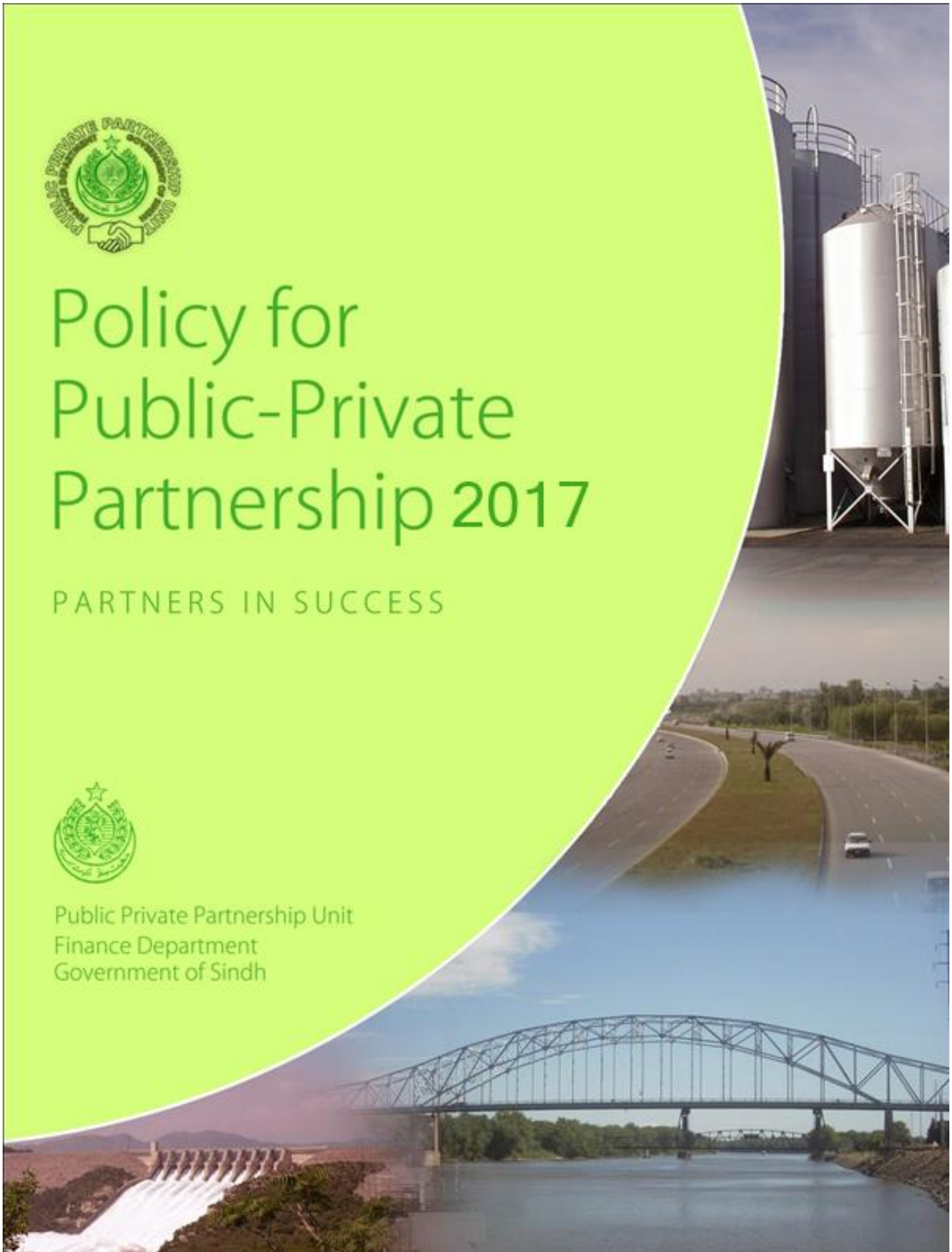
Policy for Public-Private Partnership 2017

PARTNERS IN SUCCESS



Public Private Partnership Unit
Finance Department
Government of Sindh

FINANCE DEPARTMENT

GOVERNMENT OF SINDH

Policy for Public Private Partnership Projects in Sindh Province

The amended Policy for Public Private Partnership (PPP) Projects have been approved by the PPP Policy Board in its 22nd meeting (7th November 2017) held under the chairmanship of Honorable Chief Minister Sindh.

ABBREVIATIONS

BOT	–	Build- Operate-Transfer
FD	–	Finance Department
GF	–	Guarantee Fund
IPDF	–	Infrastructure Project Development Facility
IPFF	–	Infrastructure Project Financing Facility
P&DD	–	Planning & Development Department
PDF	–	Project Development Facility
PPP	–	Public-Private Partnership
VGF	–	Viability Gap Funding

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INTRODUCTION

1. Public-Private Partnerships (PPPs) are being widely used as a procurement method by governments all over the world. The objective of such partnerships is to better serve the public through partnering arrangements with private sector. PPP mode of procurement, though at nascent stage in the province of Sindh at present, has great potential in the future. In view of the special characteristics of PPP projects and the need to attract qualified private investors to support these projects, a special legal and regulatory framework is needed. To meet this objective, the Government of Sindh ("the Government") has enacted a PPP Law and promulgated new Rules for PPPs. These policy guidelines have been drafted to supplement the legal and regulatory framework for PPPs and to assist both the private and the public sectors in implementing this innovative procurement methodology.

2. For sustained development, PPPs will have to be mainstreamed in Sindh, rather than being used just for a few special projects. To fully utilize the PPP potential and to ensure that PPP projects are successful and mutually beneficial, a comprehensive enabling environment for private investments in infrastructure facilities is being created through the adoption of relevant policies, establishment of a legal and regulatory framework and introduction of clear guidelines for cost recovery and PPP financing arrangements.

3. The PPP Policy aims at reinforcing the considerable enthusiasm for PPPs in various sectors, addressing the lack of trust between the public and private sectors to collaborate in infrastructure projects, and facilitating the creation of effective partnerships. The Government is committed to overcoming some of the built-in obstacles to the development of PPPs and to streamline the process so that potential projects can be properly evaluated and approved based on sound feasibility studies and well designed and transparent procurement practices. The PPP Policy describes both what needs to be done for PPPs and how to do it in a consistent manner.

PPP CONCEPT

A. Rationale

4. PPP procurement for infrastructure projects is being promoted by the Government to:

(i) Improve the efficiency and effectiveness of the public sector in the delivery of public goods and services;

(ii) Leverage limited public sector funds for key infrastructure projects;

(iii) Provide opportunities for the application of innovative technologies and methods that are best provided by private sector companies;

(iv) Allocate some of the development, construction and operational risks in public service projects to private sponsors who are better placed to manage those risks; and

(v) Apply rigorous feasibility and procurement techniques in preparation and execution of PPP projects to obtain best value for the public.

B. PPP Definition

5. There is no universally accepted definition of PPPs. Instead, a wide range of definitions can be found. However, it is clear that PPPs have been adopted around the world as a service delivery tool. Instead of the public sector procuring a public asset and providing a public service, the private sector creates the asset through a dedicated standalone business (usually designed, financed, built, maintained and operated by the private sector) and then delivers a service to a public sector entity/consumer, in return for payment that is linked to performance. PPPs permit the public sector to redirect its capital expenditures to meet urgent social needs and convert the infrastructure costs into affordable operating expenditure spread over time. PPPs allow each partner to concentrate on activities that best suit their skills. For the public sector, that means focusing on developing sector policies and identifying service needs, while for the private sector the key is to deliver those services efficiently and effectively. These ideas are captured in the definition applied in the Sindh Public Private Partnership Law ("PPP Law") which succinctly states:

"Public-Private Partnership" means a partnership carried out under a Public-Private Partnership Agreement between the public sector represented by an Agency[1] *and a private party for the provision of an infrastructure facility, management functions and / or service with a clear allocation of risks between the two parties"*

6. In PPP program, the Government sees itself becoming more of a regulator and less a provider of public services. A clear and fair sharing of risks in financing, developing,

operating and maintaining infrastructure services between the public and private sector, based on a mutual commitment to achieve a desired public sector outcome while obtaining appropriate rate of returns for the private sector, is a distinguishing feature of PPP projects and essential for their success.

