1. At the one end are those contracting vehicles in which the government retains full responsibility for design, construction, operations, maintenance, capital investment, financing and commercial risk and at the other are those models in which the private sector assumes a greater share of the responsibilities and risks.

We want to point out that we have given only a short description of the major options, while in practice hybrids of these models can often be found.
**Service contracts**

Service contracts are legally binding arrangements between a properly empowered government authority and a private partner to perform specific, usually non-core tasks within infrastructure systems. The term is far famed as outsourcing. Outsourcing is the contracting out of the facilities management services required by an organisation to external service providers. These contracts are typically competitively bid and are for short periods of few months to two years, after which they are re-bid. The responsibility for provision of the overall service, as well as any capital investment, remains with the public authority. Service contracting can be an attractive form of PPP where there is strong political or community opposition to wider involvement of the private sector, opposition to price increases, or where the government is seeking to shed responsibility for non-core functions.

**Operation and management contracts**

Operation and management contracts transfer responsibility for the operation and maintenance of government-owned entities to the private sector. Under such contracts, ownership of the entity and responsibility for service provision remain with government. Likewise, the bulk of the commercial risk and all the capital and investment risks remain with the public authority. Management control and authority, however, is transferred to a private partner, which applies its expertise to improve management systems and practices. Management contracts are generally three to five years in duration. Compensation may be in form of a fixed fee, as in the case of a fixed fee management contract, or it may be linked to performance indicators, as in the case of a performance-based management contract. However, under both models, the public authority still bears the financial risk associated with its responsibility for capital investment. Operation and management contracts are most beneficial where the main objective is to rapidly enhance a public enterprise’s efficiency, or to prepare for a deeper level of PPP, but they are not recommended if a government has as one of its main objectives accessing private finance for new investments because they do not necessarily transfer financial risk to the management contractor.
Leases
Under a lease, a private firm (Lessee) leases the assets of an enterprise from a properly empowered government authority (Lessor) and assumes full responsibility for operations and partial responsibility for investments for a period usually between ten and fifteen years. Typically under a lease, the user fee, or tariff in the case of utility services, is used to pay the “lessee fee”, which remunerates the Lessee for his costs, plus a reasonable return. The remainder of the tariff goes to the government and is used to fund capital investments. Under a lease, the government retains title to the assets and bears the responsibility for financing and planning capital investments and rehabilitation of assets. Lease are most appropriate where there is scope for large gains in operating efficiency but only limited need or scope for new investments. Leases have also sometimes been advocated as stepping stone toward a deeper level of PPP in the form of concessions. Their administrative complexity and the demands they place on governments are nearly as great as those of concessions, so a lease is a much bigger first step than a management contract.

Concessions
Under a concession, the private partner (Concessionaire) bears overall responsibility for the services, including operation, maintenance, and management, as well as capital investments for rehabilitation and renewal of assets, and the expansion of services. Concession can be contracted for an existing facility or for new one. The fixed assets either remain the property of the public authority or revert to public ownership at the end of the concession period. Concession contracts usually last for between twenty to thirty years, depending on the level of investments and the period required for the Concessionaire to recover its investments plus a reasonable rate of return. The Concessionaire is paid for its services directly by the consumer, based on the contractually set fee or tariff, which is adjustable over the life of the contract. The main advantage of a concession is that it passes full responsibility for operations, maintenance, rehabilitation, renewal and service expansion to the private partner and so creates incentives for efficiency in all the utility’s activities. Therefore, concessions are an attractive option where large investments are required. Concessions are administratively complex undertakings for governments, because they confer a long-term monopoly on the Concessionaire and thus require rigorous monitoring and enforcement.

Build-Operate-Transfer (BOT) contracts and its variants
BOT (Build Operate Transfer) designates the way of contracting the building of large infrastructure facilities with the involvement of the private sector. The organisers of the building, normally called sponsors, take over the financing, the organisation and the responsibility of the construction of such a facility and then, after it has been built, the responsibility for its use, maintenance and management for a certain period, mostly between 15 and 30 years. After the expiry of such a period, the sponsors return the facility to the government for future usage. BOT is a short term for the most frequent form of such contracting. However, in practice, there are many variants to the model. Besides BOT, there are other short terms such as BOOT, DBOOT, DBFO or PFI, BOOST, BRT, BLT, BTO, BOO, BBO, BT, ROO, DCMF [5]. These variants all have certain differences, and we shall herewith describe the differences between DBFO and BOT models. DBFO (Design Build Finance Operate) or PFI (Private Finance Initiative) model has been developed in Great Britain in the 1990s and has later spread to many European countries. Many public facilities (schools, hospitals, government
buildings, etc.) have been built using this financing model. The basic difference between the DBFO and the BOT models lies in the fact that for the first ones, the Government (or more often the local self-government) pays off the contractually defined “unique monthly payment” to the sponsors on a regular basis, during the whole duration of contract (after the start of the exploitation period), while the BOT contracts are most often funded by the user of the facility. BOT contracts and variants are the most complex form of the public-private partnership.

