

**PUBLIC PRIVATE PARTNERSHIPS (PPP)**  
**Practice and Regulatory Policy in Kenya**

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for  
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## **Acronyms**

APOPS	Asset Procurement and Operating Partnership Systems (South African Department of Public Works)
BEE	Black Economic Empowerment (RSA)
BOO	Build Own Operate
BOT	Build Operate Transfer
BOOT	Build Own Operate Transfer
CG	Consultative Group
DBFO	Design Build Finance Operate Transfer
ESTU	Executive Secretariat and Technical Unit
FY	Financial Year
GDP	Gross Domestic Product
GDP	Gross Domestic Product
GOK	Government of Kenya
IPO	Initial Public Offer
IPP	Independent Power Producer
Ken Gen	Kenya Electricity Generation Company
KERAPA	The Kenya Railways Pensioners Association
KPA	Kenya Ports Authority
KPLC	Kenya Power and Lighting Company
KRC	Kenya Railways Corporation
KRSRBS	Kenya Railways Staff Retirement Benefits Scheme
Ksh	Kenya shilling
MDGs	Millennium Development Goals
MoTC	Ministry of Transport and Communications
MOU	Memorandum of Understanding
MRLGH	Ministry of Regional and Local Government and Housing (Namibia)
NGOs	Non Governmental Organisation
PAT	The Principal Agent Theory
PFI	Private Finance Initiative
PPP	Public Private Partnerships
PRPC	Parastatal Reform Programme Committee
PSC	Public Sector Comparator
PSP	Private sector participation
RSA	Republic of South Africa

## **Executive Summary**

The Government is increasingly seeking to develop financing mechanisms, which bring together the public and private sectors, not only to control budgetary expenditure but also to pool these two sectors' specific know-how. This form of cooperation is commonly referred to as Public Private Partnerships (PPPs), which may be formally defined as "...institutional relationships between the state and the private for-profit and/or the private not for-profit sector, where the different public and private actors jointly participate in defining the objectives, the methods and the implementation of an agreement of cooperation". Public procurement and full privatisation lie at the opposite ends of a continuum defined by the extent of service obligations imposed, and ultimate ownership of assets. Though closely related, there are differences between public procurement, PPPs and full privatisation. Often the criteria used to choose the private partner for PPPs are more complex than just who offers the best price and who conforms to the technical specifications.

There is no unified theoretical basis for PPPs. However, among the various theories one may point out the Principal –Agent framework given the specific nature of risks existing in most PPP projects. Most of these risks are uninsurable. Indeed, the probability of risk materialization directly depends on the PPP partners' behaviour. Consequently, the risk allocation should be treated within the transaction. The Principal – Agent Theory (PAT) deals the most with the risk allocation topic. By modelling the relation between an informed party (the Agent) and an uninformed one (the Principal), the PAT highlights two problems rising from the information asymmetry: adverse selection and moral hazard.

In terms of best practices, Governments must however overcome a number of challenges in implementing PPPs. These include developing and establishing strong legal and regulatory frameworks that can clarify the legal authority to grant concessions, the procurement process, the contribution from the public authority of assets that can make the project viable and the rebalancing of tariffs which will make the project viable from a financial point of view. In addition, there must be political commitment to give confidence to the partners to make investments. Effective public administration is also important preferably through a dedicated central PPP unit located within Government that can oversee the whole PPP process and has cross cutting authority over all Ministries.

Currently, PPPs are being discussed as one of the three crosscutting issues under the Government's Private Sector Development Strategy 2006-2010. In addition, work on establishing a PPP Unit is currently underway within the Ministry of Finance. The two key Acts of Parliament that variously spells out the legal framework for PPPs in Kenya are the Privatization Act No. 2 of 2005 which after some delay was given Presidential Assent on 13<sup>th</sup> October 2005, and the Public Procurement and Disposal Act, No 3 of 2005 assented on 26<sup>th</sup> October 2005.

The general euphoria around policy encouragement for PPPs ignores a range of concerns about PPPs based on public interest considerations. Most fundamentally, there are questions about whether PPPs should be unambiguously preferred to public sector investment and operation of

services, and the need to evaluate the social and economic impact of the risks and future liabilities created by PPPs. There are a number of specific public interest concerns: about the way PPPs transfer the costs of paying for investment from present generation to future generations; about the dangers of fragmenting, casualising and worsening conditions of employment of soon to be PPP'd public service workers; about the real transparency of the processes by which PPPs are likely to be effectively established, operated; and about the comparative economic consequences of PPPs and public sector options.

In our conclusions we state that the issues discussed in the report raise significant challenges to conduct of successful PPPs in Kenya. The complexity of such arrangements and the high costs involved is enough cause for the Government to take a careful approach to PPPs. It should also recognise that PPPs pose many of the same problems inherent in procurement or privatisation and are not a panacea for development. We therefore recommend that the Government must determine clear operational guidelines with respect to acceptable forms of PPPs and their prioritisation, procedural clarity on the basic steps in establishing PPP projects, basic approaches to risk allocation, value for money and principles around the provision of guarantees and financial and budget evaluation criteria.

In establishing the PPP Unit there are several issues that must be tackled. Firstly, there is a need to review, analyse, and recommend draft amendments to existing legislation clarifying the power and authority of local and central Governments as well as public enterprises to enter into long-term contractual arrangements with private sector service providers. Secondly, there is a need to develop minimum standards and regulations governing PPP contracts. Thirdly, the PPP Unit will need to establish policies and procedures for preparing and packaging projects, and ensure quality control over these activities. Fourthly, capacity building in project planning, co-ordination and monitoring of PPP projects among public officers is another essential element required to strengthen the implementation capacity. Fifthly, whereas a comprehensive policy, legislative and institutional framework has already been passed in Kenya to serve the needs of the Government's privatisation programme there is need to blend a framework for PPPs into that for the privatisation programme with suitable enhancements to cater for the formal and institutional needs of a PPP programme.

# Public Private Partnerships (PPP) Regulatory Policy in Kenya

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## 1. Introduction

### 1.1 The objectives of the study

In order to maintain a high level of economic investment, Governments all over the world are increasingly seeking to develop financing mechanisms, which bring together the public and private sectors, not only to control budgetary expenditure but also to pool these two sectors' specific know-how. The increasing involvement of the private sector is also part of the more general change over the last decade in the role of the State in the economy, characterized by a move from the role of direct operator to one of organiser, regulator and controller of economic activities. This form of cooperation is commonly referred to as Public Private Partnerships (PPPs).

The objectives<sup>1</sup> of this study are to review the status of PPPs in Kenya and to discuss comparative approaches to their design and identify best practices for PPP frameworks. Secondly, it was intended to propose appropriate mechanism and regulatory approach for auditing performance and cost-effectiveness of PPPs taking in consideration competition law and policy as well as consumer protection and other regulatory policies that may be relevant for the proposed framework for PPPs. Thirdly, there was a requirement to conduct an audit on the appropriate procurement issues that arise from existing practices in PPPs and to propose appropriate structural, legal and policy reforms that should inform the adoption of PPP frameworks in Kenya.

### 1.2 Methodology

In the course of undertaking this study, two main approaches were used: desk study on the theory and practice of PPPs, and interviews and consultations with key informants.

#### 1.2.1. Desk Research on PPP

Various documents were studied and reviewed in this study, most of which provided valuable information on the subject of PPPs in theory and practice particularly on the two case studies discussed in the paper. Key to those documents reviewed was the Procurement Act, Monopolies and Price Control Act and documents currently under revision with regard to its amendment. These documents are detailed in the references to this study.

#### 1.2.2. Interviews and Consultations

The author held consultations with members of the private sector, Ministry of Finance (Investment Department and Procurement Directorate) and specialists in the field of government investments with the aim of obtaining current information especially on the progress towards implementation several laws pertinent to PPPs particularly the recently enacted Government Procurement and Disposal of Assets Act and Privatization Act.

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<sup>1</sup> See Terms of Reference for this study attached as Annex 1.

### **1.3 Structure of the Paper**

The rest of this paper is structured as follows: Chapter 2 defines PPPs and then presents a brief historical and theoretic framework for PPPs and briefly presents how PPPs are implemented in other parts of the world, both in the developing countries of Africa and the developed countries. It also presents key issues in adopting best practices in implementing and regulating PPPs. Chapter 3 discusses the current state of PPP in Kenya from a comparative perspective of the current regulatory framework and implementation of PPPs with the received best practices. Chapter 4 presents some issues and measures that may be considered in formulating changes in the current legal and institutional framework for PPPs in Kenya. Chapter 5 presents some important lessons from Africa derived from implementing PPPs while Chapter 6 concludes the study and summarises our recommendations for improving the policy and regulatory framework for PPPs in Kenya.



## 2. Theory and Practice of PPPs

### 2.1. Defining PPPs - Public Procurement, PPPs and Privatisation

PPPs may be defined as "...institutional relationships between the state and the private for-profit and/or the private not for-profit sector, where the different public and private actors jointly participate in defining the objectives, the methods and the implementation of an agreement of cooperation"<sup>2</sup>. PPPs are a variation of Privatization in which elements of a service previously run solely by the public sector are provided through a partnership between the government and one or more private sector companies. Unlike a full Privatization scheme, in which the new venture is expected to function like any other private business, the government continues to participate in some way. These schemes are sometimes referred to for short as PPP or P3.

Public procurement and full privatisation lie at the opposite ends of a continuum defined by the extent of service obligations imposed, and ultimate ownership of assets. Though closely related, there are differences between public procurement, PPPs and full privatisation. Often the criteria used to choose the private partner for PPPs are more complex than just who offers the best price and who conforms to the technical specifications. PPPs emphasise the actual delivery phase of the project, while under a simple tender, government bears the responsibility for specifying exactly what it needs. When procuring large infrastructural projects e.g. highway projects, governments generally have two options for underwriting capital expenditures: tax revenues or user fees. The tax-based approach has traditionally been favoured in the United States, Northern Europe and Japan, and involves using general tax revenues, earmarked fuel taxes or other dedicated taxes to pay for projects. Southern European nations such as France, Italy, Portugal, and Spain – together with many developing nations – have favoured the use of user fees collected in the form of tolls to finance their infrastructure needs.

PPPs presents as a middle case between public procurement and privatisation. They involve a more open relationship in which business is encouraged to propose alternatives rather than mere provision of a service and the private sector operator will often need to design the best solution given the government's specifications. Other things would include offering technical expertise and provision of viable financial arrangements for the project, and most critically, the bearing of the associated operational risks.

As illustrated in Table 1 below, the criteria used to choose the private partner in PPPs are often more complex than mere consideration of who offers the best price and who conforms to the technical specifications required for the project.

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<sup>2</sup> See Jütting, J (1999), pg. 1. Compare this with SAIIA (2005), pg. 12 which defines PPPs as "a contract between a public sector institution and a private party, in which the private party assumes substantial financial, technical and operational risk in the design, financing, building and operation of a project". In both examples of importance is the issue of long-term partnership and succinct specification of obligations of both parties particularly with regard to distribution of risks.

**Table 1: The Public Procurement, PPP and Privatisation Continuum**

	<i>Public Procurement</i>	<i>PPP</i>	<i>Full privatisation</i>
<b>Definition</b>	<ul style="list-style-type: none"> <li>Supply by the private sector of works, goods or service as defined by the public authority.</li> </ul>	<ul style="list-style-type: none"> <li>PPPs introduce private sector efficiencies into public service by means of a long-term contractual arrangement. They secure all or part of the public service, call upon private funding and private sector know-how.</li> </ul>	<ul style="list-style-type: none"> <li>Privatisation means transferring a public service or facility to the private sector, usually with ownership, for it to be managed in accordance with market forces and within a defined framework.</li> </ul>
<b>Main Features</b>	<ul style="list-style-type: none"> <li>Contracting authority establishes clearly what is to be built, how and by what means.</li> <li>Invitations to tenders are accompanied by very detailed technical specifications regarding the type of work being procured.</li> <li>Price quote is the single most important criterion in the evaluation of bids</li> <li>The procurement process is short-term in nature and does not involve long-term occupancy of infrastructure assets, and thus does not lay emphasis on the operational phase of the project.</li> </ul>	<ul style="list-style-type: none"> <li>Contracting authority establishes the specifications of a project and leaves to the private sector the responsibility of proposing the best solution, subject to certain requirements.</li> <li>Price is one of the many criteria in the evaluation of bids. A lot of emphasis is on the technical and financial capability of the bidder, financial arrangements proposed, and the reliability of technical solutions used.</li> <li>Given the long duration of the concession period, emphasis is on the arrangements proposed for the operational phase.</li> </ul>	<ul style="list-style-type: none"> <li>Privatisation authority prepares the divestment plan.</li> <li>Involves transfer of ownership to the private sector.</li> <li>Is generally a complex transaction with carefully designed contracts and a multi-stage competitive tender process.</li> <li>Generally, the public sector withdraws from management of the entity on privatisation.</li> <li>Almost all risks are borne by the private sector.</li> </ul>

Source: Adapted from SAIIA (2005), Table 1, and pg. 13

More emphasis is placed on ability to deliver the service or infrastructure. In the case of a simple tender, the government bears the responsibility for specifying exactly what is required. In the case of a PPP, the private operator may be required to design the best solution given the government's specifications, offer technical expertise and provide viable financial arrangements for the project, and to bear the associated operational risks.

In contrast, privatisations of public utilities usually occur within a regulatory environment that can impose detailed service and investment obligations, such as rollout schedules to rural areas or price caps for poor consumers. In reality, privatisation and PPPs exist on a continuum defined by the extent of service obligations imposed, and ultimate ownership of assets.

## **2.2. Historical perspectives of PPPs**

Historically, the most common application of PPP in Europe were started in the transport and urban water supply sectors where users were easily identified and revenue streams at least partly supported the investments. The Irish Republic followed the European and British developments in supporting the concept of PPP as a matter of policy and focused on time to delivery savings and capacity constraints in the economy, including labour skills and infrastructural deficit. The Exchequer in Ireland has considerable scope to provide infrastructure from public funds, in contrast to the UK, so that the budget constraint imperatives for PPP adoption are not as strong. The utilisation of PPP models in the USA is more limited in comparison with the European activity. The most common funding model used for infrastructure development in the USA is by way of bond issues from stakeholder partners. Experience in the USA shows up problems when Federal taxation law and State regulations are not favourable to aspects of PPP implementation, and one objective of the policy framework is to seek rationalisation of the legislative and regulatory environment.

In Australia, the birthplace of PPPs was in Victoria, which followed closely both variants of the UK model for PPP. In the developing countries, Malaysia can be mentioned. From what is known, the main applications with PPPs are in the transport and water and wastewater sectors, in common with other international experience. In order to reduce the burden on government funds, most of the PPPs follow the Build Own Operate Transfer (BOOT) models. The Government process for PPP schemes normally involves selection of at least two potential consortia from the private sector – Government selects the consultants, contractors and financiers to be involved. The Government provides a specification of its service needs, and allows the consortia to develop proposals to meet these needs. The Malaysian Government experience with their version of PPPs is mixed. Toll roads have been developed under the model, apparently successfully. Water supply schemes that were privatised have met with community rejection when the private sector dealt directly with the customers.

Transportation PPPs were pioneered in Europe and by the 1990s, two types of partnership approaches had evolved. Under the more common “real toll” scenario, private concessionaires arrange financing, construct roadways, maintain them, service their debt, and derive revenue from tolls collected directly from motorists. One of the main benefits of the “real toll” concession approach is that it enables governments to tap into sources of private capital and avoid using public monies to build highways. Real toll PPP precedents established in France and Spain have been replicated in such diverse locations as Iceland, Malaysia, Republic of South Africa, Croatia , Australia , China and Brazil . An equally wide range of countries is now poised to launch ambitious surface transport partnership projects, including Poland, Romania, Lebanon, Egypt, and Austria.

As PPPs have become more common, many governments have become eager to capitalize on the increased efficiencies of the private sector and have found that private developers deliver greater

value for money. This has precipitated the “shadow toll” approach initially adopted in the United Kingdom, where governments award concessions to build-operate-maintain toll-free highways and then compensate the investors based on roadway usage and/or availability of those facilities. Privately financed shadow toll highways are currently operational in the United Kingdom, Finland, Spain and Portugal. In the United States, the private sector historically had an important role in highway construction operation and financing. Although the role of the private sector in highway financing and operation declined in the mid-part of the 19th century, in the late 1980’s, private-sector involvement in these cases reemerged.

### **2.3. Theoretical framework for PPPs**

There is no unified theoretical basis for PPPs. However, among the various theories one may point out the Principal –Agent framework<sup>3</sup> given the specific nature of risks existing in most PPP projects. Most of these risks are uninsurable. Indeed, the probability of risk materialization directly depends on the PPP partners’ behaviour. Consequently, the risk allocation should be treated within the transaction. The Principal – Agent Theory (PAT) deals the most with the risk allocation topic. By modelling the relation between an informed party (the Agent) and an uninformed one (the Principal), the PAT highlights two problems rising from the information asymmetry: adverse selection and moral hazard. Both of them lead to higher risk in the realization of the project outcome. The question is how to allocate efficiently these risks between partners in the reference (complete) contract. The target followed in the determination of risk allocation criteria is the total cost minimization. This must maximize the Principal’s utility. The analytical process followed by the PAT consists in maximizing the Principal’s utility subject to the Agent’s participation and incentive constraints. The respect of these two constraints must permit both partners to improve their situation, compared to a situation in which only one constraint would have been taken into account. As Laffont & Martimort [2002] point out, “incentive and participation constraints define the set of incentive feasible allocations” (p.30). Both risk allocation criteria enounced by the PAT come from these two constraints.

In the PAT framework, the Agent’s effort is not observable. At the same time, the Agent’s behaviour is at the root of the performance. In order to assure a certain level of performance, the Principal should give the Agent incentives to perform. The incentive constraint should be tackled. The authors belonging to the PAT concentrate on the imposing of potential cost overruns on partners as an incentive device. The payment the Agent receives from the Principal depends on his performance. There are several general conclusions on PAT: Firstly, the risk should be allocated to the Agent to the extent he does manage the risk. Secondly, risk should be allocated to the least risk averse partner in order to minimize the overall risk-bearing cost. In the Principal-Agent literature, the Agent is most of time supposed to be risk averse whereas the principal is supposed to be risk neutral. Thirdly, the Principal should support risk in order to minimize the overall risk-bearing cost.

## **2.4. PPPs in Africa – Practice and perceived Benefits**

### **2.4.1. Why PPPs?**

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<sup>3</sup> For a recent analysis that uses the PAT framework for PPPs with an emphasis on risk allocation in the defence industry see Oudot, Jean-Michel (2005). A presentation uses “Natural selection model” commonly applied to theory of evolution in discussing PPPs in higher education in Republic of South Africa (see Mabizela, M (2005).

By expanding the private sector role, public agencies are able to tap private sector technical, management and financial resources in new ways to achieve certain public agency objectives such as greater cost and schedule certainty, supplementing in-house staff, innovative technology applications, specialized expertise or access to private capital. On the other hand the private partner can expand its business opportunities in return for assuming the new or expanded responsibilities and risks. Some of the primary reasons for public agencies to enter into public-private partnerships include:

- Accelerating the implementation of high priority projects by packaging and procuring services in new ways;
- Turning to the private sector to provide specialized management capacity for large and complex programs;
- Enabling the delivery of new technology developed by private entities;
- Drawing on private sector expertise in accessing and organizing the widest range of private sector financial resources;
- Encouraging private entrepreneurial development, ownership, and operation of highways and/or related assets; and,
- Allowing for the reduction in the size of the public agency and the substitution of private sector resources and personnel.

PPPs provide benefits by allocating the responsibilities to the party – either public or private – that is best positioned to control the activity that will produce the desired result. With PPPs, this is accomplished by specifying the roles, risks and rewards contractually, so as to provide incentives for maximum performance and the flexibility necessary to achieve the desired results.

Hence using PPPs to deliver services are perceived to bring benefits that include expedited completion compared to conventional project delivery methods, project cost savings, improved quality and system performance from the use of innovative materials and management techniques, substitution of private resources and personnel for constrained public resources; and, access to new sources of private capital. Activities that can be included in such partnerships are varied and can be combined. PPPs can be applied to a large range of services. These include project conceptualisation and origination, design, financial planning and finance, construction, operation, maintenance, toll collection; and, programme management. These activities are typically bundled into contract packages reflecting the public agency's objectives related to schedule and cost certainty, innovative finance, or transfer of management and/or operational responsibility.

In Africa<sup>4</sup>, PPPs began only in the mid- to late-1990s. To date PPPs have been used mainly to make improvements to economic (physical) infrastructure, such as telecommunications, electricity and water. However, in recent years, PPPs have also been used to improve social infrastructure, such as health and education, and other services (garbage collection, agriculture extension services, etc). Traditionally, these services, especially in Africa, have been provided by the public sector. This is mainly because most of them require large capital

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<sup>4</sup> The figures in this section are obtained from ADB (2002).

outlays, and have a long gestation period. Moreover, because of social considerations their pricing tends to be inflexible.

Between 1990-1998 Africa accounted for about US\$14 billion of the total investment of US\$496 billion made in PPP projects in developing countries. This compared unfavourably with US\$237 billion (or 47.8 percent of the developing country total) for Latin America and the Caribbean, US\$147 billion (29.6 percent) for East Asia and the Pacific, and US\$38 billion (7.7 percent) for South Asia. The low figure for Africa is thrown into sharper relief given that infrastructure investment requirements in Africa are estimated at between 5-6 percent of GDP, which is equivalent to about US\$250 billion over the next ten years. Given the paucity of public funds, African countries will increasingly depend on private funding for the development of services traditionally provided by the public sector. Estimates suggest that Africa requires infrastructure investment of 5 to 6 percent of GDP per year. It is estimated that African countries will require about US\$18 billion in infrastructure financing, or approximately 6 percent of GDP, each year this decade. Neither the public sector nor the multilateral development institutions have the capacity to provide more than a small fraction of this investment. If African countries are to get the economic and social infrastructure and other services they need, then the private sector, working in partnership with governments, must play a leading role in bridging the resource gap.

#### **2.4.2. PPPs in Republic of South Africa (RSA)**

Republic of South Africa (RSA) has the greatest cumulative experience of public-private partnerships in Africa, with over 50 such partnerships in development or implementation at national or provincial level, and 300 projects at municipal level, between 1994 and 2005<sup>5</sup>. The South African National Treasury, the key ministry that approves these deals, has built on almost a decade of PPPs, and has developed a *PPP Manual* and *Standardised PPP Provisions* to guide all projects of this nature.

The *PPP Manual* refers to two specific types of PPPs: where the private party performs a function usually carried out by government, such as providing water or maintaining a road; or where the private party acquires the use of state property for its own commercial purposes; or a hybrid of the two. Payment could involve the institution paying the private party for the delivery of the service; or the private party collecting fees or charges from users of the service; or a combination of these. This partnership involves locking in long-term collaboration between both parties to share the costs, rewards and risks of projects — all the possibilities that things could go wrong — unlike the once-off transaction involved in public procurement (where government buys goods and services like offices, vehicles and computer maintenance) or full privatisation (where government sells assets to the private sector).

The RSA experience suggests that PPPs are complex, demanding and time-consuming but that under the right conditions, and in the right sectors, they can offer significant benefits to government, the private sector and consumers. They have been generally more successful in sectors such as ports, telecommunications, and transport and eco-tourism projects than power and water. However with the correct regulatory framework and strong political commitment,

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<sup>5</sup> See SAIIA (2005), pg. 11.

they do offer value for money to governments and good opportunities for investors. A recurring theme is that for PPPs to be successful, governments need to undertake thorough feasibility studies that address the issues of affordability, value for money and risk transfer.

## **2.5. Typical procurement packages and financing mechanisms**

From the public agency's perspective, expanding the role of the private sector offers a range of advantages relevant to specific project needs. Projects are likely to benefit from PPPs when tight schedules, complex design and construction or innovative finance are involved. For example, toll roads – normally financed by debt – require scheduled and cost-certain project delivery. Using a Design-Build contract for toll road projects shifts the risk and responsibilities of meeting these objectives onto the private design/build entity, which is best positioned and incentivized to meet these requirements. Some toll road partnerships also involve the private sector providing innovative approaches to supplying debt and equity finance that can augment scarce agency tax resources for special projects or program expansion. From the private sector business entity perspective, PPPs provide expanded business opportunities to provide services not part of traditional highway development. Private entities are able to compete on the basis of a broader set of technical skills and expertise. Expanded partnership arrangements also often provide increased flexibility to employ new approaches such as innovative finance. And while the expanded roles may introduce new risks (such as meeting fixed schedules and cost commitments), they also offer new rewards in the way of expanded fee opportunities.

Financial packages would include private sector operations and maintenance on a performance basis, private sector program management for a fee and/or with program costs and schedule maintenance incentives, design-build for fixed fee on fixed time frame, project build-operate-transfer (BOT), design-build finance-operate-transfer (DBFO); and, Build-own-operate (BOO). PPP projects are often undertaken to supplement conventional procurement practices by taking additional revenue sources and mixing a variety of funding sources, thereby reducing demands on constrained public budgets. Some of the revenue sources used to support PPPs include:

- Shareholder equity;
- Grant anticipation bonds;
- General obligation bonds;
- State infrastructure bank loans;
- Direct user charges (tolls and transit fares) leveraged to obtain bonds; and,
- Other public agency dedicated revenue streams made available to a private franchisee or concessionaire.

PPP financings often involve the co-mingling of different financing tools and private commercial debt.

## **2.6. Key elements of best practices in PPPs**

Governments must however overcome a number of challenges in implementing PPPs. These include developing and establishing strong legal and regulatory frameworks that can clarify the legal authority to grant concessions, the procurement process, the contribution from the public authority of assets that can make the project viable and the rebalancing of tariffs which will make the project viable from a financial point of view. In addition, there must be political commitment

to give confidence to the partners to make investments. Effective public administration is also important preferably through a dedicated central PPP unit located within government that can oversee the whole PPP process and has cross cutting authority over all Ministries.

### **2.6.1. Governance**

Governance can be broadly defined as the exercise of political, economic and administrative authority to manage a nation's affairs. Governance is thus about the importance of institutions, the interactions between different levels of government within a country, the interaction between the public, including nongovernmental organizations and business, and government. Good governance in PPPs refers to a number of inter-linked ingredients. Governance in PPPs combines at least the following five key ingredients:

**Transparency** - Transparency refers to the way in which the design and initiation of projects, procurement and selection process, ought to be organised. Secondly, it takes into account the interests of all 'stakeholders', for example, local citizens, NGOs, employees/trade unions, civil society, media, investors, lenders, government.. There has to be an elimination on use of bribes and other forms of corruption to win favours and approval for projects from governments.

**Public accountability** - The public needs to know that its interests will be protected in a number of specific areas. Firstly, that the PPP will obtain 'value for money'. Secondly, that the project has clearly defined goals which can be measured, and should be met. Thirdly, that procedures for the award of the contract will be fair and according to the criteria as laid down in the project specification. Lastly, that if the financing of the projects involves a subsidy from the state, the size of the subsidy will be known to the citizen since financing of PPPs is a complicated exercise that creates political and regulatory risks for all the parties involved. PPPs involve future financial obligations on the taxpayers.

**Public management** - PPPs involve a redefinition of the role of Government in the context of infrastructure projects, focusing on supervision and regulation and moving away from direct ownership and management. PPPs allow Governments to attract private sector funding and involvement, without incurring the adverse political repercussions sometimes associated with full-scale privatization. Government retains a significant role and can guard against private sector excesses. It can also retain ownership of the assets in question, and avoid perceptions of "selling out" to foreign buyers. The PPP approach, in other words, avoids undermining the essentially "public" character of many infrastructure projects.

**Sustainable development** - Sustainable development refers to a process where integrated consideration of economic, environmental and social processes ensure the long-term viability of a project. PPPs are ideal vehicles to achieve such integrated objectives, because of their multiplicity, multi-sector structure. Policy makers must ensure that PPPs increase the delivery of services to those who need them most and should not exclude those in most need by raising tariffs beyond the purchasing power of those who are economically and socially disadvantaged.

**Dispute resolution** - The multiplicity of parties in privately financed projects makes conflict predictable. Yet despite its perceived negative impact, conflict within PPPs can lead to creative and constructive outcomes when it is managed by encouraging open discussion that allows full



exploration of the participants' needs, concerns, values, meanings, and interests – the essential ingredients of authentic communication. This process can contribute significantly to the accountability and transparency that PPPs strive for, and serves itself as a mechanism for channelling constructive conflict towards positive outcomes.

***Safety and security*** - Safety and security are paramount requirement in the delivery of infrastructure services. All projects should be properly screened to examine whether they are feasible from this respect and thus there should be experts able to give advice on how projects can achieve the highest standards in these criteria.

### **3. The Current State of PPPs in Kenya**

#### **3.1. PPPs and their role in supply of Government services**

In Kenya like in most developing countries, the role of government in the economy is still quite substantial. Whereas total government expenditure as a proportion of GDP at market prices was 22% in 2000/01 FY, it stood at 34% in 2004/05 FY. However, there has been hardly any change in the proportion of government expenditure towards social as compared to economic services. Total government expenditures for social services as compared to economic services has remained fixed at 30% and 10% of total expenditures for each of the last 4 FYs<sup>6</sup>. However proportion of public services contracted out to be delivered by private companies is still very low. Hence there are still opportunities to deepen social expenditures and increase the use of the private sector in financing economic and services in Kenya.

In Kenya, the pressure to reduce expenditure and cut down taxes has forced the government to resort to the private sector. In the last few years even where adequate competition has not been prevalent and service provision has largely remained monopolistic, e.g. in the telecommunications sector evidence suggests that where private sector bears the risk, it delivers better results than any credible public sector alternative. To make services work for the poor people, Kenya must review its service delivery mechanisms and the institutions that provide the service. New management practices and technologies are changing the way programmes and services are delivered. Rapid development in information and communications technology has created many opportunities related to service delivery, giving rise to globalisation and intensified international competition.

In parts of the developed world, PPPs are well developed. For example, in the UK, deregulation of employment and services starting in the 1980's created the conditions for the different kinds of privatisation that have been a key characteristic of British public services. The latest figures indicate that almost one fifth of public services - worth UK £60 billion are delivered by private and voluntary bodies in 2006. A pioneer in the use of the PPP approach, or the Private Finance Initiative (PFI) as it is sometimes called in the UK, PPPs have proven to be very successful with over 407 signed PFI projects valued in March 2005<sup>7</sup> at nearly UK£ 42 billion. This probably amounts to more than the rest of the world put together. In the UK, the PPP approach is applied across a wide range of services, including transport, education, prisons, health care, defence, leisure, Government offices, the environment, housing, courts, and IT. The major types of PPP found in the UK are contracts for services, concessions, joint ventures and investment programme management.

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<sup>6</sup> According to Economic Survey 2005, in 2001/2002 total expenditure was Ksh. 311 billion of which Ksh. 90 billion was allocated to social services and Ksh. 39 billion to economic services. By 2004/2005 the comparative figures were Ksh. 431 billion, Ksh. 135 billion and Ksh. 56 billion respectively (Republic of Kenya (2005a), Table 6.8, pg. 107.

<sup>7</sup> See UNISON (2005), Table B, pg. 5.

### **3.2. Policy and Institutional Framework for PPPs**

As early as 1992, as part of the framework to implement the privatization Programme a high level policy making committee, the Parastatal Reform Programme Committee (PRPC), assisted by a secretariat, the Executive Secretariat and Technical Unit (ESTU), was established under the chairmanship of the Vice President and Minister for Finance. The functions<sup>8</sup> of the PRPC were:-

- (i) to supervise and coordinate the implementation of the Parastatal Reform Programme in general;
- (ii) to prioritise and determine the timing of the sale for each non-strategic PE;
- (iii) to approve the operational guidelines for privatization to be followed by ESTU, including the criteria and procedures to be followed in the divestiture decisions;
- (iv) to give final approval or rejection for the sale of public assets;
- (v) to monitor and evaluate the progress of implementing the programme; and
- (vi) to provide political impetus for privatization and participate in building public awareness and the national consensus in support of the government programme.

The functions of the Secretariat were:

- (i) to formulate and recommend policies, procedures, programmes and operational guidelines for divestiture;
- (ii) to prepare, with the collaboration of the holding companies where applicable, target lists of candidates for privatization for approval by the PRPC;
- (iii) to prepare, with the collaboration of the holding companies where applicable, PEs for privatization and monitor all technical privatization matters undertaken by consultants, including: valuation, selection of optimal privatization method.

More recently, to enhance transparency in the implementation of the privatization programme, the NARC Government, through the new Privatisation Act is in the process of establishing a Privatization Commission which will implement all privatisations involving the transfer of a public entity's interest in a state corporation or other corporations; the transfer of operational control of a state corporation or a substantial part of its activities and any other privatization prescribed by regulations. This will place the implementation of privatization of all shares held by public institutions including the government, the local authorities and state corporations and the transfer of all or substantial part of their operations through management contracts, leases and other forms of Public Private partnerships under the oversight of the Commission.

In its draft *Sessional Paper No 2 of 2005 on "Privatization of State Corporations and Investments"*, the NARC Government reiterates its role of being a facilitator for private sector led economic growth and investment. Its proposed privatisation strategy is, therefore, stated to be an integral part of the public sector reforms that are to be implemented by Government to spur the recovery of the Kenyan economy, improve the social economic indicators and help Kenya to move toward the Millennium Development Goals (MDGs). It states "Through outright privatisation and various forms of Public Private Partnerships, the Government intends to

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<sup>8</sup> See Republic of Kenya (2005b), pg. 9

mobilize resources to rehabilitate, modernize and expand Kenya's productive capacity, and has outlined a number of privatisation initiatives whose implementation is to commence immediately"<sup>9</sup>. With specific reference to infrastructural development a recent statement also states that, " In Kenya, "private sector investment should be encouraged and facilitated, not only through formal concessioning contracts, but also localised private-public partnership initiatives to contribute towards road construction and repair". (Republic of Kenya/CG Donors (2005), pg 5) *CG 2005, Joint Statements of Development Partners for the Kenya Consultative Group Meeting Roads, PG. 5.*

Currently, PPPs are being discussed as one of the three crosscutting issues under the Government's Private Sector Development Strategy<sup>10</sup> 2006-2010. Therein it is stated "The Directorate of Procurement in the Ministry of Finance has been charged with the responsibility of developing a PPP policy, legal and regulatory frameworks and institutional structures to support them" (Republic of Kenya/Ministry of Trade and Industry, 2005, pg. 61). In addition, work on establishing a PPP Unit<sup>11</sup> is currently underway within the Ministry of Finance.

Thus, whereas to date there is not single official document that comprehensively sets out the policy and institutional framework for PPPs, the concept is well grounded both in GoK engagement and sectoral implementation discourse with the private sector, particularly in the infrastructure sector. The Kenya government has embraced PPPs with a clear request for the private sector to engage in or undertake financing, construction, operation and maintenance of public sector infrastructure and development projects. Services may be franchised, outsourced, or grants given for specific services. The Government is keen to provide various incentives, including ensuring an appropriate investment climate.

Whereas the Irish Republic has followed the European and British developments in supporting the concept of PPP as a matter of policy there were certain special considerations that provide important lessons for Kenya. Firstly, a critical advice given to the Government in 1998 was to proceed carefully with pilot applications of PPP, in circumstances that indicated lowest ex-ante risks. One aspect of the approach taken by Ireland was that the PPP policy and timeframe was that there was a clear sequencing of PPP policy development followed by cautious execution of PPPs.

### **3.3. The Privatization and Public Procurement and Disposal Acts**

The two key Acts of Parliament that variously spells out the legal framework for PPPs in Kenya are the Privatization Act No. 2 of 2005 which after some delay was given Presidential Assent on 13<sup>th</sup> October 2005, and the Public Procurement and Disposal Act, No 3 of 2005 assented on 26<sup>th</sup>. October 2005.

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<sup>9</sup> Republic of Kenya (2005c), pg. 12

<sup>10</sup> Republic of Kenya/Ministry of Trade and Industry (2005)

<sup>11</sup> Conversation between the author and Mr. Kitungu, Director of Reforms, Ministry of Finance

### *The Privatization Act*

- Sec. 2 (1) broadly define privatization to include all transactions that result in the transfer to a private entity the assets, operational control and operations of all public assets. PPPs are given due recognition in the description of the methods of privatization.
- Sec 18 (1) recognizes some seven benefits that may be derived from privatization and directs the Privatisation Commission to take due regard to these benefits, which are detailed in 18 (2) and includes infrastructural improvement, improving the efficiency of the economy, and generation of additional government revenues.
- Sec 25 (b) defines as one of the methods, “concessions, leases, management contracts and other forms of public-private partnerships”.

To the extent that the Act in Sec. 3 establishes the Privatisation Commission as a body corporate with functions to formulate, manage and implement the privatization programme, the institutional structure for implementing PPPs as part of the privatization programme is clearly established.

#### *3.3.1. Public Procurement and Disposal Act*

The purpose of the Act is to establish procedures for procurement and the disposal of unserviceable, obsolete or surplus stores and equipment by public entities to achieve the following objectives -

- (a) to maximise economy and efficiency;
- (b) to promote competition and ensure that competitors are treated fairly;
- (c) to promote the integrity and fairness of those procedures;
- (d) to increase transparency and accountability in those procedures;
- (e) to increase public confidence in those procedures, and
- (f) to facilitate the promotion of local industry and economic development.

It should be noted that according to Sec 4 (1), (b) the Act applies, inter alia, to contract management, i.e. services that the government may wish to contract other entities to undertake on its behalf. The Act specifically prevails where there are any conflicts with other Acts regarding public procurement as stated in Sec. 5 (1): “ If there is a conflict between this Act or the regulations made under this Act and any other Act or regulations, in matters relating to procurement and disposal, this Act or the regulations made under this Act shall prevail.”

With specific regard to PPPs, this is recognised by the Act under Sec. 92 (1), which states that:

“A procuring entity may use a procurement procedure specially permitted by the Authority which may include concessioning and design competition. For the purpose of this section (a) "concessioning" means a procurement that encourages **the mobilization of private sector resources** for the purpose of public financing, construction, operation and maintenance of development projects and may include build-own and operate, build-own-operate and transfer, build-operate and transfer or similar types of procurement procedures.” For these “specially permitted procurement procedures”, under Sec 92 (4), the Public Procurement Oversight

Authority may exempt the procedure from the application of normal procurement procedures as detailed in Part IV of the Act or vary the application of such a provision.

Hence, as can be seen above, PPPs in a way are firmly governed by at least two Acts that broadly provides the legal basis for such undertakings.

### **3.4. Case Study - The Kenya Railways Concessioning**

#### **3.4.1. Introduction**

It is acknowledged that an effective transport system is critical to a nation's development through provision of economic, social and cultural links to the outside world, and connecting the population and the economic activities within a country. The quality of transport infrastructure affects production costs, employment, access to markets and levels of investment. Kenya's transport infrastructure consists of a road network comprising high traffic inter-urban, urban, secondary and rural roads, a main line railway with three branch lines, a port, three international airports and a number of domestic airports and airstrips. As with much of the transport sector in Kenya the rail infrastructure is in poor condition and poorly maintained. Kenya Railways Corporation (KRC) is currently hauling less than a third its freight capacity and is losing market share to roads. The current problems faced by KRC have been caused by a lack of, as well as inappropriate, investment (particularly in maintenance) and poor management.

#### **3.4.2. Asset condition and quality of service**

The majority of rail services in Kenya are provided by KRC, a State Corporation, which was established in 1978 through an Act of Parliament following the winding up of its forerunner, the East African Railways Corporation. The main purpose of the railway is to provide a freight link between the port of Mombasa and Kenya's hinterland, and on to landlocked countries in East and Central Africa, primarily Uganda. The railway line is over 2,700 km long, has a one metre-gauge, and runs along the southern half of the country and the Kenyan side of Lake Victoria. It links with both Uganda and Tanzania Railways at Malaba and Taita-Taveta respectively. KRC also operates both freight and passenger vessels on Lake Victoria, although currently only the freight vessels are operational. Freight business constitutes over 80% of the company's revenue. KRC also has workshops for maintenance of locomotives, a joint venture with the University of Nairobi (Numerical Machining Complex) to make spare parts for both KRC and other customers, and a training institute for both KRC as well as other government and private sector organisations.

By end of 2005, KRC's fleet consisted of 160 maintainable locomotives and 2,600 active wagons (although actual stock was more than 6,000). Low reliability, utilisation and turnaround of this rolling stock due to poor condition, and loading / off loading delays at terminal points are the most critical constraints to KRC's operations. Further, the gauge for the Nakuru-Kisumu line is narrower than for the rest of the network requiring off-loading and reloading of the goods at Nakuru. The annual freight capacity is about 6.4 million tonnes although in 2004/05 KRC handled only about 2.6 million tonnes. Since 1978, KRC has been on a steady decline. Between 1978 and 2005, the KR cargo freight market share dropped from 70 per cent to under 20 per cent. Cargo haulage fell from 4.3 tonnes in 1983 to just 2.8 tonnes in 2005. It has also accumulated debts totalling Sh20.5 billion.

On paper, KRC should be very able to compete with road on this route -it is price competitive, the distances are long, and the loads are heavy or bulky, which are traditionally the areas where rail has an advantage over road. However, even though the track from Mombasa to Uganda is fit for an axle load of 18 tonnes, it is currently under-utilised because the company's wagons are unable to carry such loads. On top of this, there is weak regulation of axle load limits on the road network. And at the heart of it all, is reliability, or the lack of it, arising from inadequate maintenance of infrastructure, inefficient management of operations and frequent breakdowns due to poor quality of rolling stock.

### ***3.4.3. Current institutional, policy and regulatory arrangements***

A National Transport Policy was prepared in 2003. The Ministry of Transport and Communication (MoTC) has overall responsibility for the transport sector involving planning, of road rail, air and maritime transport. Aside from policy, in the rail sector the ministry is also responsible for approving major tariff increases, approval of terms of service of railway employees and approval of major capital works. The sector is regulated by the Kenya Railways Act of 1978, which established KRC as a statutory corporation charged with providing rail infrastructure and services in the country. The legislation provides no monopoly for KRC, so in theory PSP in the sector is possible via contract with KRC. Magadi Railways is the only example of this in the sector. Financing of capital works and maintenance is through a mix of GOK and donor funds. In 1997 the GoK announced its decision to privatise KRC. A privatisation strategy study recommended that privatisation be achieved through a concession arrangement, which was approved by a cabinet decision in 1999, and subsequently in September 2002 the IFC was appointed as the transaction adviser.

A new legal framework for the concessioning was put in place through an amendment of Cap 397 - Kenya Railways Corporation Act. This provides for the establishment of a Corporation to be known as Kenya Railways, for the transfer to the Corporation of the undertakings of the East African Railways Corporation within Kenya, for the functions of the Corporation.

### ***3.4.4. The Concession Terms and Bidders***

The value of the infrastructure assets of Kenya and Uganda railways jointly is estimated at US\$ 184 million. The value of the rolling stock able to provide services is estimated at US\$ 120 million (almost 50% of registered rolling stock items is regarded as scrap). Approximately US\$120 million will be required in form of deferred maintenance to get all rolling stock assets running again. The total value of equipment assets is estimated at US\$53 million (including US\$25 million for the marine vessels in Uganda). The total value of the real estate assets is estimated at US\$ 166 million (this include value of operational buildings estimated at US\$38 million and value of land at US\$128 million).

The concession long-term investment in Kenya (25 years) is estimated at US\$250-300 million (with US\$30-40 million in the first 5 years). The long-term investment for the concession in Uganda is estimated at US\$54 million, and US\$18 million for the short-term investment for the first 5 years. Already the EU is financing the repairs of the Nile Bridge, new culverts and construction of 30 km of new track along the main Kampala-Malaba railway line in Uganda.

Two consortia presented their bids of which the first bid was received from a consortium led by Sheltam Close Corporation of South Africa. The Sheltam consortium is referred to as the Rift Valley Railways Consortium and comprised the following partners:

- Sheltam Rail Company (Pty) Limited, South Africa (61%)
- Comazar (Pty) Limited, South Africa (10%)
- Primefuels (Kenya) Limited, Kenya (15%)
- Mirambo Holdings Ltd, Tanzania (10%) and
- CDIO Institute for Africa Development Trust, South Africa (4%).

The second bid was from a consortium led by Rites Limited of India. The RITES Consortium comprises:

- Rites Limited, India, (70%) and;
- Magadi Soda Company Limited of Kenya (30%).

Aggressive and ambitious targets had been set for the winning bidder. These targets included:

- The obligation to grow traffic by at least 75% over the first five years, which would require substantial investments.
- A minimum investment requirement of \$6 million a year
- Commitment to pay the Governments at least 5% of gross revenues every year - compared to the current situation, where the Government is required to provide financial support to the railway.

The winning bidder would be required to offer 40% shareholding to Kenyan and Ugandan investors by the end of the 5th year of operations. The proposed joint concession shareholding structure (transaction configuration) entails the formation of a Holding Company (that will comprise 2 national companies, one registered in each country). The Lead Investor is required to take at least 35% of the Holding Company. Specific targets are set for at least 20% Kenyan ownership and at least 20% Ugandan ownership of the Holding Company. It is worth noting that the 40% shareholding reserved for local ownership is open to both public and private ownership with equal opportunity.

The governments required the concession fee structure to entail:

- Upfront fee of US\$3 million in Kenya and US\$2 million in Uganda;
- Variable annual fee for each Concession for 25 years: 5% of annual gross revenues for the first five years; 7% of annual gross revenues thereafter;
- Fixed annual fee for each Concession for each of the 25 years: amounts may vary from one year to the other;
- Fixed annual concession fee for each of the 7 years for the Kenya passenger services (the amounts may vary each year);
- A performance bond by each concession company will be prepared to cover penalties for non-performance of obligations and cap liquidated damages for concessionaire default;



- Core infrastructure and existing assets (and their rehabilitation) will remain owned by the Governments of Kenya and Uganda; and
- New investment on infrastructure will remain the responsibility of the Governments.

Rift Valley Railways Consortium, led by South Africa's Sheltam Trade Close Corporation, won the rights to run Kenya and Uganda railways for 25 years. The agreement between Kenya and the company is scheduled to commence on March 31, 2006.

#### ***3.4.5. Issue of staff pension***

The Kenya Railways Pensioners Association (KERAPA) has been formed to fight for the rights of former employees who fear for the security of their pensions following the forthcoming concessioning of the railway. The concessionaire is expected to retain between 2800 and 3600 of the existing staff of 6300. KRC itself only plans to keep 30 employees. The surplus will be retrenched and will receive severance payments. KRC has identified assets worth Ksh. 12.4b shillings (about US\$161m) to start the Kenya Railways staff retirement benefits scheme (KRSRBS). The assets, mainly land and buildings, will be sold and funds from the proceeds will be used to establish the scheme. The government has been asked to contribute Ksh. 1.5b (about US\$ 20m) to start the fund. KERAPA Secretary-General Robert Azariah is sceptical, pointing out that KRC was 3 months behind with pension payments in July and that it takes "up to 6 months" to receive pension payments at country stations. According to KRC, the 8665 existing pensioners will be paid all their accumulated pensions and other dues before the concessioning. KRC currently pays out Ksh. 55m shillings monthly (about US\$ 715 000) on pensions.

In late 2005, courts in Kenya and Uganda halted the concessioning pending the completion of lawsuits challenging it filed by railway employees and pensioners who stand to lose their jobs and benefits. In Kenya, Justice Jackson Ojwang of the High Court stopped the concessioning pending the determination of a suit filed by 6,000 pensioners seeking payment of Ksh17b. Kenya Railways pensioners have filed a suit in Kenya seeking to have their accrued pension of Sh6.8 billion set aside before its concessioning. Officials of KERAPA sued the corporation, saying it owes them the colossal amount on account of accrued pension. Permanent Secretary in the Ministry of Transport, Mr. Gerishon Ikiara says the Government had made a tremendous effort in obtaining funding from international financiers to the tune of US\$ 70 million (about Ksh. 5.25 billion) to cater for those who would be retrenched. Another Sh900 million has been obtained from World Bank to meet cash flow requirements of the Pension Fund. As of mid-January 2006 the case was still to be determined.

#### ***3.4.5. Lessons learned and some issues of concern***

Main lessons for policy makers and regulators are many and include the need to provide adequately for legislative and regulatory framework at national, across the country and regional levels to enable concessioning to avoid delays. The legislative framework should also provide for efficient and safe operation of the concession. Harmonization of regulation across the countries and creation of a joint commission for regulation is important. Signing of an interface agreement and inter-government MOU on joint concessioning is important.

Due to the magnitude and operation across the countries, the joint concession requires a strong commitment by the governments and strong political will in its every stage of the project starting

from the conception, planning, preparation, design, negotiation and implementation. It is important to involve workers/labour in critical stages of the project and provide for their safety net through retrenchment scheme and selection of required labour by the concessionaire.

The key lessons for Kenya to learn and issues to address in implementing the privatisation are:

- a) Financial proceeds (e.g. concession fees) should not be the government's highest priority. Of more importance is investment into the railway stock.
- b) Passenger services are very rarely profitable so some form of subsidy is likely to be required if government wishes them to be continued
- c) Separating operations from infrastructure has limited benefits for a small "single purpose" railway and introduces a degree of complexity (e.g. disputes over who is responsible for delays and the need to harmonise investment decisions) that may outweigh the benefits of separation -the integrated concession proposed would seem to address this concern.
- d) KRC's main competitor is the Mombasa - Malaba road. The privatisation of KRC will have an impact on the potential concessioning of that highway and *vice versa*. Careful coordination is required to ensure that the privatisation of one does not undermine the other. The majority of KRC's customers are commercial businesses meaning that concerns over tariff increases will meet less public resistance (provided government continues to provide support to passenger services).
- e) A key area of concern for government is likely to be that of retrenchments which as the Court has determined, will be mandatory prior to finalisation of the concession.

## **4. Legal and Institutional Reforms for PPPs in Kenya**

### **4.1. Competition and consumer policy, and key issues for consideration in adopting PPP**

The ideology of promoting private enterprise through PPPs must be seen from the perspective of allocating private monopolies in a national situation where the capacity to regulate such prior public monopolies is still under development. It must be recognised that the Country's competition policy and law is currently under review and issues touching on regulation of monopoly power in the public interest is far from solved. Now is the time to underpin these concerns while formulating the finalisation of PPP, Procurement, privatisation and competition laws and regulations

The general euphoria around policy encouragement for PPPs ignores a range of concerns about PPPs based on public interest considerations. Most fundamentally, there are questions about whether PPPs should be unambiguously preferred to public sector investment and operation of services, and the need to evaluate the social and economic impact of the risks and future liabilities created by PPPs. There are a number of specific public interest concerns: about the way PPPs transfer the costs of paying for investment from present generation to future generations; about the dangers of fragmenting, casualising and worsening conditions of employment of soon to be PPP'd public service workers; about the real transparency of the processes by which PPPs are likely to be effectively established, operated; and about the comparative economic consequences of PPPs and public sector options.

### **4.2. Performance Measurement and PPPs**

Performance measurement may be defined as the selection and use of quantitative measures of Programme/project capacities, processes, and outcomes to inform the public or a designated public agency about critical aspects of a programme, including its effects on the public (National Research Council, 1999). Over time distinctive types of performance measurement have been developed amongst of which one can mention just a few. Market-based performance measurement focuses upon issues of interest to clients and customers and often is in the form of customer satisfaction assessments. From the perspective<sup>12</sup> of PPPs Government-based performance measurement systems concentrate on developing indicators determining whether programmes and organizations are making wise use of public monies.

Public organizations often find it difficult to develop and fully engage in performance measurement systems. Even in the US when the U.S. Congress mandated that agencies develop performance measurement systems under the Government Performance and Results Act it took considerable time for some agencies to have the message to sink in and to devote resources to effort. These difficulties are magnified when the performance measurement system is to reflect the work of a PPP. Whereas of course it is beyond the scope of this paper to establish *a priori* the performance measurement systems for PPPs in Kenya, there are several recurrent themes that emerge that will pose challenges for establishing performance measurement systems for PPPs.

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<sup>12</sup> This discussion on performance measurement and PPPs draws from Gordon Kingsley, G and Dara V. O'Neil (2004).

*Partnerships are Not Built in a Day* – Even when there is some mandate instructing organizations to partner the way in which they are constructed relies upon these relationships. If such relationships are absent then the partners are likely to require a slow pace of development as trust builds up among participants. Performance measurement systems that do not account for the differences in starting points may have unrealistic expectations.

*The Utility of Expressing Shared Vulnerabilities* – Practitioners have learned that a useful exercise is for the senior stakeholders in a partnership from participating organizations to have an open and frank discussion early in the effort to identify the exposure of their organizations to harm either directly from partnership activities, or from a failure of a partnership to produce a successful outcome. From a performance measurement perspective this is the equivalent of establishing the level risk experienced by the participating organizations.

*Administrative Partners vs. Participating Partners* – One of the consistent failures of partnerships is a lack of clarity about who is responsible for the partnership. Practitioners frequently note the need for multiple champions at all of the levels of the participating organizations who are affected by the partnership. This core of champions must meet with some frequency to assure that administrative responsibilities are clearly assigned and that follow-through is adequate.

*The Tragedy of Turnover* – While organizations enter into partnerships with some enthusiasm, they also will try and buffer the organization from the activities associated with partnering. It is more common for a handful of champions to emerge who are charged with getting the work done.

*Recognizing the Full Range of Transaction Costs* – Participating partners routinely discount transactions costs before engaging in a partnership. Typically, partnership activities are not the sole job of managers charged with making it happen. They are asked to do their normal job plus meet the challenges posed by the partnership. Managers anticipate that this will bring some costs in the form of meetings, and making institutional adaptations to accommodate the partnership.

*Establishing An Acceptable Distribution of the Costs of Partnership* – A second issue associated with costs has to do with each partner absorbing an acceptable amount of the cost of partnership. One of the common games played amongst professionals engaged in partnerships is getting your partner organizations to conform to your administrative procedures.

#### **4.3. Missing the Procurement Act provisions**

There is a general question about the likelihood for effective working relationship between the institutions to be created under the two relevant Acts, i.e. Public Procurement and Privatisation Acts. The bulk of the planned institutional arrangements for PPPs is concerned with possible implementation of the Privatization Act, yet the Public Procurement Act published barely one month after the enactment of the former Act comprehensively revised procurement procedures for the Government and there is no reference to the Privatisation Act. The opportunity of including relevant provisions in the Public Procurement Act was not recognized.

#### **4.4. Sub-contracting**

The question of sub-contracting as creating potential problems needs to be recognized. Sub-contracting in its various forms has led to worsening of conditions, loss of training and unreliable and dangerous work in many services in many countries and these problems are general to all sub-contracting. There does not seem to be any consideration for regulation of sub-contracting under PPPs in both Acts.

#### **4.5. Neutrality of public choice**

The principle of neutrality as it relates to value judgment on the decision whether or not to externalise services is an economic and organisational choice made by a local or national authority. Encouraging PPPs, removing obstacles to them, clearly implies discouraging the alternative, of using the public sector. It also involves a preference for private ownership. The asset financed by a PPP needs to be classified as an asset, off the sector balance sheet, and so escapes the curbs on government debt. Encouraging PPPs entails encouraging the formation of privately owned assets over the alternative of publicly owned assets.

This vagueness is consistent with an approach based on the private interest of expanding the market. To those interested in market opportunities, it does not matter much exactly what are the features of the contract. Hence in evaluating PPPs against public interest two central comparative questions arise: Firstly, is the PPP a better way of financing the capital investment involved than alternatives? Secondly, is the PPP a better way of operating the service than alternatives?

Thus the key choice is between public sector provision and a PPP, or other variants on these options. When considering the PPP option, the government has to compare the cost of public investment and government provision of services with the cost of services provided by a PPP.

By unambiguously encouraging PPPs and remove obstacles to them, may have the effect of distorting the higher level choice, for example by offering guarantees to entice private contractors. In the context of this choice it is important that PPPs are not made too easy or attractive, e.g. by offering exemption from fiscal restraint, or from procurement disciplines, or providing state-backed guarantees which are not properly costed. These inducements would distort any evaluation between a PPP and a public sector provision.

#### **4.6. Capital investment: private borrowing is more expensive**

PPPs are helpful because they allow public investment outside the fiscal guidelines. There are two crucial weaknesses in this position: the by-passing of better alternatives, and the failure to make a long-term assessment of the implications of PPPs. PPPs have to be demonstrated to be a better option than other ways of investing and delivering the same service. PPPs have a fundamental disadvantage as a way of financing capital expenditure, compared with finance raised by government borrowing: governments can invariably borrow money more cheaply than any private company, As the IMF puts it; “private sector borrowing generally costs more than government borrowing. This being the case, when PPPs result in private borrowing being substituted for government borrowing, financing costs will in most cases rise ...”<sup>13</sup>. This means that the PPP has to demonstrate that there are significant efficiency gains from involving the private sector, in order to offset the borrowing costs.

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<sup>13</sup> International Monetary Fund (2004), para 22.

#### **4.7. The efficiency argument**

Policy pronouncements harangue on the subject of efficiency and assumes from the outset that the public sector will benefit from the know-how and working methods of the private sector) but does not at any stage justify this. There is no systematic evidence that the private sector is more efficient than the public sector. The IMF, by contrast, is aware that the evidence does not support a general assumption of superior private sector efficiency: Much of the case for PPPs rests on the relative efficiency of the private sector. While there is an extensive literature on this subject, the theory is ambiguous and the empirical evidence is mixed”.<sup>14</sup>

#### **4.8. Uncertainty and incomplete contracts**

A problem with all outsourcing is the uncertainty of the future, which means that contractual relations have to be renegotiated, limiting the range of options and flexibility of the public authority. It may be argued that what happens after the contract can be determined by provisions in the contract itself, and in this way the allocation of risks can be defined and controlled. There are two great weaknesses in this position. Firstly, the key question is not allocation of risk within PPPs, but the riskiness of PPPs compared with the alternative of public sector provision. Secondly, in reality it is impossible to specify everything in a contract, because unforeseen circumstances will arise. This is a key reason why businesses are vertically integrated instead of outsourcing core activities, and by the same logic provides a reason for public ownership rather than use of PPPs. This is especially important in the case of public services, because the state can never transfer responsibility for the public interest that the service is serving, and so entering into long-term PPP contracts limit the state’s ability to respond to uncertain future changes in the public interest leading to the state to reducing its own powers to act.

#### **4.9. Renegotiation: unequal opportunities**

This need for constant renegotiation is often seen as an opportunity for the private partner to improve the terms of their contract, but for the public partner it is normally disadvantageous, partly because of the greater knowledge and legal expertise of the private companies leads to contract revisions more favourable to the contractor. In France, which has the longest experience of such concessions to build roads, water works and other infrastructure, an official report observed that the system left elected councillors on their own, without support, to deal with conglomerates wielding immense political, economic and financial power.

If every substantive revision has to be retendered, then PPPs will become so uncertain that private companies will lose interest. This real problem should rather be addressed in a comparative evaluation of PPP proposals with other public sector option: the risk to the public authority of this kind of future deterioration in the terms of the contract has to be quantified.

#### **4.10. Uncertainty of outcome: secrecy, lies and mistrust**

The uncertainty of the future is compounded because of strategic behaviour by the companies designed to improve their own position, and exploit omissions and failures by public authorities. There is real experience of these problems and these must be noted. PFI schemes in the UK show common exaggeration of costs or reduction in quality. With hospitals, the cost of PFI

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<sup>14</sup> International Monetary Fund (2004), para 25.

schemes has invariably been higher than originally forecast, requiring 30% cuts in bed capacity and 20% reductions in staff in hospitals financed through PFI. Corruption is a common problem with public sector contracts, and PPPs are at least as susceptible as others.

## 5. PPPs – Lessons from Africa

Before giving specific lessons from Africa, it is insightful to refer to the UK, which has arguably the most PPP experience of any jurisdiction worldwide. There the experience with PPPs has not been all good. The establishment and management of PPPs is often associated with high transactions costs that undermine the gross efficiency gains, both directly and indirectly by limiting *ex ante* competition through high entry (bidding) costs. In the case of London Underground, in February 1999 the government budgeted to spend £ 150 million for bidders' costs. After prolonged negotiations the accepted level amounted to a total of £275 million of bidders' costs being reimbursed<sup>15</sup>. The UK National Audit Office concluded that “the process of negotiating the deals, and obtaining consents (including state aid clearance), was costly for all the parties involved” [(Comptroller and Auditor General (2004), pg. 7)]. With regard to private financing of health services in the in the UK, several major problems<sup>16</sup> have been identified. Firstly, all hospitals were desperately short of beds, putting pressure on hospital staff to get patients out as quickly as possible. Secondly, all trusts running the hospitals were under severe financial pressure, partly as a result of the escalating costs associated with PFIs. Thirdly, there were concerns over poor quality of design of buildings, including poor ventilation, lack of space and inadequate fittings and materials. Lastly, the quality of care had declined, with concerns about time spent with patients and the level of multi skilling required.

In Africa Governments are increasingly looking to PPPs to radically improve infrastructure networks in their countries and enhance service delivery to their people. This development finance model — where the state shares risk and responsibility with private firms but ultimately retains control of assets — will improve services, while avoiding some of the pitfalls of privatisation: unemployment, higher prices and corruption. In theory, PPPs may have the potential to solve sub-Saharan Africa's profound infrastructure and service backlogs, where nearly 600 million people lack access to electricity, almost 300 million have no access to safe water and there are just eight telephones (either mobile or fixed line) per 100 inhabitants. A recent review of case studies of PPPs in Africa<sup>17</sup> reveal that the PPP process is complex, and for PPPs to potentially bring the efficiency of business to public service delivery and avoid the politically contentious aspects of full privatisation there are certain important lessons. The eight case studies in the report draw lessons from PPPs in toll roads, ports, prisons, and telecommunications, eco-tourism and water and electricity provision.

### 5.1. Are there sectoral characteristics?

The experience in Africa like in most other countries has been that PPP programmes start in transport, with later migration to other sectors. The main reason is often the high cost of such projects coupled with attendant easier ability for the private sector partners to get revenues through toll charges. The rate of ‘migration’ to other sectors (health, education, energy, water, waste treatment) often reflect:

- i) national priorities, and

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<sup>15</sup> See Valila (2005), pg. 18 for a discussion of transaction costs of PPPs.

<sup>16</sup> See Evatt Foundation (2005), pg. 2.

<sup>17</sup> See SAIIA (2005) from where these lessons are drawn from.



ii) ii) legal frameworks.

There has also been a tendency for projects to cascade from central to local government/ municipalities.

## **5.2. Politics Matters**

Government and the private sector often underestimate the extent and effect of political opposition to privatisation initiatives. Conversely, protest is minimised when Governments work hard to explain the need for PPPs and publicly discuss options well before deals are signed. There are often price increases, overstaffing of public enterprises may imply substantial job losses, and the companies may be taken over by foreign multinationals. In addition to these concerns, the potential profits lead to suspicions of corruption. In order for governments to succeed, they need to manage the politics of reform by ‘building consensus for reforms through public education and consultative mechanisms’ and by ensuring transparency in awards and the oversight of private infrastructure schemes.

By placing licences and concession contracts in the public domain, governments can allow consumers to see how prices and quality of service will be affected, the quality of service they can expect and understand their rights and obligations. Private companies engaging in PPPs also need to heed the advice that politics matters. In the case studies the experience of Northern Electricity in Namibia is a case in point. Contracted by the Namibian Ministry of Regional and Local Government and Housing (MRLGH) in 1996 to operate a set of state-owned (and state-financed) assets in the more densely populated northern region of Namibia, Northern Electricity provided a reliable and profitable service in a rural area where the local authorities had been losing approximately N\$10 million (US\$1 million) annually.

Despite Northern Electricity’s success in managing the business of electricity provision, their management contract was not renewed by the newly created Electricity Control Board and the contract was awarded instead to a joint venture between the national utility company NamPower and several local and regional governments. When politics is understood as characterising a particular allocation of benefits among competing interest groups, then private companies are advised to pay attention.

## **5.3. Pricing is Fundamental**

The politics and viability of PPPs are both deeply affected by pricing. Many governments turn to PPPs or privatisation when they cannot afford to continue to provide free or inexpensive services, or the capital expenditure required to extend services. While business can bring efficiency and needed investment, it can’t work miracles. Allowing companies to raise prices rapidly on formerly cheap public services can spark a political storm. But ignoring market forces and suppressing price hikes entirely can force businesses to back out of PPP deals. Managing the transition from an era of state-subsidised service to more market-based pricing is critical.

African governments are constrained when it comes to pricing policy because the regulator often does not have accurate information on the costs of suppliers, and translating fixed costs into per unit charges requires complex assumptions and accounting analysis. Regulators tend to permit price increases because they are weak or poorly staffed, sympathetic to the state firm, or the

company provides poor or misleading information. In such a situation it is easier for a private company to push through price increases to ensure that it retains a comfortable return on equity.

South Africa's PPP Unit learned the importance of pricing and affordability through the Asset Procurement and Operating Partnership Systems (APOPS) prison deals. Part of the problem was that the department had not calculated what it could afford in terms of its Medium-Term Budget Framework and the high specifications also affected the costs.

#### **5.4. Corruption Destroys Partnerships**

Historically, corruption has been an enormous problem affecting public procurement in Africa. Even with simple tenders, officials have found myriad ways to direct contracts to favoured bidders. Because PPPs deal with far more complex services and thus the choice of companies cannot be reduced to the single variable of price, PPPs offer far greater latitude for manipulations by foreign or local firms or government officials that are hard for the public and anti-corruption systems to spot. While officials hope that the involvement of independent transaction advisors will reduce corruption since they are being paid a set amount and have no incentive to manipulate the process, it is too early to tell whether this will be effective.

In Kenya for example, the government's planned 25-year concessions for sections of its road network that form part of the Northern Corridor received a setback following evidence of attempted diversion of funds. In September 2004 the Kenyan government instituted an investigation and suspended three top officials at the ministry of Roads and Public Works following allegations in the *East African Standard* that staff at the ministry were planning to divert KSh100 million (about US\$1.23 million) meant for the project to their private account.

#### **5.5. Risk Transfer/Risk Management**

Any sizeable deal carries with it a raft of things that can go wrong, or risks. If it had its way, government would prefer a PPP where business would bear all the costs and risks associated with less than anticipated demand, regulation and currency fluctuation, for a negligible price and profit. The company would be unlikely to accept that deal. From the business perspective, the ideal PPP would involve very fat profits, no risk, government subsidies and monopoly control. Again, government would decline. In reality, crafting a PPP means bridging these extremes fairly to mitigate the risks that each side fears.

A major risk to both the public and private sectors is demand risk. This is the possibility that consumers will not buy the product or service at sufficient volume to make the PPP viable at established prices. Using the example of a toll road, in cases where feasibility studies show insufficient traffic demand but the road is an important one, as with the scenic Chapman's Peak toll road in Cape Town, South Africa, provincial government will provide a subsidy upfront and a 'patronage guarantee' should road usage fall below an agreed amount.

Comparing the risk-adjusted Public Sector Comparator (PSC) model with the institution's budget will give an indication of the PPP's affordability. Various financing instruments have been developed to manage the risks in infrastructure projects. One of the more serious of these risks is currency mismatch, which arises when funding is denominated in a foreign Currency but the infrastructure is to be paid in local currency, which is prone to devaluation. Currency risk is not

specific to private projects — governments and public enterprises borrow in foreign currencies as well. The long-term solution to the currency mismatch problem is to develop local currency markets so that long-term local currency financing and hedging options are available.

### **5.6. Providing a Range of Service Options**

In privatising basic services, governments in developing countries have often set high quality standards and imported engineering approaches used in developed countries. This has often meant that the services are too costly for the poor. Governments must help poorer or unserved consumers by introducing a range of service alternatives, for example in water and electricity. This applies both to the type of service offered – for example indoor running water versus external standpipes – and to the service providers. Although indoor plumbing may be the ideal, refusal to consider cheaper solutions can guarantee that rural areas never receive service. In the Philippines for example, the government has allowed the private water operators in Manila to meet their expansion targets by using alternative providers within the concession zone. The two main water companies supply water in bulk to local firms, who then supply their customers through plastic hoses and small pipes. The two companies have also reduced expansion costs in poorer neighbourhoods by using cheaper and smaller diameter pipes.

### **5.7. Local Economic Empowerment**

PPPs offer opportunities for the transfer of economic power to the local population through greater participation in and ownership of businesses. PPPs can be good for local empowerment in a number of ways:

- The long-term nature of contracts allows the growth of local equity and management over time;
- Risks are clearly identified in PPPs, ‘clearly costed and appropriately allocated, so black participants know in advance what they are committing to; and
- The utilisation of a range of large, medium and small enterprises, through subcontracting and procurement, can bring tangible local economic development benefits to targeted groups.

The South African government has identified the Black Economic Empowerment (BEE) as a way in which PPP projects can achieve optimal value for money in government’s delivery of infrastructure and services.

### **5.8. Regulating the Private Sector, Enforcing Contracts**

Governments need to regulate and monitor PPPs to ensure compliance with agreed performance targets. Most infrastructure services are natural monopolies, whether in public or private hands. Private monopolists may seek to levy prices significantly above marginal costs or public monopolies may allow costs to rise above efficient levels or offer services of inferior quality. Other problems include consumers not being able to access information to assess the quality of the service they get and issues of environmental standards, public health and safety. Governments are generally bad at regulating themselves since there is an inherent conflict of interest when government both provides a service and sets the rules governing it. African countries have tended to lack regulatory agencies or vest the regulatory function with the ministry or parastatal concerned with the project (such as in Gabon with water and electricity, Mozambique for the port concession or Tanzania for the container terminals). African

governments have thus tended to use their early PPPs as opportunities to develop their regulatory capacity.

As long as the department concerned has sufficient technical capacity and political independence, it can perform the same function as an independent regulator.

### **5.9. Building the Capacity of the Public and Private Sectors**

Capacity is a serious constraint for African governments to conduct successful partnerships with the private sector. African countries need to develop their capacity to plan, negotiate, implement and monitor successful PPP projects. While the argument can be made that PPPs are too complex for governments lacking adequate capacity, starting with smaller projects and developing such capacity gradually will help to overcome this problem. The SADC Banking Association's PPP Capacity Building Programme has carried out training in PPPs in Mozambique, Botswana, Tanzania and Mauritius. It also reviewed the institutional and regulatory environments with regards to PPPs in those countries. Capacity development is needed in both the public and private sectors. The lack of a robust private sector in many countries means that governments are unable to solicit the expertise needed to develop projects, which means that raising money for PPPs is more difficult. The programme does not suggest that a PPP is the most suitable procurement option for all infrastructure projects; instead it advocates for the utilisation of principles that underlie PPPs, namely affordability, value for money and risk transfer.

## **6. Conclusion and Recommendations**

The issues discussed in this report all raise significant challenges to conduct of successful PPPs. The complexity of such arrangements and the high costs involved is enough cause for the Government to take a careful approach to PPPs. It should also recognise that PPPs pose many of the same problems inherent in procurement or privatisation and are not a panacea for development. There is need for the Government to establish clear operational guidelines with respect to:

- Acceptable forms of PPPs and their prioritization;
- Procedural clarity on the basic steps in establishing PPP projects (conceptualization and initiation);
- Basic approaches to risk allocation, value for money and principles around the provision of guarantees;
- Financial and budget evaluation criteria;
- Approaches to regulation (especially cross-sectoral considerations);
- Parameters for the management of privatisation issues (retrenchments, empowerment, etc.);
- Project feasibility appraisal criteria;
- Authorization procedures;
- Recourse procedures and dispute resolution; and
- Treatment of unsolicited bids

The Government intends to establish a Public Private Partnerships (PPP) Unit. There are two key tasks that must be done before the Unit is operational as a Unit within the Privatisation Commission. Firstly, there is a need to review, analyze, and recommend draft amendments to existing legislation clarifying the power and authority of local and central governments as well as public enterprises to enter into long-term contractual arrangements with private sector service providers. Secondly, there is a need to develop minimum standards and regulations governing PPP contracts. There is a strong possibility that existing laws will be amended so that PPPs can become a more widely used option for government managers. The expected PPP framework would then lead to a transparent and successful development of infrastructure projects and services in Kenya.

The PPP Unit will need to establish policies and procedures for preparing and packaging projects, and ensure quality control over these activities. A well established and operated PPP unit should help strengthen investor confidence in the government's ability to facilitate responsible private sector participation in key sectors. Any PPP initiatives undertaken without creating an environment conducive for investing in PPP projects could result in a low uptake rate and high perceived risks, both of which can be detrimental to investor confidence.

A number of PPP projects are either on-going or at various stages of project development. The success of these PPPs will depend, to a large extent on the establishment of a strategic framework comprising of: a clear guiding policy; appropriate legal provisions and institutional set up capable of efficient implementation of PPP projects; standard procedural guidelines for the process; and adequate transaction, technical, contract management and project monitoring expertise. Capacity building in project planning, co-ordination and monitoring of PPP projects

among public officers is another essential element required to strengthen the implementation capacity. The overall implementation framework will ensure that PPP implementation is uniformly coordinated and managed to optimise expected outcomes for Government.

A comprehensive policy, legislative and institutional framework has already been passed in Kenya to serve the needs of the Government's privatisation programme. Among other things this framework provides for implementation of non-privatization transactions, such as PPPs, under the Privatization Commission and the established legal framework and process if the Government considers it necessary. In this respect it is possible to blend a framework for PPPs into that for the privatisation programme with suitable enhancements to cater for the formal and institutional needs of a PPP programme. Specifically there will be need to provide for strong post closure contract management.

As the set of skills needed to implement a privatisation programme are similar in many respects to that needed to implement PPPs, the PPP programme is likely to benefit from the legal framework which has already been passed by Parliament, the oversight of the Commission and transaction and infrastructure skills available under the Commission. Meanwhile before the Commission is fully established, it would be possible for the PPP programme to benefit from the transaction and infrastructure development expertise available in the Department of Government Investments and Public Enterprises (DGIPE), which is currently representing the Treasury in matters relating to PPPs. In the long run it would also be possible for the Programme to benefit from capacity created under the Commission once the privatization programme is phased out. Placing the PPP unit under the Privatization Commission would also enable the PPP unit to pay reasonable/market rates of remuneration to enable the Unit to attract the required expertise.

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