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**Research Article/Araştırma Makalesi**

## **The Institutional Dimension of Public-Private Partnerships: Governance<sup>1</sup>**

### *Kamu-Özel İşbirliklerinin Kurumsal Boyutu: Yönetişim*

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**Abstract**

Failure to realize governance objectives is considered to be one of the reasons why public-private partnerships have become increasingly controversial and why there have been many negative experiences during the project process. This study examines the relationship between public-private partnerships and governance. In the framework pioneered by international organizations and accepted in the literature, it is possible to eliminate many problems experienced in public-private partnership projects by implementing governance principles. On the other hand, although there are many discussions in the literature on the conceptual basis of governance, there are no studies that address these conceptual debates within the framework of public-private partnerships. It is thought that this deficiency in the literature will also leave the discussions on the present and future of the relationship between public-private partnerships and governance incomplete. The originality of this study is that it evaluates the concept of governance in public-private partnerships and its foundations based on the New Institutional Economics and New Public Management approaches. When the concept is considered together with its foundations, the question of whether governance principles can really be a solution to the problems of public-private partnerships becomes controversial. Although the focus of the study is not on this debate, it aims to open the door to further discussions on the subject.

**Jel Codes:** H39, H83, B15

**Keywords:** Public-Private Partnerships, Governance, New Institutional Economics, New Public Management

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## Öz

Yönetişim hedeflerinin gerçekleştirilememesi, kamu özel işbirliklerinin giderek tartışılmalı hale gelmesinin ve proje sürecinde yaşanan pek çok olumsuz deneyimin nedenlerinden birisi olarak düşünülmektedir. Bu çalışma, kamu özel işbirlikleri ve yönetim arasındaki ilişkiyi incelemektedir. Uluslararası kuruluşların öncülüğünü yaptığı ve literatürde de kabul gören çerçevede, yönetim ilkelerinin hayata geçirilmesiyle kamu özel işbirliği projelerinde yaşanan pek çok sorunun ortadan kalkması mümkündür. Öte yandan, literatürde yönetişimin kavramsal olarak nereden beslendiğine dair pek çok tartışmaya rastlansa da bu kavramsal tartışmaları kamu-özel işbirlikleri çerçevesinde ele alan çalışmalara rastlanmamıştır. Literatürdeki bu eksikliğin, kamu özel işbirliği ve yönetim ilişkisinin bugünü ve geleceğine dair yapılacak tartışmaları da eksik bırakacağı düşünülmektedir. Bu çalışmanın özgünlüğü, kamu özel işbirliklerinde yönetim kavramını Yeni Kurumsal İktisat ve Yeni Kamu Yönetimi yaklaşımına dayanan temelleriyle birlikte değerlendirmesidir. Kavram, dayandığı temelleriyle birlikte ele alındığında ise yönetim ilkelerinin kamu özel işbirliklerinin sorunlarına gerçekten bir çözüm olup olmayacağı sorusu tartışılmalı hale gelmektedir. Çalışma, odağı bu tartışma olmasa da konuya dair yapılacak sonraki tartışmalara kapı aralamayı amaçlamaktadır.

**Jel Kodları:** H39, H83, B15

**Anahtar Kelimeler:** Kamu Özel İşbirliği, Yönetişim, Yeni Kurumsal İktisat, Yeni Kamu Yönetimi

## 1. Introduction

Since the 1990s, when Public Private Partnerships (PPPs) started to become widespread, their debates have continued increasingly. These debates have been exacerbated because many PPP projects have been delayed, canceled, or resulted in significant public losses. On the other hand, in recent years, a perspective led by international organizations that strengthening governance tools can significantly reduce the problems of PPPs has become widespread (United Nations, 2008; World Bank, 2009; Organization for Economic Development and Cooperation, 2012).

There are a limited number of studies on the relationship between governance and PPPs both at the empirical and theoretical levels in the academic literature (Casady et al., 2017; Lee et al., 2018; Hammami et al.; 2006). Based on the studies in the literature, it is possible to say that there is a strong relationship between PPPs and governance. However, there is no deepening of where the issue conceptually feeds from. It is thought that the lack of this pillar of the discussion will also leave the discussions on the present and future of the relationship between PPPs and governance incomplete. Therefore, for a deeper understanding, it is important to discuss the relationship between them by including the conceptual dimensions of governance.

The roots of the relationship between PPPs and governance should be sought in the neoliberal transformation process that started in the 1980s. This process, led by Reagan in the USA and Thatcher in the UK, includes practices such as privatization, liberalization of capital movements, and others, eventually ending social welfare states. "The stability and structural adjustment" programs of the International Monetary Fund (IMF) and the World Bank (WB), called the "Washington Consensus," accelerated this transformation process. The word 'Washington' refers to the fact that the program originated in Washington and was shaped by the IMF, WB, US Treasury, Central Bank, and think tanks; the word 'consensus' refers to the strengthening of the market mechanism, the provision of financial and monetary stability, the downsizing of the public sector through privatizations, and the consensus on the economic model in which the state is given a secondary role (Zabcı, 2009: 41-42). However, the rigid market-oriented economic rules that coalesced around the Washington Consensus in the 1980s did not yield the expected results and became the target of increasingly frequent criticism. These criticisms include the inadequacy of the Washington Consensus to explain the economic success of East Asian countries, the lack of significant contributions of neoliberal policies to economic performance, and the (unnecessarily) harsh measures that have highly negative consequences for the poor (Saad-Filho, 2007: 198). In the new period, announced by Joseph E. Stiglitz at the WB Conference (1997) and expressed as the Post-Washington Consensus, debates on the transforming role of the state have become widespread, and concepts such as governance, openness, transparency, and accountability have become increasingly important. The main feature that distinguishes the Post-Washington Consensus from the market-oriented Washington Consensus is the state's reintroduction as a market regulator.

The theoretical basis of the transition from the social welfare state to the regulatory state model is the New Institutional Economics (NIE) and the New Public Management (NPM)

Approach. According to Hood (1991), NIE paved the way for administrative reforms such as competitiveness, user preference, transparency, and incentives, while the marriage of NIE and management approaches has revealed the idea of NPM. The NPM, by claiming that the social state approach enlarges the body of the state excessively and that the state has become an obstacle to individual freedoms, argues that the state's role should be limited and a transition should be made from public administration to public management. One of the main arguments of NPM is that the efficient management of the public sector positively affects the private economy and international competition. Therefore, what needs to be done for better economic performance in the changing global environment is the development of public management (Ömürgönülşen, 1997). Governance has been the tool for the neoliberal transformation process, which has evolved from NIE to NPM, replacing the social state approach. According to Bayramoğlu (2018), privatization, regulation/deregulation, and competition policies constitute the application forms of governance within the framework of NPM and Transaction Cost Theory<sup>3</sup>. The conceptual arsenal offered by the new institutionalist school has significantly contributed to the governance project's institutionalization at different scales.

The structure of PPPs is in direct harmony with the main arguments of the neoliberal transformation process. Therefore, the governance tool used to operationalize these arguments is also crucial for the effectiveness of PPPs. Studies prepared by international organizations such as WB, United Nations (UN), and the Organization for Economic Cooperation and Development (OECD) are among the most comprehensive studies addressing PPPs from a governance perspective. However, in these studies, while the governance principles required for an effective PPP process are included in detail, the difficulties encountered in implementing these principles are not sufficiently covered. Besides, in the academic literature, while there are many studies on the relationship between infrastructure investments and institutionalism (Knack & Keefer, 1995; Mauro, 1995; Esfahani & Ramirez, 2003; Zergawu et al., 2020), there are a limited number of studies on the relationship between PPPs and governance, which is a more specific form of the subject.