PPP documents in the European Union
The European Commission has so far published three important documents discussing the public-private partnership. In January 2003, it has published the Guidelines for Successful Public-Private Partnerships, a practical tool for the public sector facing the possibilities of structuring the schemes of public-private partnerships. The Guidelines do not aim to provide an overall methodology or define current and future policy but rather to focus on a number of critical issues crucial for the successful implementation of PPP projects.
In April 2004, the Commission has published the Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions analysing the PPP phenomenon in the light of the European Union regulations on public contracts and concessions. The Green paper also raises a set of questions about the existing practice and problems in European Union’s members which have already implemented projects following the model of the public-private partnership.
A few months later, in June 2004, the Resource Book on PPP Case Studies was published. It describes 26 PPP case studies in European countries. The examples described in the book are a valuable material which can be consulted in future planning and contracting of PPP projects.
Besides the above-mentioned documents, many European countries published their own guidelines, acts and programmes aiming at promoting the public-private partnership.

PPP in the Republic of Croatia and the City of Rijeka
As a European Union candidate country, the Republic of Croatia has a strong interest to occupy, as good a position as possible in the moment of accession to full membership. In that regard, PPP contracts in the development of infrastructure are especially attractive since they allow for new, large sources of funding for strategic projects a lot before, without the need to wait for future public budgets.
Firstly, there are some requirements that have to be fulfilled at the highest levels of public government for this funding model to come into life. The Government should clearly define its opinion on PPP within the long-term strategy of infrastructure development. The legal and institutional frameworks to promote these projects should also be arranged. Croatian legal acts and regulations contain provisions which can be applied to complex models of public-private partnerships, but these are not explicitly mentioned. For example, regulations on concessions are incorporated in numerous Croatian acts which should be harmonised and consolidated. Still, Croatia has an operating legal framework which allows for foreign investments, and there is also the Act on Public Procurement. We can conclude that some preconditions for public-private partnerships exist, but these are rudimental and need to be upgraded, modernised and adapted to new conditions. The situation is similar with regard to the institutions competent for the preparation and actualization of projects within the public-private partnerships.
In the Republic of Croatia public-private partnerships are only at their very beginning. However, first steps towards the implementation of the PPP have been made. The Government expressed its positive opinion on PPP which has been made known to the public through the media. In March this year, the Government has also founded the work-group for public-private partnerships whose task is to establish the requirements to be fulfilled in order for the PPP projects to be undertaken, as well as the rules of procedure for the realization and control of PPP projects. At the moment, PPP contracts are to be the primary method of funding the building of capital projects related to education and health, following the British PFI (DBFO) model. Members of Government think that PPP shall allow more successful integration of the Republic of Croatia into the European Union. It is necessary to mention that some successful infrastructure facilities have already been built in Croatia following the BOT model, but this paper shall emphasize the projects of local government units.

The head of the Work-group for the public-private partnerships is the Vice-Premier for economy, and one of the members is the Mayor of the City of Rijeka, together with two other mayors. In its document entitled *Guidelines of the City Government for the term 2005-2009*, the City of Rijeka has foreseen the realization on a large number of capital objects (swimming pools complex, sports hall, museum, roads and municipal infrastructure, etc.) where the funds needed to build them go a lot beyond the funds available from the local budget. The City government intended to fund the capital objects by variants of long-term financing of the local self-governments in the first place by issuing municipal bonds in the amount allowed by the Act on the budget which prescribes the total annual payments shall not exceed 20% of income gained in the previous year. Another unfavourable circumstance was that all indebtedness of a local self-government have to be approved by the Government and are subject to additional limitations related to total income of all self-governments in Croatia.

In that situation, the City of Rijeka explored new possibilities of funding the capital and other infrastructure constructions as well as public facilities which created new goals:
- to make long-term co-operation with the private sector and
- to fund the developmental projects of the City of Rijeka without burdening the local budget.

Application of PPP models satisfies both these goals and represents attractive solution in order to build and start using the constructions long time before it would be allowed by traditional ways of funding from the budget or by credit indebtedness.

In its attempts to prepare a valid base for new forms of funding, the City of Rijeka has founded a work-group for PPP at local level. Even though PPP models have not been applied yet in the City of Rijeka, first collaboration attempts between the public and the private sector in the construction of public facilities have already appeared.

One of the examples is the construction of the garage “G“ within the sports complex. The garage was planned as a 4-floor construction with the majority of parking places and a smaller area to let for various purposes. Total value of the construction has been estimated to 5.5 million € including the land on which the construction is built. After the analysis of possible funding models, made by the expert team, the City government accepted the proposal to adopt the model of *operative leasing* to fund the construction of the garage. One of the main reasons for the decision, as given in the explanation of the expert team, is because the payments of operative leasing are considered business cost and therefore there is no long-term indebtedness of the leasing beneficiary. The negative side of operative leasing is that the owner of the real estates from the beginning and at the end of the period is the leasing provider, i.e. the leasing company.
The City Government of Rijeka has allowed the transfer of investment authority for “G” garage, as well as the transfer of property of the real estate – land where the construction shall be built to the commercial society owned by the city at 100% which has one of the basic activities parking management (hereinafter: the Investor). Consequently, the Investor shall find the leasing company and conclude a lease contract and consign the right to build for its benefit and the payment of the established compensation. The compensation for the right to build, the value of the project documentation, the municipal taxes paid and the revision of the project documents will be accepted in the project as part of the guarantee of the Investor. The total funding shall be diminished for the amount of the above. The land remains property of the Investor. The finished construction shall be the property of the leasing company, and the Investor shall pay for the construction costs in by paying the monthly lease rates for the next 15 years amounting up to maximum 75% of the total cost of construction. The leasing contract shall determine the remaining value of the real estate at which, upon the expiry of the contractual deadline, the real estate can be bought off subtracting, however, the amount of the guarantee already paid.

The construction shall be financed and built by the leasing company for itself and on its own, and to the benefit of the leasing beneficiary. After the construction is built, the Investor rents it and uses it until the end of the contractual period. Since the financial analysis has shown the construction is not profitable or, in other words, the estimate of the incomes (from parking and lease of business premises) and expenditures showed it will not be possible to pay the rent without additional sources, and therefore the co-financing contract has been signed between the Investor and the City of Rijeka.

Construction financing following the operative leasing model can not be considered financing following the model of public-private partnership. The basic characteristic of the public-private partnership is the partial transfer of risks to a private partner during the determined period and the private partner's involvement in project management. However, operative leasing as described in this paper can undoubtedly be considered a major step forward towards the co-operation of the public and the private sectors, which is, accompanied with the support of the local and state governments, unquestionable.

In the example of the construction of the “G” garage, the private partner takes all the risks related to the construction and the partnership is clear in the sharing of property – the land remains in the property of the public partner while the private partner becomes
the proprietor of the real estate built on the public partner's land. The adequacy of the funding model adopted in the presented example is also evident from the fact that the project is managed by the city's company whose major activity is parking management and the quality of parking services offered is therefore expected to be very good and taking into consideration the fact that the private partner is a leasing company which, should it had managed the construction, would have had to sub-contract the parking management to a company specialised in the parking activity.

The goal of concluding the operative leasing contract was to retain the credit potentials of the City of Rijeka and the Investor leaving the possibility of indebtedness for the building of some other capital objects. The major disadvantage of the given model for the public partner is contained in the fact that the real estate remains property of the leasing company for the whole duration and in the end of the contractual period. However, upon the expiry of the lease contract the real estates can be bought off for the market price of the remaining value.

**Conclusion**

The public-private partnership gains more and more attention in European Union countries, and various interest groups have different, often opposite opinions on its application. The success of the public-private partnership primarily depends on the public government’s attitude, on the thoroughness of the project’s preparation, on the expertise of the negotiators on both the public and the private partners’ sides, as well as on public relations. Besides that, a public partner has to be very careful when entering such co-operation with a private investor because it is publicly responsible for his actions. For that reason, the each side’s responsibilities for the entire project and its implementation have to be well-defined in the contracts. Nonetheless, public partners have to make sure there is a good public control in all stages of the project.

At present, the Republic of Croatia lives in a dynamic period facing European Union full membership. The position of the country within the European Union mostly depends on its economic and political conditions in that moment. It is therefore important to lead the country into as good a position as possible, both economical and political. One of the moving forces for the development of the economy is undoubtedly good infrastructure which has to be developed burdening as less as possible the public budget and with the minimum foreign indebtedness. One of the solutions for infrastructure investments could be the public-private partnerships. PPP models can bring significant amounts of private funds for the development of infrastructure and public facilities. Croatia is currently in the preliminary phase in which a positive attitude towards PPP has been achieved, and defining the legal and institutional framework for the implementation of new models of financing is started.

**References**