For major infrastructure projects, the capital investment and operational expenses incurred by the private investor can be recovered under the PPP concept by charging users for the service provided, through fixed or partially fixed periodic payments, or receiving availability payments in the form of unitary payments or annuities from the public sector over the period of the contract, or by a combination of both. The Government recognizes that infrastructure projects require long gestation periods to ensure affordable tariff levels, which expose private investors' investment to significant risks. It must therefore establish a framework that reassures the investment community about the Government's commitment to the rule of law and contractual fairness.

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[1] Department, attached department, body corporate, autonomous body of the Government, local government, or any organization or corporation owned or controlled by the Government or the local government.

POLICY OBJECTIVES AND PRINCIPLES

7. Government intends to achieve following objectives, using PPP approach:

(i) Promoting social development, employment generation, and inclusive economic growth through development of infrastructure;

(ii) Ensuring sustainable long-term funding for infrastructure development through mobilization of private investments;

(iii) Ensuring technical, economic and financial viability of infrastructure projects through adequate project preparation;

(iv) Improving the efficiency of management, operation and maintenance of infrastructure facilities through introduction of modern technology and management techniques;

(v) Achieving a larger scope and better quality of infrastructure services for end users through the additional financial and human resources mobilized from the private sector;

(vi) Ensuring financial sustainability of infrastructure services through full cost recovery supplemented by viability gap funding (VGF), if necessary; and

(vii) Protecting the best interests of all stakeholders including end users, the Government and the private sector.

8. To achieve these objectives, the Government shall adhere to the following principles:

(i) **Legal Certainty** – compliance with the relevant laws and regulations;

(ii) **Fairness –** creation of a level-playing field for all private investors, without any discrimination;

(iii) **Transparency** – access to information to private investors and the public at all stages of the project cycle;

(iv) **Competition** –Provision of equal opportunity to all prospective bidders to participate in the tendering process without any hindrance.

(v) **Contract Sanctity – securing of** rights and interests of parties to the PPP agreement; and

(vi) **Mutual Support and Benefit –** fair and mutually beneficial cooperation of parties to the PPP agreement.

9. The Government's commitment to promoting PPPs is expected to lead to the following benefits:

(i) **More services** that will help cover both the current and future needs in social and infrastructure development.

(ii) **Better services** that will improve the quality of life of people in general and would lead to economic uplift of the poor strata of the society in particular.

(iii) **Affordable services** that will allow access to low-income end users. Certain segments of the population cannot pay commercial tariffs, whereas the private service provider needs to fully recover its costs in order to sustain operations. In such cases, the Government will provide subsidies in the form of VGF.

(iv) **Timely services** that will help the Government meet the urgent service demands of its citizens.

10. These benefits will be achieved by the following means:

(i) **Faster project implementation** by the private sector resulting in projects being completed on time. As borne out by experience in both developed and developing countries, public sector projects experience more delays than those undertaken by the private sector in PPP mode.

(ii) **Leveraging public funds** with private financing from local and international markets. For every rupee that the Government spends it will strive to leverage the maximum possible from the private sector. The ultimate objective will be to limit the Government's contribution to providing targeted subsidies to low income consumers in order to allow full cost recovery by the private service provider.

(iii) **Leveraging public land** to make the projects commercially viable through lowering the cost of the project and partly to minimize the need of commercial loan in the project. In both ways, the projects shall be commercially viable and doable.

(iv) **Enhanced accountability** in service delivery by linking service provision to a firm contractual arrangement. The service levels will be defined clearly in the PPP agreements in terms of outputs and outcomes required from the private sector. The government agencies will be required to put in place strict monitoring mechanisms. Poor performance by the private service provider will be penalized and may result in contract termination.

(v) Since the focus in engaging with the private sector is on services it provides during the entire concession period, the private investors will have the incentive to ensure that the underlying assets are of good quality and adequately maintained.

11. The PPP Policy puts a great weight on safeguarding public interest and consumer rights by:

(i) Aiming at uninterrupted public access to essential infrastructure;

(ii) Ensuring public health and safety; (i) Protecting the environment: the government shall determine parameters of Initial Environment Examination (IEE): After the Project identification, the Administrative Department would describe very clearly the Environmental & Social Impacts including resettlement and gender equality etc in light with the parameters laid down in the existing Environmental & Resettlement Framework in Pakistan, and efforts will be made to ensure implementation consistent with international good practices, as reflected in internationally recognized standards such as the Equator Principles;

(iii) Providing adequate and equal protection of end users' rights to privacy, regardless of their ethnicity, gender, age, occupation, and civil, social and economic status;

(iv) Providing information to the public about the obligations of the private sector and the Government; and

(v) Setting affordable user charges and tariff structure.

TYPES OF PPP AGREEMENTS

12. The PPP contracts are structured into different configurations depending upon the nature of the project and the risk allocation between the Government and the private sector. The bidding documents carefully describe in each project the type of PPP arrangement to be applied to assist the government agencies and investors in formulating proposals, assessing their respective business strategies and preparing the documentation for each proposed transaction.

13. The Sindh PPP Act 2010 describes various concession contracts found in PPP arrangements but does not restrict the contract arrangements to the defined few. Following categories will be used in processing PPP proposals in Sindh depending upon the suitability to the specific project. These categories are indicative and do not restrict government agencies from applying other arrangements with the approval of the PPP Policy Board:

(i) **Build-and-Transfer (BT):** A contractual arrangement whereby the private party undertakes the financing and construction of an infrastructure project and after its completion hands it over to the Agency. The Agency will reimburse the total project investment, on the basis of an agreed schedule. This arrangement may be employed in the construction of any infrastructure project, including critical facilities, which for security or strategic reasons must be operated directly by the Agency.

(ii) **Build-Lease-and-Transfer (BLT):** A contractual arrangement whereby the private party undertakes the financing and construction of an infrastructure project and upon its completion hands it over to the Agency on a lease arrangement for a fixed period, after the expiry of which ownership of the project is automatically transferred to the Agency. The lease payments are structured to reimburse the Private Party for its investment and repay the loan.

(iii) **Build-Operate-and-Transfer (BOT):** A contractual arrangement whereby the private party undertakes the financing and construction of an infrastructure project, and the operation and maintenance thereof. The private party operates the facility over a fixed term during which it is allowed to collect from project users appropriate tariffs, tolls, fees, rentals, or charges not exceeding those proposed in agreement. This enables the private party to recover its investment and operation and maintenance expenses for the project. The private party transfers the facility to the Agency at the end of the fixed term that shall be specified in the Public-Private Partnership Agreement.

(iv) **Build-Own-and-Operate (BOO):** A contractual arrangement whereby the private party is authorized to finance, construct, own, operate and maintain an infrastructure project, from which the private party is allowed to recover its investment and operating and maintenance expenses by collecting user fees from
(v) Project users. The private party owns the project and may choose to assign its operation and maintenance to a project operator. The transfer of the project to the Agency is not envisaged in this arrangement. However, the Agency may terminate its obligations after the specified time period.

(vi) **Build-Own-Operate-Transfer (BOOT):** A contractual arrangement similar to the BOT agreement, except that the private party owns the infrastructure project during the fixed term before its transfer to the Agency.

(vii) **Build-Transfer-and-Operate (BTO):** A contractual arrangement whereby the Agency contracts out an infrastructure project to the private party to construct it on a turn-key basis, assuming cost overruns, delays and specified performance risks. Once the project is commissioned, the private party is given the right to operate the facility and collect user fees under the Public-Private Partnership Agreement. The title of the project always vests in the Agency in this arrangement.

(viii) **Contract-Add-and-Operate (CAO):** A contractual arrangement whereby the private party expands an existing infrastructure facility, which it gets leased from the Agency. The private party operates the expanded project and collects user fees, to recover the investment over an agreed period. There may or may not be a transfer arrangement with regard to the added facility provided by the private party.

(ix) **Develop-Operate-and-Transfer (DOT):** A contractual arrangement whereby favorable conditions external to an infrastructure project, which is to be built by the private party, are integrated into the Public-Private Partnership Agreement by giving it the right to develop adjoining property and thus enjoy some of the benefits the investment creates such as higher property or rent values.

(x) **Rehabilitate-Operate-and-Transfer (ROT):** A contractual arrangement whereby an existing infrastructure facility is handed over to the private party to refurbish, operate and maintain it for a specified period, during which the private party collects user fees to recover its investment and operation and maintenance expenses. At the expiry of this period, the facility is returned to the Agency. The term is also used to describe the purchase of an existing facility from abroad, importing, refurbishing, erecting and operating it.

(xi) **Rehabilitate-Own-and-Operate (ROO):** A contractual arrangement whereby an existing infrastructure facility is handed over to the private party to refurbish, operate and maintain with no time limitation imposed on ownership. The private party is allowed to collect user fees to recover its investment and operation and maintenance expenses in perpetuity.

(xii) **(XI) Joint Ventures (JV):** Joint ventures (JVs) are also a form of PPPs in which a company is co- owned and operated by the public and private sector partners. We have seen JV extensively useful and suitable for economic sectors such as mining, manufacturing and agriculture, JVs in the infrastructure sectors like roads etc pose several problems. The Government's dual role as the regulator and a part owner could lead to conflicts of interest. A clear risk allocation, which is a major advantage of PPPs, is blurred by JVs. There are however, some inherent problems with JVs and that include direct negotiations and avoiding Competent Bidding Process which should always be avoided in JVs. Transparency is the underlying objective in all sorts of procurement and JVs are no exception to it.

(xiii) **Management Contract (MC):** A contractual arrangement whereby the Agency entrusts the operation and management of an infrastructure project to the private party for an agreed period on payment of specified consideration. The Agency may charge the user fees and collect the same either itself or entrust the collection for consideration to any person who shall pay the same to the Agency.

(xiv) **Service Contract (SC):** Any outsourcing contract by an Agency to any private party whereby the private party undertakes to provide services to the Agency for a specified period with respect to an infrastructure facility. The Agency shall pay the private party an amount according to an agreed schedule.

14. As defined in this PPP Policy, the PPP modalities do not include privatization, which is handled under a different framework and by different institutions.

SECTORAL COVERAGE OF THE PPP POLICY

15. PPP projects have been traditionally used worldwide in the hard core infrastructure sectors such as energy, transport and water supply. More recently, the use of this approach has been expanded to infrastructure development in social sectors, such as education and health facilities. Suggestions have been made to expand the scope of the PPP Policy to all sectors. In addition, there are two fundamental differences between the infrastructure and economic sectors. As defined in Para- 6 above, infrastructure PPP projects are long-term contractual arrangements between the public sector and a private company for the provision of infrastructure services, which have the character of public goods. Typical examples of such services, which are regulated by the Government, are supply of water; collection and disposal of solid waste; and provision of roads. In these sectors, services are the output and PPP projects are the preferred approach to private sector participation. By contrast, the economic sectors are unregulated and produce private goods such as industrial equipment, cars, milk or rice. Products are the output, and private investors get involved in these sectors through partial or full privatization.

16. Based on the above considerations, the Government's PPP Policy will cover infrastructure projects in the following sectors broadly defined to include social sectors:

(i) **Transport and Logistics** including provincial and municipal roads, rail, as well as warehousing, wholesale markets, slaughter houses and cold storage;

(ii) **Mass urban public transport** including integrated bus systems as well as intra and inter-city rail systems;[2]

(iii) **Local government services** including water supply and sanitation, solid waste management; low cost housing, land reclamation, education and health facilities;

(iv) **Energy projects** including hydro and thermal power generation projects including power projects emanating alternative sources of energy;

(v) **Tourism Projects** including cultural centers, sports, entertainment and recreational facilities and other tourism related infrastructure;

(vi) **Canals or dams** (Which have possibility of Private sector participation);

(vii) **Information and Communication Technology**;

PPP FRAMEWORK

17. Given the intense global and domestic competition for capital, the Government is putting in place a PPP framework that aims at attracting private investments by:

(i) Providing policy and legal certainty to investors;

(ii) Introducing effective institutional arrangements for PPPs;

(iii) Ensuring fair risk sharing between the public and private sector;

(iv) Developing adequate regulatory arrangements, including effective mechanisms for dispute resolution;

(v) Introducing tariff regimes that are based on full cost recovery;

(vi) Making supplementary financing arrangements for project preparation and implementation;

(vii) Developing a pipeline of attractive PPP projects; and

(viii) Providing other incentives such as waiver of taxes for a specific period with the approval of PPP Policy Board and the Government.

(ix) Providing other incentives such as waiver of taxes for a specific period with the approval of PPP Policy Board and the Government.

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2 Airports and railroads are not included because they are usually owned and operated under federal regulations.

18. The PPP framework, which consists of various policies, legal, institutional and regulatory components, has the following main objectives:

(i) Creating an enabling environment for private sector participation in infrastructure development; and

(ii) Ensuring consistency in preparing and executing PPP projects across infrastructure sectors.

19. Table 1 summarizes how the different components of the PPP framework are linked to the above- mentioned prerequisites for attracting private investors.

Table 1: Components of the PPP Frame work

Prerequisite	Component
Policy certainty	PPP policy guidelines on its implementation
Legal certainty	Sindh Public Private Partnership Act 2010
Effective institutional arrangements	PPP institutional framework (PPP Policy Board, PPP Unit, Risk Management Unit, and PPP Nodes)
Fair risk sharing	Risk management guidelines through PPP RMU (Risk Management Unit)
Adequate regulatory arrangements	Initially regulation by contract, later independent regulatory bodies e.g. appointment of Independent Engineer and Independent Auditor for a project
Full cost recovery	Cost-based tariff setting and adjustment mechanisms, complemented by direct government support through viability gap funding (if necessary)
Supplementary financing arrangements	Viability Gap Fund mechanism
Pipeline of attractive PPP projects	Preparation and execution of pilot projects to start the process; increased bankability of projects via incorporation of social and environmental safeguard provisions

PPP LAW

20. For the private investments in infrastructure to materialize, a comprehensive and consistent cross- sector legal framework is essential that establishes a clear and predictable environment within which investors will finance, implement and operate PPP projects. International experience indicates that several areas are especially important for the success or failure of such projects. A failure is more likely when the responsibilities within government for PPP development are not clearly delineated, the procedure for selecting the private partners is vague, and the procedure for dealing with unsolicited project proposals from private investors is not defined. Moreover, because of the importance of the contractual relationships, there must also be a consistency in the treatment of investors and lenders participating in PPP agreements, which is best achieved through clear directives in the law and regulations.

21. To provide a firm legal framework, th*e Public Private Partnership Law, namely Sindh Public Private Partnership Act 2010* has been enacted. The PPP law is based on an inter-country comparison, incorporates international best practices, and is consistent with the other components of the enabling PPP framework. Apart from specifying the various sectors and PPP modalities covered, the law outlines the institutional arrangements for PPPs; specifies the government agencies acting as the public sector partners; assigns the responsibility for PPP project identification and preparation; stipulates the rules, procedure and responsibility for the selection of the private sector partners; lists the main terms and conditions of PPP agreements, including social and environmental responsibilities; outlines the types of government support; and defines the cost recovery and risk sharing principles.

INSTITUTIONAL ARRANGEMENTS

A. Main Components

22. International experience suggests that establishing clear, effective and efficient institutional arrangements is another prerequisite for successful implementation of PPP projects. The Government has therefore created the following new entities as an integral part of the enabling PPP framework:

(i) A high-level Public Private Partnership Policy Board headed by the Chief Minister of the Province to formulate PPP Policy based on strategic goals and implementation in the Province;

(ii) A central PPP Unit located in the Finance Department to assist the PPP Policy Board in formulating and implementing PPP Policy;

(iii) PPP Nodes as focal points for specific PPP projects in line departments and city district governments; and

B. PPP Policy Board

23. To ensure a consistent approach to PPPs across sectors and an efficient use of funds by line departments and local governments, strong and effective coordination will be provided by the PPP Policy Board as constituted under Section 4(2) of the Sindh Public Private Partnership Act 2010.

24. The PPP Policy Board will be the final deciding body for all PPP projects in Sindh. As such, it will have the following responsibilities:

(i) Formulate the PPP Policy, guidelines and rules for the Government;

(ii) Supervise and coordinate implementation of the PPP Policy by line departments and local governments;

(iii) Approve, reject or send back for reconsideration PPP project proposals submitted by an agency within six (6) months;

(iv) Decide on any direct or contingent support for a project proposal submitted by an Agency;

(v) Approve, reject or send back for reconsideration recommendations submitted by an agency on contract awards to private party; and

(vi) Issue risk management guidelines, to assess that government support for projects is included in the annual budget of the Province and that such support is fiscally sustainable, and establish procedures to implement such guidelines consistent with the PPP Law;

(vii) Assist the agencies in solving major problems impeding PPP project preparation and implementation;

(viii) approve funding for projects receiving support through the Project Development Facility ;

(ix) be the final deciding authority for all the projects; and

(x) take all other steps necessary to give effect to the provisions of PPP Act 2010.

C. PPP Unit

The Government of Sindh has established the PPP Unit in the Finance Department to promote and facilitate the development of Public-Private Partnerships in the Province, assist an Agency in preparing and executing mega projects which could afford the cost of project structuring and due diligence, and act as a catalyst for Public-Private Partnerships.

1. The PPP Unit will have the following main functions:

(i) Assist the PPP Policy Board in formulating, implementing the Public Private Partnership Policy and provide technical support to the PPP Policy Board and act as its secretariat;

(ii) Develop operating guidelines, procedures and model documents for PPP projects for approval by the PPP Policy Board, using gender-fair language;

(iii) Develop technical and human resources to support Public-Private Partnership initiatives at the Agencies while promoting women's access to capacity building opportunities;

(iv) Provide technical support and advice to line agencies throughout the Public Private Partnership process;

(v) Evaluate and prioritize project proposals submitted by agencies;

(vi) Evaluate the type and amount of government support sought for a project;

(vii) Review bid evaluation reports, submitted by an agency;

(viii) Prepare and regularly update a pipeline of projects;

(ix) Oversee project implementation and issue semi-annual review and annual consolidated reports on the Public-Private Partnership projects in the Province; and perform any other functions as may be assigned to it by the Board.

26. Identification and management of risk is an integral part of the PPP evaluation process. Fair and clear sharing of risks between public and private partners is a prerequisite for success of PPP Projects. In many countries, this function is carried out by a specialized unit. In Sindh, the Government has decided to place this function with the PPP Unit until it has well trained and experienced risk management specialists to staff an independent unit. The PPP Unit will work as risk manager in light of the risk management guidelines to be approved by the PPP Policy Board.

27. In carrying out the risk management function, the PPP Unit shall:

(i) Develop risk management guidelines for PPP projects;

(ii) Examine whether requests for government support and the proposed risk sharing arrangements are consistent with the risk management guidelines and fiscally sustainable;

(iii) Ensure the inclusion of approved government support in the Government's Annual Development Program;

(iv) Monitor the Government's direct and contingent liabilities related to PPP projects;

(v) Monitor the financial performance of PPP projects during their operation; and

(vi) Perform any other functions as may be assigned to it by the PPP Policy Board.

D. PPP Nodes

28. The administrative head of each Agency which seeks to implement a project on a Public-Private Partnership basis, should form a Public-Private Partnership Node with the approval of concerned Minister consisting of officers from within the Agency or other Agencies as the case may be, which may include representative from the Finance Department, a gender focal point representative of the Agency and independent technical and legal experts if deemed appropriate to develop the project. The PPP Nodes will have the following main functions, during the performance of which they may seek support and advice of the PPP Unit:

(i) Identify suitable PPP projects and prioritize these within their sector or geographical area of responsibility;

(ii) Recruit transaction advisors for project preparation and tendering;

(iii) Supervise the preparation of feasibility studies that are inclusive of social, environmental, and gender analyses, and if their outcome is positive, submit the PPP project proposals to the PPP Policy Board;

(iv) Conduct a competitive tendering process consisting of pre-qualification and bidding to select the private sector partners;

(v) Carry out bid evaluation and submit recommendations on contract award to the Board;

(vi) Negotiate and sign the Public Private Partnership agreement;

(vii) Monitor and evaluate implementation and operation of the project.

(viii) if needed, seek support and advice from the Unit for the performance of any of the above function; and

(ix) prepare periodic progress reports on the Agency's projects to be submitted to the PPP Policy Board through Unit.

E. Demarcation of Responsibilities

29. Table 2 summarizes the demarcation of the principal responsibilities within the PPP institutional framework. The demarcation reflects the crucial role played by the PPP Nodes in the identification, preparation, tendering and monitoring of PPP projects; prioritization role, the quality control and the role of fiscal guardian played by the PPP Unit; and the approving authority exercised by the PPP Policy Board during the project preparation and tendering phases.

Table 2: Demarcation of Main Responsibilities for PPP Projects

Entity	**Proposed Location**	***Project-Related Responsibility***
PPP Policy Board	Chief Minister House	• *Inter-departmental coordination* • *Approval/rejection of PPP project proposals* • *Approval/rejection of contract award recommendations* • *Decision-making on major PPP policy and implementation issues*
PPP Unit	Finance Department	• *Project identification* • *Project preparation for those projects competent authority (PPP Policy Board) assigns and carrying out of the whole project development and transaction stage* • *Quality control (review of PPP project proposals for completeness and viability)* • *Cross-sectoral and intra-provincial prioritization* • *Technical support to the PPP Policy Board* • *Review of justification and eligibility for government support* • *Fiscal sustainability* • *Risk Management to be separately evaluated by the RMU*
PPP Nodes	*Line departments and city district governments*	• *Project identification* • *Project preparation (feasibility study)* • *Selection of private sector partners (tendering)* • *Monitoring of implementation and operation*

RISK SHARING AND MANAGEMENT

30. A risk is defined as any factor, event or influence that threatens the successful completion of a project in terms of time, cost or quality. A key principle of PPP projects is that risk should be allocated to the party best able to manage it. The effective allocation of risk has a direct financial impact on the project as it will result in lower overall project costs and will therefore provide enhanced value for money if compared to traditional procurement methods.

The objectives of appropriate risk allocation include:

- To reduce long term cost of a project by allocating risk to the party best able to manage it in a most cost effective manner
- To provide incentives to the contractor to deliver projects on time, to required standard and within the budget
- To improve the quality of service and increase revenue through more efficient operation
- To provide a more consistent and predictable profile of expenditure

31. To ensure that the desired high level of private investments in PPP projects materializes, adequate risk mitigation and fair risk sharing between the public and private sector are essential. A sound investment climate is the best risk mitigation mechanism. This calls for continuous and sustained policy reforms that lead to a stable macroeconomic environment, well-functioning judicial system, independent and technically sound regulation, full cost recovery (or a well-targeted output-based subsidy where the full cost recovery would make such services unaffordable), and open access in the infrastructure sectors.

32. It is necessary to identify the various types of risks (financial, structural, social, environmental etc.) in each sector and for each project type, and to allocate them to the party that can best control them. There is no universal solution applicable to all situations, and the range of possible solutions is wide, depending on the specific circumstances of each case. Risk allocation must be laid out in very clear terms for each project but its transfer from public sector to private investors has to be gradual, until the stage is reached when market instruments rather than government guarantees can be used for risk hedging.

33. As a part of the enabling PPP framework, the Government will develop risk management guidelines for the PPP Projects as an instrument for assessing, pricing, monitoring and managing the contingent liabilities that arise from selective guarantees for PPP projects against risks related to policies and performance of the Government and its agencies. In view of the links to its existing budgeting, fiscal accounting and debt management systems, FD will play a key role in developing and implementing the guidelines through the PPP Unit, with the view to ensuring that risks of individual PPP projects are appropriately allocated between the public and private sector, and that the Government’s overall exposure is well managed.

34. The dual objective of the risk management guidelines will be to support infrastructure development while maintaining the fiscal sustainability of Sindh's budget.

The guidelines will describe the following:

(i) The types of risks to be borne by the Government (in particular, the political risks such as changes in policy, delay of agreed tariff adjustments, and expropriation);

(ii) Those to be borne by the private sector (in particular, the commercial risks such as construction cost overruns and delays, and failure to perform according to specifications);

(iii) Those to be assigned on a case-by-case basis such as force majeure, inability of government agencies to pay for infrastructure services (the so-called credit or offtake risk), and demand risk;

(iv) The main principles for providing government support such as (a) legality; (b) PPP project quality in terms of technical, economic, financial, and environmental viability; (c) fiscal prudence in terms of total exposure and annual budget; and (d) transparency in terms of deciding about government support before bidding; and

(v) Review and approval procedures for government support.

A. Identification, Allocation and Mitigation of Risks

35. Under public procurement, the Government bears all or most of the risks. A major advantage of PPP projects is that as many risks as appropriate are shifted to the private sector, which then receives the rewards for its investment and risk taking.

36. Risks can be looked at from the perspective of the different parties concerned: (i) the private sector partners, (ii) the lenders, (iii) the Government, and (iv) the users of the services provided by the PPP project. Risks can also be grouped into categories according to their type: (i) commercial risks, which are related to the sector or business activity being contemplated; (ii) risks specific to a country, which include political, economic, financial, environmental, and social risks; and (iii) risks of a general nature such as force majeure. Risks can also be differentiated according to when they arise in the project cycle: (i) development phase risks, (ii) construction phase risks, and (iii) operation phase risks. PPP risks are both generic and project specific. The feasibility study prepared by the Government for each PPP project will identify and propose allocation of all these types of risks.

37. The general risk process, to be followed when developing PPP projects, will start with risk identification. The type of the project and the choice of the PPP modality will determine what risks are applicable. A PPP project involving a service or operation and maintenance contract may have little or no market risk. In other PPP projects such as BOTs, such risk is very significant. The risk identification will be followed by risk allocation. The basic principle will be that risks should generally be borne by the party best able to manage them at minimum cost. This implies that the optimum risk allocation is not the same as the maximum risk transfer to the private sector. Typical examples are construction and operation risks, which are usually borne by the private sector, and policy and expropriation risks, which are clearly within the control of the Government and therefore borne by the public sector. Proper risk allocation will generate incentives to and penalties for the private sector to supply cost-effective and higher-quality infrastructure and service delivery.

38. The Government will ensure that the private sector takes appropriate and least-cost risk mitigation measures on its part in order to sustain the PPP project. For the risks allocated to the public sector, the Government will issue, if necessary, guarantees to backstop the obligation of its agencies, which have entered into a PPP agreement with private firms. The fiscal impact of these contingent liabilities will be quantified and monitored by the PPP Unit.

REGULATORY ARRANGEMENTS

39. Some PPPs in Sindh will be in unregulated sectors, while others will be regulated by line departments and local governments. During this initial phase, regulation by contract will play an important role. The Government will therefore develop good model contracts in each sector as part of the pilot PPP project preparation.

40. To ensure strong private sector participation in infrastructure development, there must be a gradual shift in the role of the Government from service provider to policy maker, planner, coordinator, facilitator, regulator for ensuring end user rights and purchaser of infrastructure services. In line with this shift, the Government intends to devolve, in the medium term of 3-5 years, its regulatory functions to newly created independent bodies, with the Government keeping the responsibility for policy making and sector planning. This separation of responsibilities will enhance the credibility of economic regulation and give confidence to investors that tariff matters are handled without political interference. There are two options
– having either a separate regulator in each of the main infrastructure sectors, or a single cross-sector regulatory body. International experience suggests that the first option is preferable.

41. Economic regulation will have two main objectives: (i) ensuring that consumers have access to essential services on a sustainable and affordable basis, and (ii) encouraging private sector participation in the development of infrastructure facilities required to provide those services. In pursuing these objectives the new regulatory bodies will have the following functions:

(i) Setting (approving) tariffs and other service charges;

(ii) Establishing standards for the terms and conditions of providing services that take into consideration the special needs of vulnerable groups such as women, children, the elderly, and persons with disabilities;

(iii) Making and enforcing market rules for the sector;

(iv) Monitoring economic and management performance of the regulated entities;

(v) Issuing, reviewing and canceling licenses (with respect to the viability of commercial arrangements);

(vi) Reviewing PPP agreements; and

(vii) Arbitrating disputes within the sector.

COST RECOVERY

A. User Charges and Other Revenues including revenue streams emanating from asset use, natural resources and development plans etc

42. Depending on the type of the PPP project and its likely financial performance, there can be several potential sources of revenue or income:

(i) Revenue solely from user charges if the project is financially viable;

(ii) Revenue from user charges plus government support if the project is marginally viable and such support is justified on social grounds;

(iii) Unitary/annuity type payments wherein the Government contracts to pay the private partner for providing the infrastructure and related services either an agreed fixed amount each year of operation or an amount based on the future situation (e.g., future traffic levels). Such payments can either be linked with user charges or can be independent of them;

(iv) Third party income (e.g. sale of electricity from energy generated at waste management plant, income from service areas on highways, toll roads)

43. For many infrastructure services such as transport and water supply, a user tariff-based PPP agreement is appropriate. Estimates of the initial tariffs and formulae for the subsequent tariff escalation during the concession period will be developed in the

feasibility study to ensure a proper or market acceptable rate of return based on an efficient operation. The tariff setting will have to reflect the following two frequently contradictory considerations:

(i) The need to fully recover the capital, operation and maintenance costs in order to ensure that the project is financially viable and that users, rather than general taxpayers, pay for the services; and

(ii) The need to take into account the ability of the users to pay the proposed tariffs and make the services affordable to them. If this affects the project's financial viability, the Government shall provide subsidy in the form of Viability Gap Funding.

44. For certain types of PPP projects, such as those without a direct revenue stream, or with a weak revenue base, or with a low demand, or with higher than acceptable risks, the feasibility study may recommend a system of annual unitary payments to the concessionaire based solely on outputs (i.e., the meeting of specific project targets by the concessionaire). This is also known as annuity based PPPs.

B. Viability Gap Funding

45. The Government will provide VGF for PPP projects that have a strong economic and social justification but fall short of financial viability because of affordability constraints imposed on tariffs. VGF will be an explicit subsidy (whether upfront or operational) that is performance driven (based on the private service provider achieving measurable outputs) and targeted towards socio-economically disadvantaged users or groups of users, such as women among others. The need of VGF, along with its form, will be established in the feasibility study; and announced in the tender documents.

46. VGF arrangements

A. New VGF structure and functions:

47. The VGF has been institutionalized. A dedicated VGF has been set up as a ring fenced Company under section 42 of the Companies Act, 2017 named as the "Public Private Partnership Support Facility (PSF)". The company is being established to manage the new VGF, thereby enhancing independence and improving corporate governance and transparency of the new VGF in its role and functions. Its role will also include risk management and monitoring the eligible projects initiated under the Sindh Public-Private Partnership Act, 2010, as amended or substituted from time to time, from the perspective of fiscal responsibility and compliance with applicable rules, regulations, and guidelines which may be issued and amended from time to time.

It shall be the responsibility of Government of Sindh to maintain funding availability at required commitment levels as annually or otherwise advised by the PSF to the Finance Department. PSF shall have the option to access funding from various sources for the new VGF, however primary responsibility shall be of the Government of Sindh through its annual budgetary allocations as advised by the PSF through the Finance Department. In order to ensure that required funding levels are maintained in the new VGF, the Sindh Finance Department shall ensure that funds are directly transferred to the PSF VGF account on the request of the PSF. Annual budgeted VGF funds allocation by Finance Department shall be transferred to the PSF VGF account by Finance Department on need basis.

PSF's independence shall beensured through a five member Board of Directors, of which at least three will be independent members in accordance with the requirement set out in the Companies Act, 2017 and equipped with relevant professional experience. The board of directors will elect an independent director as its chair.

The use of the PSF's new VGF facility to support any PPP project shall require prior PSF Board approval, and in case of approval of PSF, the PPP Unit shall make a recommendation to the PPP Policy Board for final approval. Post January1, 2022 the existing VGF facility shall mergewith New VGF managed by PSF. PSF shall be the exclusive deciding authority for providing any VGF support to PPP projects referred to PSF.

B. Existing VGF

48. The Sindh Government has an existing functioning VGF that is managed by the Sindh Finance Department through the Sindh Fund Management House setup within the Sindh Finance Department. The existing VGF shall continue to be managed by the Sindh Finance Department until January 1, 2022 after which it shall merge with the new VGF managed by PSF. All accounting, record keeping and data base management of all forms of Government support, VGF funding custodianship, reporting, liability and risk management and funds fiduciary management shall rest with the PSF.

49. The Government of Sindh shall however until January 1, 2022, ensure the following process for the use of the existing VGF and the new VGF under the control and management of PSF:

i) The existing VGF may only be used to support PPP projects approved by the Government through the PPP Policy Board under the PPP Act 2010 prior to January 1, 2022. This would include all existing approved and functioning PPP projects and new projects approved for VGF support prior to January 1, 2022.

ii) Government of Sindh shall continue to provide funding to the existing VGF to fulfil all commitments and obligations of the PPP project portfolio approved by the Government of Sindh prior to January 1, 2022.

50. Any new PPP project considered for VGF support, by the PPP Unit shall be submitted to PSF for VGF support. In the event PSF declines new VGF support for specific reasons, line department shall have the option through the PPP Unit, prior to January 1, 2022, to refer the project to the PPP Policy Board with the request of seeking funds from the existing VGF and providing full details and reasons as below:
i) why the PPP project has been declined funds by the PSF, and
ii) why the line department believes the PPP project should be provided support from the

existing VGF, and
iii) how the line department shall mitigate risks and address concerns raised by PSF.

51. In case of approval of PSF, the PPP Unit shall make a recommendation to the PPP Policy Board for final approval.

52. The final authority on new VGF usage would remain with PSF

53. Other recommended inclusions in PPP Policy/rules

54. Insurance Coverage

55. To reduce the impact of unforeseen/ contingent obligations that would require Government funding support to PPP projects, the private party to the contract should arrange insurance coverage to meet the risks described below. The cost of arranging this risk coverage would be a part of the agreed tariff and may have to be met from some element of annual subsidy support of the Government. This recurring cost would in most instances cushion the larger impact on Government fiscal resources in case of an unforeseen eventuality/incident.

56. The following Risks are recommended to be covered through insurances taken out by the concessionaire in relation to the PPP Project with the approval of PPP Policy Board.

57. Loss of Profit for any business interruptions by reason of circumstances beyond the control of either party. Such risks to be agreed and identified in the concession contract with defined formula for covering these costs

58. Expropriation and termination by either party, or consequential termination by reason of force majeure including unresolved political force majeure events. This would imply that concession contracts would have quantifiable costs for such events and Government contingent obligations are determinable and therefore insured amounts and costs also determinable for inclusion in tariff/user charge amount.

C. Project Development Facility

59. Government agencies in Sindh have capacity and resource constraints and find it sometimes difficult to develop PPP projects that deliver value for the Government and consumers and, at the same time, are attractive to private investors. To overcome this obstacle, the Government has established a PDF Fund. All PPP Nodes, which want to implement a PPP project in their sector or geographical area of responsibility, will have recourse to PDF Funds for project preparation.

60. Project preparation has the following objectives:

(i) Ensuring overall success of the PPP program;

(ii) Ensuring technical, economic and financial viability and environmental sustainability of PPP projects; with special reference to equator principle as well as gender equality commitments of the Pakistan government.

(iii) Designing sound contractual structures for PPP projects that make these bankable;

(iv) Minimizing and fairly allocating risks of PPP projects;

(v) Allowing informed decision making by the Government, based on good-quality feasibility reports that are supplemented by adequate social and gender analyses;

(vi) Enhancing competition and thereby ensuring success of tendering;

(vii) Providing the basis for contract negotiations;

(viii) Avoiding unnecessary future delays; and

(ix) Facilitating financial closure for PPP projects.

61. Given the complexity of PPP projects, external experts will be needed to provide advice during project preparation and transaction execution. To structure viable and bankable PPP projects, the PPP Nodes will have to recruit transaction advisors with proven track records in their field of expertise and with demonstrated ability to apply environmental and social safeguards, and gender equality principles in their work, However, the cost of such advisors is significant and may exceed the available budget. Recognizing the importance of adequate project preparation, the Government has established the PDF for feasibility studies and transaction execution advisory services. The PDF, which will be administered by the PPP Unit, will ultimately be a revolving fund, with the project preparation costs reclaimed from winning bidders.

PPP PROJECT LIFE CYCLE

62. The following five main phases can be distinguished in the life cycle of PPP projects:

(i) Project inception;

(ii) Project preparation (feasibility study);

(iii) Transaction execution (procurement of private partners); and

(iv) Construction, operation and transfer (development, delivery and exit).

(v) Monitoring and evaluation

A. Project Inception

63. The PPP Nodes in the line departments and local governments will identify and conceptualize potential PPP projects from their master plans and other planning documents. This phase will include an initial needs and options analysis to determine the best solution for developing the given infrastructure facility and/or providing the necessary infrastructure service, as well as an initial viability analysis. To help prepare the PPP projects and select the private sector partners, the PPP Nodes will recruit transaction advisors who will be selected on the basis of their track record in their field of expertise as well as a demonstrated ability to integrate environmental, social safeguards, and gender equality principles in their work. Prior to doing so, they will decide whether to fund the cost of these advisors from their own budget or the PDF. In the latter case, the PPP Nodes will submit a request for PDF funding through the PPP Unit to the PPP Policy Board. This activity is subject to the capacity building of the PPP nodes and unless sufficient evidence is evinced, PPP Unit shall help them identify the PPP Projects.

B. Project Preparation

64. The PPP Nodes will manage preparation of the PPP projects by the transaction advisors with active consultation of the PPPU for the early few projects. The preparation will consist of a feasibility study that includes environmental, social and gender analyses, supplemented by an initial environmental examination, environmental impact assessment (if required), risk analysis, assessment of the need for government support, a plan for the conduct of stakeholder consultations that identifies strategies to ensure participation of target groups, particularly women's organizations, determination of the PPP modality (project structuring), and drafting of tender documents including the PPP agreement. An important part of the feasibility study will be financial modeling to determine project bankability and affordability, including estimates of viability gap, if any. Another important activity will be stakeholder consultations.

65. Upon completion of the feasibility studies, the PPP Nodes will prioritize the identified PPP projects within their sectors and geographic areas, using criteria such as supply and demand gaps, social and economic benefits for women and men, financial attractiveness, risks and uncertainties involved, and readiness for implementation. The prioritized PPP project proposals will be submitted through the PPP Unit to the PPP Policy Board.

66. The PPP Unit will exercise quality control by reviewing the viability of the PPP project proposals and the completeness of their documentation, as well as their compliance with the objectives and principles of the PPP Policy. PPP projects that pass this review will be prioritized by the PPP Unit across sectors and the province, taking into account Sindh's development objectives, and submitted to the PPP Policy Board for approval. The approved PPP projects will be included in a provincial priority list and widely publicized by the PPP

Unit.

The PPP Unit shall continue to develop initial PPP Projects independently or with active consultation of the PPP Nodes as the case may be, to create some standards of the transactions and set some basic parameters of project development and contractual arrangements which are otherwise absent in here. Depending upon the competent authority which is PPP Policy Board in this case, the Project development assignment can be relegated to PPP Unit during the early PPP project developments to strengthen the capacity and creating some benchmarks for PPP projects. Requests for government support through VGF, if required, will be an integral part of the PPP project proposals submitted by the PPP Nodes. The PPP Unit will review all requests with budgetary implications and assess their justification and eligibility, and analyze the fiscal impact of the related direct and contingent liabilities. Based on this review and analysis, the PPP Unit will make a recommendation to the PPP Policy Board. If approved, the PPP Unit will make the necessary arrangements for including such support in the Annual Development Program.

C. Transaction Execution

67. In accordance with the Public Procurement Regulatory Authority Rules private partners for all PPP projects will be selected through transparent and competitive tendering, using an appropriate process of pre-qualification and bidding. Direct negotiations to select private partners will not be allowed and negotiations are admissible only with the interested developers who have submitted their technical and financial bids subject to the equal opportunities to all the interested bidders. After obtaining approval for the PPP project the PPP Node will publish a notice inviting private companies and consortia of such companies to submit pre-qualification applications. Based on appropriate pre-defined criteria such as legal requirements, technical capability as documented by previous experience with similar projects, and financial capability, the PPP Node will evaluate all pre-qualification applications to determine which among the companies and consortia meet these criteria. If less than two applicants are pre-qualified, the PPP Node will analyze the reasons for this outcome, improve project structuring, and re-initiate the pre-qualification process for additional participants.

68. To provide clarifications to bidders and discuss the terms and conditions of the draft PPP agreement, the PPP Node will conduct a pre-bid conference and will issue supplemental notices, as necessary. If only one valid bid is received, the PPP Node will evaluate it. Depending on results of the evaluation, the PPP Node will recommend through the PPP Unit to the PPP Policy Board whether to negotiate the contract with the sole bidder or withdraw the PPP project from the market and undertake it in the traditional way by the public sector.

69. Bid evaluation of a PPP project shall be carried out by a Technical and Financial Evaluation Committee to be notified by the Government of Sindh with the approval of Chief Secretary, and will be carried out in two phases. First, the technical, operational, environmental and commercial soundness of the bids received will be assessed vis-à-vis the requirements, criteria, minimum standards, and basic parameters specified in the

tender documents, and non-compliant bids will be rejected. The responsive bids will be evaluated in the second phase from the financial viewpoint. The evaluation will be based on a single parameter specified in the tender documents. Depending on the type of the PPP project, the following bid parameters may be used for the financial evaluation:

(i) Lowest proposed tariff, toll, fee or charge at the start of operation of the project if a parametric formula for periodical tariff adjustment is prescribed in the tender documents;

(ii) Lowest present value of the proposed tariffs, tolls, fees and charges for the period covered by the PPP agreement if there is no such formula;

(iii) Lowest present value of payments from the Government;

(iv) Lowest present value of VGF subsidy to be provided for the period covered by the PPP agreement;

(v) Highest present value of the proposed payments to the Government, such as concession fees, lease/rental payments, fixed/guaranteed payments or variable payments/percentage shares of revenues for the period covered by the PPP agreement;

(vi) Highest Quote bid price mechanism for the projects where government land is being offered as the assets for the projects like resort projects and the bidder with highest quoted bid (the base price plus the best premium) while keeping all the other factors of regulatory and environmental nature in constant etc; or

(vii) Any other appropriate single financial bid parameter approved by the PPP Policy Board upon recommendation of the PPP Node or PPP Unit.

70. After completion of the bid evaluation, the PPP Node will announce bid evaluation report in accordance with PPRA Rules. The PPP node thereafter, shall submit through the PPP Unit to the PPP Policy Board a bid evaluation report, including a recommendation on award of the contract and a request for approval of VGF, if any. Subject to approval by the PPP Policy Board, the PPP Node will announce results of the bidding and issue a notice of award to the selected private partner.

71. Contract negotiations between the PPP Node and its private partner will focus on terms and conditions not specified in the tender documents. No post-bid changes will be allowed during contract negotiations in those terms and conditions, which have been described in the tender documents as binding and have formed part of the bid evaluation. After the signing of the PPP agreement, the private partner will endeavor to achieve financial close within the period specified in the tender documents, but not exceeding 12 months.

D. Construction and Operation

72. The PPP Node will be responsible for monitoring and evaluating the PPP project during its construction and operation to ensure its conformity with the plans, specifications, performance standards, and tariffs in the PPP agreement. The PPP Node will submit annual reports on the PPP project to the PPP Unit specifically ensuring that operation and maintenance of the resulting infrastructure, goods and services will include provisions that shall promote equall access by all targeted users.

PPP PROJECT PIPELINE

A. Pilot PPP Projects

73. The Government recognizes that even with a sound policy, legal, institutional, risk management and regulatory framework, private sector investors will come only if there are attractive PPP projects. The first step towards achieving this objective is the preparation and periodic updating of long-term sector strategies and master plans, which will outline the necessary physical expansion to meet the forecast demand. In line with their policy making and planning functions, this is the responsibility of the line departments and local governments. These sector strategies and master plans will form a solid basis for screening infrastructure projects and selecting the best PPP candidates.

74. Given the emphasis the Government is placing on PPPs to meet Sindh's infrastructure needs, all projects in the sectors not below the value of Rs. 100.00 million (a reasonable estimate may be made compulsory to accommodate advisor's fees) should first be considered for implementation on a PPP basis. If the concerned departments propose that a project be undertaken under traditional public procurement using public funds, they should justify their choice and demonstrate that this option would be more cost-effective for the Government or that the project does not meet selection criteria for PPPs. It should be noted that time saving is generally not a good justification to undertake a project in a non-PPP manner.

75. To reduce uncertainties for investors, the PPP projects will be thoroughly prepared before the selection of private sector partners by undertaking feasibility studies that include environmental, social, and gender analyses, acquiring the necessary land, and obtaining the necessary permits and approvals. There is ample evidence that shifting the responsibility for these preparatory activities to the private sector results in (i) land speculation; (ii) weak competition as each bidder has to prepare its own feasibility study; (iii) high bid prices as bidders include significant risk margins; and (iv) major delays in contract negotiations and financial closure, or even inability to achieve it, as there are too many uncertainties and issues left open in the tender documents.

76. Selection of the private sector partner will start only after the PPP project has been thoroughly prepared. It will be a transparent process consisting of prequalification and bidding. Direct negotiations will not be allowed as in the absence of competition, the Government would not know whether Sindh is getting the best value for its money. To facilitate the selection process, model tender documents for different sectors and types

of PPP projects will be developed. 65. Doing the first transactions the right way is essential for boosting investors' confidence in the PPP Policy and its implementation. The Government will therefore pilot suitable PPP projects in several sectors parallel to the development of the enabling PPP framework in order to demonstrate its application and benefits. When selecting the pilot projects, priority will be given to financially attractive projects of medium size with manageable risks, which require upfront investment by the private sector. If some of these projects are economically viable but financially marginal because of the current low user charges, there will be a commitment by the Government to provide VGF support until the charges have been brought up to full cost-recovery levels.

66. Preparation and execution of the pilot projects will be conducted in full compliance with the following main principles of the enabling PPP framework:

(i) A clear separation of the roles of planner and regulator (the Government) and those of owner and operator (private sector partners);

(ii) No direct negotiations with the prospective private sector partners;

(iii) Preparation by the Government of feasibility studies with environmental, social and gender analyses, including the PPP project structuring and risk allocation, prior to tendering;

(iv) Decision on the Government's direct and/or contingent support also prior to tendering;

(v) Indication of such support, if any, in the tender documents; and

(vi) Use of a transparent two-stage process for tendering (pre-qualification and bidding).

67. Depending on its type, the typical schedule for a pilot project will consist of about 6-9 months for the recruitment of transaction advisors, 6-12 months for the feasibility study and 9-12 months for the transaction execution from pre-qualification to bidding to contract award and signing, or 21-33 months in total. This could be reduced to 16-26 months if the sole sourcing method is used to directly appoint the transaction advisors.

B. Unsolicited Proposals

68. PPP projects are generally classified as solicited or unsolicited. Solicited projects are initiated by public sector institutions and are part of the Government's priority programs. By contrast, unsolicited projects are proposed by the private sector. All unsolicited proposals will be treated on a case-by-case basis, with the view to selecting projects that demonstrate genuine innovation and furthering of public policy. The following principles will be followed:

(i) A private company may propose at its initiative a PPP project to the PPP Node in the line department or local government or to the PPP Unit, provided the project is not included in Sindh's priority list and is economically and financially feasible with or without any VGF support.

(ii) Such unsolicited proposal should be accompanied by an independently verified feasibility study encompassing all aspects of standardized documents developed by the PPP Unit.

(iii) The PPP Node will consider all technical, financial and other relevant aspects of the proposal, and may modify the same in consultation with the project proponent.

(iv) The PPP Node will request the project proponent to submit details of its technical, commercial, managerial and financial capability.

(v) If such proposal is found feasible for PPP mode, the PPP Node or the PPP Unit as the case may be, shall send it to the PPP Unit for approval of its eligibility for PPP procurement from PPP Policy Board, following the same guidelines and procedures for all PPP projects, including its Value for Money analysis. If the unsolicited proposal is approved, comparative bids will be invited through advertisement without disclosing the name of the initiator. The initiator will be given five percent additional weighting on the combined secured score in evaluation.

(vi) If no valid comparative bids are received, the PPP Node will negotiate the PPP agreement with the project proponent.

CONTRACTUAL SAFEGUARDS

A. Project Preparation and Construction

69. Although it is expected that PPP projects will be executed under various types of contractual structures, the Government will insist in virtually all such contracts that the public interest be protected through appropriate contractual mitigation techniques to ensure value for money throughout the project life cycle. These techniques will involve

some or all of the following:

(i) Prior to the award of the contract, a transaction advisory team will assist the government in preparing the feasibility study inclusive of environment, social and gender analyses, drafting the request for proposals and negotiating the PPP agreement with the private sponsor. The transaction advisory team will include a legal advisor, engineers and financial analysts experienced in PPP projects;

(ii) An independent engineer will be integrated into the project monitoring structure. The independent engineer will oversee the technical aspects of the project, review; if jointly appointed by the lenders and the Government, approve loan disbursements; and monitor operation and maintenance to ensure that the project company is complying with the performance standards of the PPP agreement; and

(iii) Construction of the facilities will generally be carried out under internationally recognized fixed- price turnkey engineering-procurement-construction contracts. The contracts may need appropriate enhancements such as performance bonds, bank guarantees and, if necessary, guarantees from the contractor's parent company to ensure fulfillment of the contractor's obligations to the project company.

B. Project Sponsors

70. The Government will include in all PPP agreements appropriate safeguards requiring that the chosen private sponsors will be contractually committed to the project at least until the construction is successfully completed and the project has entered into commercial operation. This will mean that once committed to the project, the sponsor will not be allowed to undergo changes in its corporate structure which alter its technical and economic capacity to complete the project. It will also not be authorized to transfer its shares in the project company to third parties until at least the project is commissioned and operational.

C. Political and Termination Risks

71. For many investors and private lenders, the political risks associated with PPP projects increase the minimum expected rate of return and spread on the long-term loans. This increases the costs of financing and creates added pressure on governments to offer guarantees and other credit enhancements to make the projects financially viable. The Government therefore will in certain long-term PPP agreements such as BOTs, BLTs or other modalities mentioned above involving private investors enter into Direct Agreements with project lenders to provide them contractual step-in rights and extended cure periods to rectify defaults by the project companies before the PPP agreement is terminated. In addition, in such circumstances where the default cannot be reasonably cured within such cure period, the Government will also provide opportunities to auction the remaining term of the PPP Agreement to third parties, or if no reasonable market based solution is possible,

may assume all or a part of the outstanding loans so that the lenders will not be unfairly penalized for the actions of the project sponsors.

72. The Government will also share some of the project risks, which cannot be adequately addressed by either the sponsors or private insurers. For instance, force majeure risks such as civil strife and war, which might be difficult to insure by the sponsors, may have to be covered fully by the Government in present circumstances. Other force majeure risks that can be insured will be expected to be covered by the sponsors' insurance and in some cases will be shared with the public sector. Having said it all, it is imperative that the requisite contract agreement shall determine the allocation of risk, and no developer/ investor shall resort to Sindh PPP Act 2010 or this policy for seeking a risk mitigation measure. The developer shall bind himself/herself in the relevant PPP Agreement or other contractual document for accepting certain risks or seeking government remedy for the risks, later has assumed.

73. Termination of the contract for convenience of the public sector is also a risk that will require the Government to fully compensate the private party, its shareholders and lenders. This compensation will be based on an agreed formula and rate of return set forth in the financial model in the PPP agreement.

D. Dispute Resolution

74. Because of the long-term nature of PPPs, the Government acknowledges the importance of incorporating in each PPP agreement informal dispute settlement mechanisms. Appropriate clauses will be included to ensure that the parties resort to mediation and negotiation before resorting to more formal adversarial dispute resolution procedures. This will expedite the resolution of disputes and provide the parties with an effective way of resolving any disputes in a fair and equitable manner consistent with the PPP Law. In addition, arbitration clauses will be included in all PPP agreements to protect the rights and obligations of the parties.