This study aims to discuss the relationship between PPPs and governance within the framework of the neoliberal transformation process. In the discussion, the main instruments of the transformation process and the conceptual dimensions of governance are also considered. In this direction, firstly, the NIE approach, which forms the root of the relationship between PPPs and governance, will be examined. Afterwards, the relationship between the NPM approach, which is fed by NIE, and PPPs will be discussed. In the third section, the relationship between PPPs and governance will be addressed, and then the difficulties of realizing the targeted governance principles in PPP processes will be discussed. In the last section, a discussion on the relationship between PPPs and governance will be carried out based on case studies.

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<sup>3</sup> Transaction Cost Theory aims to protect the parties to almost all transactions other than simple transactions from losses that may occur in relation to exchange transactions through the governance structure. This approach is also expressed as the meeting point of NIE and governance (Şenalp, 2007).

## 2. The Origins of the New Institutional Economics

The NIE approach is one of the primary sources fueling the PPPs that became widespread in the 1990s. The NIE approach, which has its roots in the first half of the 20th century, gained popularity in the 1970s<sup>4</sup>. Before NIE, institutional economics was represented within the framework of the Original Institutional Economics (OIE) approach. NIE has developed on the foundations of OIE. Therefore, it is essential to mention the OIE approach while discussing NIE. Thorstein B. Veblen (1857-1929), John R. Commons (1862-1945), and Wesley C. Mitchell (1874-1948) are the pioneers of the OIE approach, which adopts an economic approach different from both the established economic tradition and the Marxist schools of thought (Sadi, 2008: 731). OIE stands in line against the abstractionist, deductive method, and economic policy propositions of neoclassical economics that seek to minimize state intervention (Senalp, 2007: 49). A vital part of the criticism made by the OIE of neoclassical economics belongs to Veblen. According to Veblen, adopting an evolutionary analysis method in social sciences and economics means examining the formation, development, and impact of non-economic institutions surrounding the economy with "historical" integrity. It is unacceptable to accept socio-political and socio-cultural institutions as "data," to assume that they do not change, and thus to exclude the processes of economic development and mutual interaction of institutions from the analysis. Veblen criticizes neoclassical economics for adopting such an "institution-free" and "history-free" theoretical framework (Şenses, 2017: 86-87).

NIE, which developed on the foundations of OIE and diverged from it, existed not as a developer of the main criticism made by Veblen but as a neoclassical analysis of the relationship between institutions and the economy (Şenses, 2017: 91). Therefore, while saying that NIE developed on the foundations of OIE, it should also be emphasized that it evolved in a different direction. The fundamental point where the new institutionalism differs from the original institutionalism is methodological individualism. NIE accepts the individual as data while making analysis from individuals to institutions (Senalp, 2007: 61). In addition, according to Veblen, the individual, from a Darwinian point of view, necessarily fulfills the requirements of the dominant cultural forces; while according to Commons, individuals can voluntarily create a world of collective rules. NIE reconciles with neoclassical economics by following a Commonsian line that exhibits a voluntarist approach rather than Veblen with structuralist tones (Bayramoğlu, 2018: 117). Commons' world of collective rules based on voluntarism is represented by collective entities such as households and firms. Methodical individualism exists as institutions that represent these collective entities (households and firms) instead of individuals. In addition to methodological individualism, limited rationality, which criticizes the rational individual assumption of neoclassical economics, is another essential title that defines NIE. In NIE, the dominance of the rational individual with full knowledge of the neoclassical approach becomes controversial with the limited rationality approach. The future is uncertain,

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<sup>4</sup> The first seeds of NIE are in Coase's work *The Nature of the Firm*, written in 1937. In this study, Coase discusses the reasons for the existence of firms. In the study, it is asked why firms are needed if the pricing system makes all the necessary arrangements. According to Coase, the main reason why starting a firm is profitable is that there is a cost to using the price mechanism. In addition, a separate contract for each exchange transaction in the market and negotiation costs are other important factors to be considered.

and in conditions of uncertainty, it is wise to use the guidance of the rules on how to act in certain situations; institutions exist to reduce uncertainty (Senalp, 2007: 63). Transaction costs, on the other hand, are another important descriptive heading of NIE, as they nullify the assumptions of a perfectly competitive market. By discussing the rules of the perfect competition market, Coase stated that a market solution is possible in a world where transaction costs are not in question and that this is not realistic, and that the most important tool to avoid transaction costs is firms (Coase, 1960). Douglass North, one of the pioneers of the NIE, explains the institutional importance of transaction costs as follows:

"Institutions are not necessarily or even usually created to be socially efficient; rather, they, or at least the formal rules, are created to serve the interests of those with the bargaining power to devise new rules. In a zero-transaction-cost world, bargaining strength does not affect the efficiency of outcomes, but in a world of positive transaction costs, it does, and given the lumpy indivisibilities that characterize institutions, it shapes the direction of long-run economic change" (North, 1990: 16).

The conceptual foundations of NIE have made significant contributions to the strengthening of the NPM approach. On this basis, it is possible to see the effects of NPM on the PPP process more clearly.

### **3. New Public Management and Public-Private Partnerships**

The ground of enhanced institutionalism targeted in PPPs is based on NIE. The actors involved choose to create an organization, or "institution," rather than relying on individuals bargaining in one or a series of negotiations to create collective activities. This institution will consolidate negotiations and provide the basis for an ongoing exchange within a set of mutually agreed rules. Therefore, PPPs are stable institutional structures governed by a shared understanding of priorities and values as well as a set of mutually agreed-upon by the partners. This stability and institutionalization can be seen as a mechanism to reduce transaction costs and facilitate decisions by creating common perspectives on policy (Peters, 1998: 15).

Besides NIE, another important turning point in the PPPs is NPM. In the process of abandoning Keynesian policies and transitioning to neoliberal policies after the 1970s, the traditional understanding of public administration gave way to the approach of public management. However, as a result of the problems that emerged in the efforts to legitimize the "Public Management Approach" at the theoretical level, the "New Public Management" school emerged (Karcı, 2008). NPM is an organization-oriented approach. The object of investigation is the institutions and organizations within the public administration or sector (Zengin, 2009: 10). According to Hood (1991), one of the theoretical predecessors of NPM, the concept of NPM emerged from the marriage of NIE and managerialism.

According to Klijn (2007), with the transition from the traditional public administration approach to the public management approach, the emphasis on private sector participation, value for money, and output performance is directly reflected in PPPs. It is possible to interpret the fact that countries such as the United Kingdom, New Zealand, and Australia, where the first examples of implementation of NPM are seen, are also the countries with the

first PPP examples as a reflection of the relationship between PPPs and NPM. According to Güzelsarı (2004), the first of the main components of the NPM approach is the shift of emphasis from politics to management. Accordingly, administrators should be cost-conscious in their decisions. The second is the shift from the pyramid model to the horizontal model in the organization of the administrative system. The third is the shift from a process-oriented management approach to a result-oriented management approach. As a result, performance criteria have become important. Fourthly, flexible delivery of services has gained importance. The concept of citizen has started to be defined as customer. Finally, discipline in resource utilization and economic frugality are emphasized. Accordingly, competition has gained importance in the provision of public services. PPPs, on the other hand, are defined by the WB as a long-term contract between the private sector and the public sector to provide a public asset or service, where the private sector assumes significant risk and management responsibility and the return is performance-based (WB, 2017). As a result, it can be seen that there is a direct alignment between the PPP framework summarized by Güzelsarı and the definition of PPPs by the WB. Providing a public service through PPPs is possible with the tools offered by NIE. In order for PPPs to achieve their purpose, the rules and institutions emphasized in the NPM framework are needed.

#### **4. Governance and Public Private Partnerships**

In the process of restructuring the state, the traditional public administration approach has been replaced by the new public management paradigm, and there has been a transition from the new public management paradigm to governance (Güzelsarı, 2004). In the last thirty years, the concept of governance has become an expression that has been brought to the forefront, especially by international organizations, and used instead of the roles and responsibilities of the state. According to Osborne & Gaebler (1992), one of the pioneers of NPM, governance is the process by which we collectively solve our problems and meet the needs of our society. The state is the tool we use, and this tool is outdated, and the process of reinvention has begun. In the WB's report titled "Governance and Development," governance is defined as the use of power in managing economic and social resources for the development of a country. Good governance is central to creating and sustaining an environment that promotes strong and equitable development and is a necessary complement to sound economic policies. In line with the goal of good governance, an efficient public sector, accountability, and a predictable and transparent policy framework are critical for markets and governments' effectiveness and economic development (WB, 1992). The way to implement effective PPPs is through "good governance." In a more detailed definition, governance means "the act, manner, or function of regulating the operations of a firm" or directing, restricting, or controlling the pace and actions, policies, or affairs of a nation, organization, or project. Therefore, good governance in terms of people, actors, and processes is essential to successfully delivering PPPs (Robinson et al., 2010: 10).

In order to implement the basic principles of good governance in PPPs, specific rules and methods gain importance in the process. Prats (2019) categorizes governance in PPPs into three basic levels. First, at the macro level, the responsibilities and roles of the various

organizations involved in each phase of the project cycle should be included, as well as the laws governing PPP design, implementation, monitoring, and dispute resolution procedures. Secondly, at the meso level, elements such as ministries, relevant units, and local governments should perform the functions required in the PPP project cycles. Finally, at the micro level, there should be PPP contracts between a private stakeholder and the government and the contract structure that governs the PPPs (for example, loan, construction, service, financing, or insurance contracts). The distribution of key functions in the process among various organizations is essential to being able to manage conflicts of interest and facilitate transparency and accountability in the process (Prats, 2019: 4). These key functions are listed as follows: promoting PPPs and identifying interested investors, technical preparation and structuring of the project as a PPP, conducting cost-benefit analysis, value-for-money analysis, and contingency risk assessment to justify the implementation of the project through a PPP, drafting the contract, conducting the tender process and submission of the project, supervising and monitoring the project. In addition, the criteria for selecting organizations responsible for performing each function should be applicable to each stage of the process, applied independently, and comply with strict technical standards (Prats, 2019: 24).

This general framework is more comprehensively covered in the guidelines prepared by international organizations. From this point of view, to expand the discussion a little more, first of all, with the general aim of gaining the support of the population in the PPP process, the necessity of coherent policies that set clear objectives and principles, define projects, set realistic targets, and outline the ways to achieve them should be underlined. In order to implement these policies, policies regarding the form of the PPPs, the level of risk to be accepted, how the risk will be managed, unforeseen risks, whether PPPs are a viable method of service delivery, and the participation of partners should be taken into account (UN, 2008). According to the detailed roadmap prepared by the OECD (2012), to create an explicit, predictable, and legitimate institutional framework, the political authority should first raise public awareness of the relative costs, benefits, and risks of PPPs and traditional procurement methods. In addition to the stakeholders in the project, end-users should also be involved in defining the project and monitoring the service quality. Ensure that all major regulations affecting the operation of PPPs are clear, transparent, and enforceable. Bureaucracy should be minimized, and new and existing regulations should be carefully evaluated. Accordingly, the regular and formal participation of all stakeholders is essential to gather as much relevant information as possible throughout all phases of the project and to reduce the information asymmetry between the private and public sectors, as well as between different public institutions (Prats, 2019: 25).

It is functional for the government to build new institutions and train public officials while simultaneously establishing necessary capacities for projects by utilizing external expertise, reducing bureaucratic processes, and increasing knowledge sharing between the private and public sectors. The stages of this process include expertise, institutions, the private sector, a national training program, and multilateral partnerships, respectively (UN, 2008). Special Purpose Vehicles acting as managing and operating companies in the PPP process are legal entities backed by public guarantees. Contracts are made between the government and the

Special Purpose Vehicle for developing, constructing, and operating specific projects (Chowdhury & