PUBLIC-PRIVATE PARTNERSHIP TOWARDS GROWTH & DEVELOPMENT: IS IT WORKING?*

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INTRODUCTION

"The State recognizes the indispensable role of the private sector, encourages private enterprise, and provides incentives to needed investments."[1] This is the constitutional mandate that acknowledges the vital role that the private sector necessarily plays in national growth and development. This is the underlying principle behind the policy and the implementation of the Public-Private Partnership ("PPP") program with the end of accelerating national infrastructure development and ensuring sustainable economic growth in mind. This is not a new thrust that the current Philippine Administration spearheaded but a mere continuation of the Build-Operate-Transfer ("BOT") program, which had been in existence since the early 1990s. As privatization in the form of BOT projects has been around for more than two decades now, it is time to make a review and an assessment of whether or not it meets the expectations it was meant to answer for.

The following are the questions we have to ask: Who really benefits from privatized infrastructure projects? Who determines what infrastructure is needed? Where and when are these projects undertaken? Who should shoulder the costs and risks of infrastructure development? Perhaps, ultimately, the question is, are PPP/BOT projects able to contribute to the growth and development of our nation?

It is in this light that this brief commentary lays down the following objectives: (1) to thresh out how the PPP/BOT scheme works, (2) to assess how far we have gone with the utilization of the PPP/BOT scheme as a mode

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[1] CONST., art. II, § 20.

of privatization, and (3) to determine whether the PPP/BOT scheme has served and continues to serve as a mechanism of growth and development for the country.

PHILIPPINE POLICY ON PRIVATIZATION

It is the "declared policy of the State to recognize the indispensable role of the private sector as the main engine for national growth and development and provide the most appropriate incentives to mobilize private resources for the purpose of financing the construction, operation and maintenance of infrastructure and development projects normally financed and undertaken by the Government."[2] This recognition of the essential role of the private sector as a mechanism of national growth and development makes the privatization program an integral part of the government's economic policy of liberalizing its economy and attracting further international investments. In conjunction with its far-reaching privatization program, the Philippines, for several decades now, has been actively encouraging and pursuing private sector participation in many key economic sectors such as power, telecommunications, and public transportation. However, regardless of the sector, what lies at the heart of the debate is the growing importance and the increased concern with economic performance and its contribution to the development process.

THE CONCEPT OF PRIVATIZATION

Privatization, in general, refers to the interest of reducing the role of the state in national economies while enhancing the scope of private ownership as well as the participation of the private sector. There are three main approaches to privatization. The first and most common usage refers to a change or a transfer of ownership of an enterprise from the public sector to the private sector as in an outright sale of governmental holdings. The second mode of privatization involves the liberalization, or deregulation, of entry into activities previously restricted to public sector enterprises. This may involve the subcontracting of government services to private undertakers. The third

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[2] Rep. Act. No. 6957, § 1 (1990). This is the Act Authorizing the Financing, Construction, Operation and Maintenance of Infrastructure Projects by the Private Sector and for other Purposes, as amended by Rep. Act No. 7718 (1994).

sense in which the term has been used is where the provision of a good or service is transferred from the public to the private sector. Here, the subcontracting would already involve the financing and development of the facility.

Whatever the mode, privatization has come to mean an economic policy reform embraced by many countries to achieve sustainable growth. It is fiscal in nature and appealing to both governments of developed and developing nations because it offers a quick solution to persistent fiscal deficits brought about by the inability of revenues to keep up with ever-increasing expenditures. As such, raising revenue has become a primary concern in privatization.

It should, however, be noted that other privatization goals are equally significant and important. These would include enhancing efficiency, broadening ownership base, promoting private enterprise and participation, providing for alternative means of delivery of services, and reducing the role of government in the market. Under a PPP arrangement, a level of cooperation between the government and the private sector is reached in order to meet public requirements.

In both theory and practice, privatization has always been rationalized and justified for the mentioned reasons. In addition, there are other factors why governments adopt a policy of privatization. Some of these factors are that: (1) public enterprise has become an unsustainable burden on the government's budget and the banking system; (2) public enterprise has yielded a disappointing rate of return on capital invested in them; (3) the costs of public enterprise may have exceeded the cost of market failures; and (4) poorly performing public enterprise have slowed the growth of the private sector in many developing countries. Despite these, recent evidence now shows that there is still a lot of economic benefit from privatization even if reform programs are not able to remedy the deficiencies of public enterprise.

THE BOT LAW: LEGISLATIVE HISTORY

The BOT scheme is not new. It was first officially recognized in the world as an approach to privatization in 1984, when the first BOT private facility was put up in Turkey as part of an enormous privatization program to

develop new infrastructure.[3] The scheme caught on and began to be utilized as an alternative means of meeting infrastructure requirements.

In the Philippines, the forebear of all BOT legislation was Executive Order ("E.O.") No. 215[4] issued by the Office of the President in 1987. It permitted private sector (Independent Power Producers or "IPP") participation in the construction and operation of power generation projects. This was largely significant because prior to this, the government through the National Power Corporation ("NAPOCOR") had a monopoly in the operation and maintenance of power plants and of the generation of electric power in the country. By the government's declaration of support for private power BOT projects, it effectively ended the monopoly of NAPOCOR in terms of power generation and development. Private sector involvement in the power industry became essential given the urgency and the level of capital expenditure necessary to implement the power expansion and maintenance program.

In 1990, the government enacted Republic Act ("R.A.") No. 6957, commonly referred to as the Build-Operate-Transfer Law or the BOT Law. It authorized a number of government -owned and -controlled corporations ("GOCCs") to enter into BOT and Build-Transfer ("BT") or turnkey contracts with private sector participants in traditional infrastructure development projects such as power, transportation, and telecommunications.

The BOT Law was passed in the hopes that it would encourage the private sector to become the nation's driving force for growth and development by engaging in or undertaking the financing, construction, operation, and maintenance of private sector infrastructure and development projects. The first BOT Law "aimed to minimize the burden of infrastructure projects on the national government budget, minimize external borrowing for infrastructure projects, and use the efficiency of the private sector in delivering public good."[5] In return, the government should provide the appropriate financial incentives, a climate of minimum regulations and procedures, and specific government undertakings in support of the private sector.

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[3] General information on public-private partnerships in Turkey (2010), *available at* worldbank.org *and* www.oib.gov.tr.

[4] Exec. Order No. 215 (1987). This is entitled "Amending Presidential Decree No. 40 and allowing the Private Sector to Generate Electricity."

[5] Initiatives for Dialogue and Empowerment through Alternative Legal Services v. Power Sector Assets and Liabilities Management, G.R. No. 192088, Oct. 9, 2012.

By the BOT scheme, one refers mainly to "the contractual arrangement where the contractor undertakes construction, including financing, of a given infrastructure facility, and its operation and maintenance. The facility is operated over a fixed term during which it is allowed to charge facility users appropriate tolls, fees, rentals and charges sufficient to enable the contractor to recover its operating and maintenance expenses and its investment in the project plus a reasonable rate of return or profits. At the end of the fixed term, the facility is transferred to the government implementing agency or local government unit." [6] Effectively, "a private party or concessionaire retains concession for a fixed period from a public party called a principal or a client, for the development and operation of a public facility. The development consists of financing, design and construction of the facility, managing and maintaining the facility adequately and making it sufficiently profitable. The concessionaire secures return of investment by operating the facility and during the concession period, the concessionaire acts as the owner. At the end of the concession period, the concessionaire transfers ownership of the facility free of liens to the principal at no cost."[7]

In 1994, R.A. No. 7718 was passed amending and enhancing the provisions of R.A. No. 6957. It broadened the scope of the law by adding to the list of possible implementing agencies, by putting in place and clarifying provisions on incentives for attracting private sector investments, and by now allowing both unsolicited proposals[8] and direct negotiation of contracts,[9]

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[6] Rep. Act. No. 6957, § 2 (1990), *amended by* Rep. Act No. 7718 (1994).

[7] Sebastian Manheere & Spiro Pollais, *Case Studies on Build Operate Transfer* (1996), *available at* http://www.gsd.harvard.edu/images/content/5/3/538865/fac-pub-pollalis-bot-part-1.pdf.

[8] Rep. Act. No. 6957, as amended, § 4-A. "*Unsolicited Proposals*. Unsolicited proposals for projects may be accepted by any government agency or local government unit on a negotiated basis: *Provided*, That, all the following conditions are met: (1) such projects involve a new concept in technology and/or are not part of the list of priority projects, (2) no direct government guarantee, subsidy or equity is required, and (3) the government agency or local government unit has invited by publication, for three (3) consecutive weeks, in a newspaper of general circulation, comparative or competitive proposals and no other proposal is received for a period of sixty (60) working days: *Provided, further*, That in the event another proponent submits a lower price proposal, the original proponent shall have the right to match that price within thirty (30) working days."

[9] Rep. Act. No. 6957, § 5-A (1990), *amended by* Rep. Act No. 7718 (1994). "*Direct Negotiation of Contracts*. – Direct negotiation shall be resorted to when there is only one complying bidder left as defined hereunder:

provided they comply with the conditions set forth in the law. It expressly allowed the use of other arrangements or other variants, such as build-transfer-operate ("BTO") and build-own-operate ("BOO"), and existing power plants were also offered to the private sector on medium- and long-term lease, management contracts on rehabilitate-operate-maintain ("ROM") and rehabilitate-operate-lease ("ROL") terms. In fact, variations of the BOT format may be limited only by the imagination and the letters in the alphabet, with the issue of ownership of the infrastructure facility and equipment as may be approved by the President as the most significant difference among them. A final innovation was the inclusion of non-traditional infrastructure sectors like education, health, and agriculture.[10]

Another law that contributed to the proliferation of the utilization of the BOT scheme (and its other variants), was the passage of the Electric Power Crisis Act of 1993 ("EPIRA") "giving the President emergency powers to urgently address the power crisis in the country."[11] It provided for the full implementation of the restructuring and privatization of the power industry, thus effectively reaffirming private sector participation in the power sector. This ensured increased participation to such an extent that by the end of 1998, IPPs accounted for about 48% of total installed generating capacity in the Philippines.[12]

Historically, the government has always initiated infrastructure

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(a) If, after advertisement, only one contractor applies for prequalification requirements, after which it is required to submit a bid/proposal which is subsequently found by the agency/local government unit (LGU) to be complying.

(b) If, after advertisement, more than one contractor applied for prequalification requirements, after which it submits bid/proposal which is found by the agency/LGU to be complying.

(c) If, after prequalification of more than one contractor, only one submits a bid which is found by the agency/LGU to be complying.

(d) If, after prequalification, more than one contractor submit bids but only one is found by the agency/LGUs prequalification bids and awards committee within fifteen (15) working days to the head of the agency, in case of national projects or to the Department of Interior and Local Government, in case of local projects from the date the disqualification was made known to the disqualified bidder: *Provided, furthermore,* That the implementing agency/LGUs concerned should act on the appeal within forty-five (45) working days from receipt thereof."

[10] Rep. Act. No. 6957, § 2(a) (1990), *amended by* Rep. Act No. 7718 (1994).

[11] Initiatives for Dialogue and Empowerment through Alternative Legal Services v. Power Sector Assets and Liabilities Management, G.R. No. 192088, Oct. 9, 2012.

[12] NAT'L. POWER CORP., ANNUAL REPORT AND PROSPECTUS (1998).

development in the Philippines, and this is true as well with the rest of Asia. The government directly undertook project finance and risks through an implementing state agency or enterprise that would contract out to the private sector for supply and construction. The only risk taken by suppliers and contractors was the government's ability to pay. The BOT scheme was aimed towards obtaining infrastructure facilities with greater efficiency and speed without the state taking an adherent financial responsibility. It was an approach where private investors received a concession to finance, build, and operate a facility over a set period of time, in exchange for the right to charge the users of the facility at a reasonable rate to make the investment commercially viable. At the end of the concession period, the facility is turned over to the state. Essentially, the system requires that the facility pay for itself on a commercial basis, through the implementation of the "user-pays" principle. Private investors take on the long-term risks of financing, developing, and managing the infrastructure facility based on potential commercial rewards. Such risks revolve mainly on operation, market, cash flow, foreign exchange fluctuations, competition, inflation, and force majeure.

The privatization policy in the Philippines did not originally envision nor cover public infrastructure projects under the BOT and other related schemes. However, as it gained popularity and recognition, the legal mandate to privatize has been expanded to include such activities as BOT and other related schemes, leasing, and management contracting. In fact, in the enactment of the BOT law and its Implementing Rules and Regulations ("IRR")[13] emphasis was placed on the following overall objectives, to wit: (1) to tap greater private sector participation in the provision of infrastructure facilities, (2) to allow government to extend the provision of basic infrastructure, and (3) to strengthen the regulatory and supervisory capabilities of concerned government agencies. The BOT Center also stressed policies and strategies that aimed to expand private sector participation and integrated planning, shifting infrastructure investment from highly developed mega-centers to regional centers as well as the interface with agro-industrial development and environmental management.

In the Philippines, initial BOT projects were a way of dealing with an emergency situation. At a time when it was faced with extensive power blackouts that made investors bypass the country, as well as severe financial difficulties, the government found that it would be easier to focus on the

[13] Implementing Rules and Regulations of Rep. Act. No. 6957, as amended (1994).

essentials that would attract private investment into BOT power generation plants. It was then that the Fast Track Power Projects of the NAPOCOR were conceived. A strong legal basis as well as increased confidence among investors gave the government the ability to take steps that demonstrated the high degree of consensus in the public and private sectors over the basic need to obtain electric power, no matter the cost. And because of the circumstances under which these projects were completed, admittedly pricing was at a premium.

Success was based on making the procurement of new generating capacity through private investment virtually the sole aim of the BOT program. The only criteria imposed on pricing was reasonableness; thus, negotiations concentrated on how investors and their funding institutions would benefit from their investments. The Republic virtually guaranteed NAPOCOR's payments in their Power Purchase Agreements as well as against its foreign exchange risks, which downplayed the perceived high-risk environment of the Philippines that might discourage investors. It was only later, when the environment for BOT projects stabilized, that the government began to address other issues, including competitive pricing and supply. As a result, the country had the most successful independent power-producing BOT program in the Asian Region in the 1990s.

NAPOCOR's policy at the time was to invite private participation in all new power plant developments for which it was responsible. In order to select private sector participants, it conducted a tender process as required by law to do before awarding the contract to the most competitive bidder. For BOT projects, NAPOCOR developed a model project documentation consistent with the law and pursuant to which the private contractor undertook the construction and financing of the power plant and operated and maintained the plant for a period ranging from 10 to 25 years. NAPOCOR agreed to supply the operator with the necessary fuel resources to operate the plant, thereby assuming the risk of fuel price fluctuations. NAPOCOR and the operator also agreed that the latter would purchase the power produced at a price that enabled the operator to recover its operating and maintenance expenses and its capital investment in the project, plus a reasonable rate of return. At the end of the fixed term, the contractor would have to transfer the plant to NAPOCOR or to the government.

Variations of the BOT scheme included the BT, BTO, and BOO. NAPOCOR was also permitted to enter into ROM or, alternatively, ROL

contracts with private enterprises for its existing facilities. Under such arrangements, the contractor undertook and financed the rehabilitation of the plant, and then operated and maintained it, or leased it, typically for a period of up to 15 years.

By June 30, 1996, NAPOCOR had completed 25 power projects with the private sector to produce an aggregate capacity of 4,173 MW. Six of these projects were to rehabilitate the company's existing plants. Several new private power plants were commissioned in 1994 and 1995, which were scheduled to commence operations between 1996 and 2003. These would later provide an additional 6,236 MW of capacity.[14]

The BOT privatization program of the government has expanded to other infrastructure sectors since then. And while far from perfect, these may nevertheless be considered huge steps towards relieving the government of its great financial burden. A burden which, had the government been forced to take it on by themselves, would surely have taken away valuable financial resources that would otherwise have been better utilized for education, health, and other basic services. The increasing needs of society and the public in general have placed a huge demand for the expansion and improvement of the physical infrastructure and service delivery by the government. The inability of the government to meet the concomitant needs of its public has forced them to turn to privatization in order to meet this demand. This strategy is chosen on the basis of the most fundamental features, that of rapid and efficient satisfaction of demand for infrastructure services in order to sustain economic growth. It also features the improvement in the implementation and management of infrastructure development that will maximize the return of investment and reduce fiscal pressures on government and its restriction of the growth of the public bureaucracy and state-owned enterprises. Finally, it inculcates into the public the principle of "user-pays," so that infrastructure facilities can become more self-financing.

E.O. NO. 8 AND THE PUBLIC-PRIVATE PARTNERSHIP PROGRAM

On September 9, 2010, E.O. No. 8[15] was promulgated in an attempt

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[14] NAT'L. POWER CORP., ANNUAL REPORT AND PROSPECTUS (1996).

[15] Revised Implementing Rules and Regulations of Rep. Act. No 6957, as amended (2012).

to revitalize the program by reorganizing and renaming the BOT Center to the Public Private Partnership Center and transferred its attachment from the Department of Trade and Industry ("DTI") to the National Economic and Development Authority ("NEDA"). This transfer perhaps indicates the thrust that the PPP program is intended for economic development.

The general description of PPP infrastructure or development projects do not depart much from the former definition of BOT projects discussed above. The legal basis remains the same: R.A. No. 6957 as amended by R.A. No. 7718. They remain as projects which are normally financed and operated by the public sector but which will now be wholly or partly implemented by the private sector.

Under the new law, however, possible projects were expanded and can include power plants, highways, ports, airports, canals, dams, hydropower projects, water supply, irrigation, telecommunications, railroads and railways, transport systems, land reclamation projects, industrial estates or townships, housing, government buildings, tourism projects, markets, slaughterhouses, warehouses, solid waste management, information technology networks and database infrastructure, education and health facilities, sewerage, drainage, dredging, and other infrastructure and development projects that may be authorized by the appropriate implementing agency, be it an executive department or a local government unit ("LGU"). These projects must be implemented by way of a contractual agreement either under the BOT or BT schemes or under any of the other variants approved by the President.

For the construction stage, the project proponent may obtain financing from foreign and/or domestic sources and engage the services of again either a foreign or Filipino contractor. Limitations imposed by nationality laws apply where the project's operation requires a public utility franchise, in which case the facility operator must be a Filipino corporation or at least 60% owned by Filipinos.[16] The Revised IRR was published and became effective in October 2012,[17] notably two years from the time that E.O. No. 8 was promulgated.

IMPLEMENTATION OF PPP/BOT PROJECTS: THE PROS AND CONS

[16] Rep. Act. No. 6957, § 2 (1990), *amended by* Rep. Act No. 7718 (1994).

[17] Revised Implementing Rules and Regulations of R.A. 6957, as amended, (2012).

The launching of the privatization program took into account many considerations, among which are the need for government to focus its energies and resources in providing basic goods and services, as well as the desire to create a favorable investment climate for the private sector by eliminating undue competition from government corporations. In the initial stages, the government's policy of privatization was directed more towards the offering of its holdings on GOCCs for outright sale and transfer to the private sector, thereby realizing value as well as encouraging competition. The program was viewed as a way to broaden public ownership of government properties in order to develop a capital market, to minimize government losses, and to generate resources for priority development projects or programs. It was seen as a suitable means to expose government to market discipline and competition in order to improve efficiency and make their operations more responsive to consumer needs. It was meant to help lessen their reliance on government subsidies, tax exemptions and guarantees and expand economic activity through greater investment by the private sector.

Increased private sector investment in infrastructure projects offered the twin benefits of additional funds and more efficient provision. This summarizes the thrust for the argument in favor of the PPP/BOT scheme. It enables the private sector to invest directly in infrastructure projects, which reduces the drain on the use of public funds. As the private sector operates on a commercial basis, it is assumed that efficiency will also improve. Public infrastructure is created without having to invest public money. Moreover, this arrangement can help facilitate technology transfer.

The advantages resulting from the utilization of the BOT model would be that it allows governments to develop needed infrastructure through flexible financing structures without incurring a substantial financial burden on its budget. It intended for a rapid scaling of operations to provide a wider offering of services that would hopefully fill business model gaps. Also, because private firms are more focused on efficiency than the public sector, they are generally more cost-effective, with the objective of at least trying to lower operating costs, to increase capital investments, and to utilize the most up-to-date and efficient technologies. There is reduced infrastructure set-up cost while shortening the timeline to operations through the utilization of third party know-how (technology transfer) in the management of resources. The strength of the BOT model is that it uses these private sector objectives to revitalize infrastructure development and augmentation using a proper

combination of strategic and financial value. The BOT model has also proven to be effective in numerous forms of capital-intensive infrastructure projects aside from power generation, extending even to road networks, transportation, port and airport facilities, correctional facilities, waste water treatment plants, and solid-waste-to-energy plants, to mention a few.

On the other hand, the imperative behind mechanisms like the BOT goes beyond the pro-market rationale that looks to resolve problems of limited funding and resources and an increasingly complex regulatory framework. While the supposed benefits of the BOT model are based more on free market ideology, the notion that BOT is a way of creating public infrastructure at little or no cost to the public hinges on a fallacy or is, perhaps at best, illusory.

At the outset, we must accept that the utilization of the BOT scheme and its variants is a business proposition and is thus predicated on the idea that investors must be certain that they can recoup a reasonable rate of return on their investment as well as make an adequate profit thereon. Many of the initial BOT projects became financial successes because they had the opportunity to optimize the economic rate of return that necessarily conflicted with the public interest. For the private sector, the determination of what is a reasonable rate of return on investment may be higher than if it were the government that implemented the project and operated the public service. The arrangement is grounded on the presupposition that in the end it is the public sector that pays. Thus, it is the users, the consumers, the taxpayers, and/or the state that ultimately pay the cost of the project. Because of this, perhaps another disadvantage may be that privatizing public infrastructure facilities may lead to a form of 'flat' taxation or imposition where only those who can afford to pay have access to the facility or service. This can result in reduced access to essential public facilities and services by those with the lowest capacity to pay, contributing to increased social inequality.

Given that large-scale infrastructure projects are more complex in their development, they are thus generally associated with cost overruns, uncertain economic viability, and social and environmental risks, rather than with high profitability. Private investors have proven to be reluctant to go near such ventures, unless governments and/or international financial institutions are willing to provide various forms of subsidies and incentives. In turn, the government, can provide such subsidies in order to lighten the

financial burden of the private sector concessionaire by retaining controlling interest over the development of the project and by allocating project money to make it more viable. Typical subsidies include investment grants, public financing of social and environmental mitigation measures, and application of state controls to restrict competition and alternatives. In contradiction to the "free market" ideals used to promote privatization, such subsidies tend to distort and undermine market realities, generate waste and corruption, and lead to less accountability in the use of public resources.

Project risks include all factors or eventualities that cannot be definitively predicted and incorporated in the project cost. The larger and more complex the project, the greater too are the risks. Risks are generally categorized into commercial, political, or legal, normally shared by the public and the private sector. The private sector usually takes care of the commercial risks, while the government takes on the political and legal risks. Typical risks can include unforeseen engineering problems, cost and time overruns, currency exchange variations, unreliable market and demand projections, environmental and social costs, project repatriation, and amendments in the legal and regulatory framework, including taxation policies and political uncertainties.

The notion that the private sector is inherently more efficient and less wasteful than the state can only be supported in situations of vigorous competition. However, it would appear that this free market condition tends to be absent in public infrastructure projects.

In many instances, foreign investors are often unable to secure financing for large infrastructure projects especially in developing countries, unless there is a significant level of "government equity" to ensure political commitment to the project. Equally noteworthy is that, as a matter of rule, government debt is ordinarily cheaper than private debt to finance PPP/BOT projects. There is therefore an increase in the value brought about by private borrowing. This, however, transfers the locus of the risks to the state. The primary goal and interest of private developers in a BOT project is naturally to ensure adequate return on their investment before the end of the concession period. For the developer, there may be little or no incentive to ensure that the facility remains financially or technically viable after it has been transferred to the government. Maintenance and capital replacement costs are likely to be kept at a minimum, especially close to the transfer date. With many of these projects, it may be relevant to ask if the state will ultimately inherit an asset or a

liability. It is also relevant to determine if the original intention was really only for the duration of the concession period, and if it has sufficiently benefited from the fact of the arrangement alone.

The private sector will, of course, be interested only in projects or enterprises that have the greatest potential to be 'commercially' profitable. Projects that do not have such potential, though they may be equally or even more vital for the provision of an essential public service, will be left for the government and taxpayers to finance. This means that there will always be market-driven tendency to transfer profit-generating activities to the private sector, while transferring non-profitable activities to the state. This helps to further perpetuate the notion that state-sponsored projects and enterprises are less efficient than those of the private sector.

While the application of the BOT scheme seems to depend heavily on mechanisms that will guarantee the private sector against loss, there seems to be no corresponding mechanism guaranteeing that the projects will lead to net gains and benefits for the government and the people concerned. At present, there appears to be no reliable cost-and-benefit analysis of PPP/BOT projects to tell us if it contributes to the growth and development of the country and its economy. Advantages and disadvantages must merely be weighed against the intricacies and rigidity of the contractual arrangement or scheme in general.

PPP/BOT PROJECTS IN LGUS

The reforms and the application of the PPP/BOT program have been duplicated in the LGUs as well. It is interesting to see the contrast in the employment of such schemes in various projects that have thus far been put up in the national as against the local milieu.

The passage of the Local Government Code of 1991 enhanced the governmental and corporate powers of LGUs, which are granted full autonomy in the exercise of proprietary rights.[18] It encouraged the participation of the private sector in local governance, particularly in the

[18] Rep. Act. No. 7160, § 22(d) (1991). "Local government units shall enjoy full autonomy in the exercise of their proprietary functions and in the limitations provided in this code and other applicable laws."

delivery of basic services to ensure the viability of local autonomy as an alternative strategy for sustainable development.[19] Furthermore, the LGUs now have the power to enter into and secure (1) loans, credits and other forms of indebtedness,[20] (2) sell bonds,[21] and (3) BOT arrangements and joint ventures with the private sector.[22]

A main feature of the provisions was for the active partnership and participation of Non-Governmental Organizations, People's Organizations, and the local private sector with the LGU in development work. Participation in governance has opened up considerably, and examples in the implementation of delivery of basic services in joint undertakings between the private sector and the LGUs abound.

However, like any reform, the Local Government Code and the innovations provided therein must be utilized and implemented in order for them to have any impact in the struggle to achieve sustainable growth and development at the local level. We have many examples of communities that have demonstrated how people-centered initiatives, and partnerships among and between the government, non-government organizations, people's organizations and the business or private sector can become realities. While there are many success stories, these must be considered in the context of the Local Government Code, which provides an enabling environment that allows for such innovations to flourish. The provision for enhanced governmental and corporate powers to LGUs granted them full autonomy in the exercise of proprietary rights. For the purpose of this paper, we look at the importance and the role of PPP/BOT projects as a growth mechanism for LGUs, not only for the delivery of basic needs and services that allow them to achieve growth and development but also to determine if the benefits that have been envisioned for the PPP/BOT schemes trickle down to the local level.

The various types of LGU-PPP/BOT Projects that have thus far been entered into in the local level revolve mostly around the following project types: (1) property development, (2) transportation, (3) information technology, (4) water system, and (5) other projects, such as industrial/special economic zones. These projects, unlike their national counterparts, were smaller in scale in terms of magnitude, complexity, and cost. As of June 30,

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[19] § 3.
[20] § 297.
[21] § 299.
[22] § 302.

2001, there are 36 projects, in various stages of completion and implementation, listed on the LGU Project Summary List of the Coordinating Council for Private Sector Participation. Examples of some projects implemented in the past included public markets, administrative and commercial centers, integrated bus terminals, ferry ports, water supply systems, and information technology projects. This mix showed a promising number and diversity of projects—a far cry from the two LGU projects currently listed with the PPP Center as of 2013.

Perhaps the numerous problems that were encountered and the considerable difficulties in attracting investors are the reasons for the decrease in the number of projects now being implemented. At the time, local chief executives literally had to chase after businessmen in order to convince them to bid on the projects. A reason for this would probably be that, during the early 1990s, the Gulf War started. This led to uncertainties regarding the oil prices not only in the Philippines but also the rest of the world. Many of the interested parties were not willing to take risks, like cost overruns and inflation, debt service interruption risks, and completion risks associated with the projects, all of which would make their bids less attractive. A number of institutional and regulatory issues had to be addressed in the implementation of the projects and in order to ensure investor interest; LGUs had to champion the projects. Local chief executives had to constantly underscore the importance and value of the projects, and the packaging of projects established had to be flexible in order to become attractive to all parties involved. Finally, in evaluating the projects, indirect costs and benefits were included.

What are the possible reasons why the private sector has shied away from entering into PPP/BOT projects as of late, such that there are fewer projects both in the national as well as the local level now than when we started in the early 1990s? The PPP Center, set up under E.O. No. 8, makes PPP "a cornerstone strategy of the national development plan to accelerate the infrastructure development of the country and sustain economic growth."[23] "The administration further pledges to provide the enabling environment for private sector investment through a stable macroeconomic and sound and consistent public policies."[24] Pronouncements, however, must be put to practice and actually implemented to institute the proper reforms. There must be no disparity in application by all the branches of government.

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[23] PPP Center Manual for LGUs, Vol. I (2010).

[24] *Id.*

There are several decisions of the Supreme Court that suggest a different interpretation of these policies. The first series of decisions promulgated by the Supreme Court are in relation to the "real property tax implications of a BOT agreement between a GOCC that enjoys tax exemption and a private corporation. Specifically, under the terms of the BOT agreement, can the GOCC be deemed the actual, direct, and exclusive user of machineries and equipment for tax exemption purposes? If not, can it pass on its tax-exempt status to its BOT partner, a private corporation through the BOT agreement?"[25] Here, the court ruled that "the exemption under the law does not apply because BPPC (the private sector concessionaire) is not a GOCC – it is an independent power corporation currently operating and maintaining the power plant pursuant to a BOT agreement. The BOT agreement cannot be the basis for the claimed exemption; tax exemption cannot be agreed upon by mere contract between the parties, as it must be expressly granted by the Constitution, statute, or franchise."[26]

This is followed by the case of *National Power Corporation v. Province of Quezon and the Municipality of Pagbilao*,[27] where the Court held that "the tax liability must be a liability that arises from law, which the local government unit can rightfully and successfully enforce, not the contractual liability that is enforceable only between the parties to the contract. In the present case, the Province of Quezon is a third party to the BOT agreement and could thus not exact payment from NAPOCOR without violating the principle of relativity of contracts."[28]

Thus, in the two cases, the private sector concessionaire or contractor becomes liable for local taxes which originally were supposed to be shouldered by the implementing agency as part of its sharing in the risks of the project. It is normal for the government to take on the risks related to the legal and political framework, including taxation policies, political uncertainty, and expropriation, as it is the party best suited to manage these risks. This is a major concern as it affects the bankability of the project. As a rule, risks should be balanced and properly allocated between the private sector and the public sector. If all risks are given to the private sector, then we can expect

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[25] National Power Corporation v. Central Board of Assessment Appeals, G.R. No. 171470, Jan. 30, 2009.

[26] *Id.*

[27] G.R. No. 171586, Jan. 25, 2010.

[28] *Id.*

them to just pass it on to the end-users or consumers. In the end, the taxpayer is still the one that pays.

In the case of *Alvarez v. People*,[29] Efren L. Alvarez, mayor of the Municipality of Muñoz, Nueva Ecija, was charged and convicted criminally for violation of Section 3(e) of R.A. No. 3019[30] or the Anti-Graft and Corrupt Practices Act, for acts done in connection with a BOT agreement. The issue concerns the Wag-wag Shopping Mall project that he entered into for and in behalf of the Municipality of Muñoz. He was charged for gross and inexcusable negligence, even if bad faith was not attendant, in approving the proponent's proposal notwithstanding its failure to comply with the minimum legal requirements that prevented the Sangguniang Bayan from properly evaluating said proponent's financial and technical capabilities to undertake the BOT Project. His conviction was based on gross negligence evident from the taking of shortcuts in the bidding process and the non-observance of the NEDA-ICC guidelines. The implication of the decision is disheartening in that it discourages other LGUs and its officials from entering into similar arrangements under the PPP/BOT schemes. Admittedly, one of the problems that may be encountered in projects like these is the complexity of the development process, starting from pre-bid, financial closing, and construction, all the way to the maintenance and operation of the facility. There may be as many as 30 to 40 contracts, perhaps even more, among those involved in the project. In the case at bar, what was possibly lacking were the legal and technical know-how in terms of policy guidance and advice on legal matters, the process of selection as well as of approving or rejecting proposed PPP/BOT projects, and the provision of technical support and capacity building or training on the part of the public sector officials. It is important that the implementing agency, whether the national government or LGU, has a clear understanding of the basic requirement that the PPP/BOT project must meet.

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[29] G.R. No. 192591, Jul. 30, 2012.

[30] Rep. Act No. 3019, § 3 (1960). "In addition to acts or omissions of public officers already penalized by existing law, the following shall constitute corrupt practices of any public officer and are hereby declared to be unlawful:

. . .

(e) Causing any undue injury to any party, including the government, or giving any private party any unwarranted benefits, advantage or preference in the discharge of his official administrative or judicial functions through manifest partiality, evident bad faith or gross inexcusable negligence. This provision shall apply to officers and employees of offices or government corporations charged with the grant of licenses or permits or other concessions."

Finally, cases like *Agan v. Philippine International Air Terminals Co., Inc.*,[31] *Republic v. Gingoyon*,[32] and *Asia's Emerging Dragon Corporation v. Department of Transportation and Communications*[33] illustrate the ultimate legal risk that investors face in PPP projects—a decision of the Supreme Court that the concession agreement entered into by the project company with the government is void and, worse, at the instance of third parties. Unfortunately, despite a growing clamor by the private sector, no government approval or opinion can assure the investors that the concession agreement is free from a successful legal challenge.

RECOMMENDATIONS

While in many cases, infrastructure projects answer primarily to the needs of the industry, the private sector, and general economic growth, we can perhaps conclude that these are justified on the premise that everyone will eventually benefit from the economic growth and industrialization that it will bring about. We hope that the benefits would eventually trickle down to all sectors of society and bring about renewed vitality to the LGUs and the entire country to achieve growth and development. This is our ideal end goal. However, before we can attain all of this, it is necessary to make substantial reforms that will improve the implementation of our PPP/BOT projects that will make them more desirable, bankable, and competitive.

To do this, it will be necessary to review the existing laws and implementing rules and regulations relating to R.A. No. 6957, as amended by R.A. No 7718, to allow for the simplification of procedures that will in turn provide for the needed flexibility in the system that will give us a clear understanding of the basic requirements that PPP/BOT projects must meet. It must take into consideration the variations as well as the types of projects that can fall under the BOT scheme. It must give us clear policy guidelines that will make it easy for us to go through the primary tasks from project identification to the completion of all the obligations created as a result of the project, taking care that such implementation abides by the generally accepted principles of good governance, transparency, accountability, regulatory efficiency, and

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[31] G.R. No. 155001, May 5, 2003.
[32] G.R. No. 166429, Dec. 19, 2005.
[33] G.R. No. 169914, Apr. 18, 2008.

fairness.

There is likewise a need to provide key actors in the scheme-specific incentives and to establish a supportive policy framework that will provide the enabling environment to encourage private sector investors to keep investing. Lastly it would be very important to develop an environment of low political risks. There should be enough commercial and ordinary risks in a project. It is not ideal for us to aggravate this with political risks that make the PPP/BOT projects less attractive and therefore less viable, such that it may need direct government support to make these projects viable. To do this, it is necessary to ensure that the allocation of risks, resources, and responsibilities are properly balanced between both the public and the private sector, and to place these upon the party best able to manage them.

CONCLUSION

The ultimate questions are: who really benefits from privatized infrastructure projects? Who determines what infrastructure is needed, and who should shoulder the costs and risks for infrastructure development? Why is it that relatively so few have utilized the BOT scheme as a mechanism of growth for their LGUs? These questions can only be answered given the specific design of a particular PPP/BOT project. There is no single correct formula, but what is certain is that given the recipe for success of the PPP/BOT scheme as a mechanism of growth and development, we must be careful in accurately incorporating the right ingredients.

The increasing needs of society and the public in general, have placed a huge demand for the expansion and improvement of the physical infrastructure and service delivery by the government. However, the inability of government to meet the concomitant needs of its public has forced them to turn to privatization, specifically the PPP/BOT scheme, in order to meet this demand. PPP/BOT or privatization in general has been utilized as a strategy that is chosen on the basis of the most fundamental features: that of rapid and efficient satisfaction of demand for infrastructure services in order to sustain economic growth and development. It features the improvement in the implementation and management of infrastructure development that will maximize the return on investment and reduce fiscal pressures on the government and its restriction of the growth of the public bureaucracy and state-owned enterprises. Finally, it inculcates into the public the "user-pays"

principle, so that infrastructure facilities can become more self-financing.

One thing is certain: the government cannot bring about growth and development by itself. It will have to partner with the rest of civil society, the private sector included, in order to reach this goal.

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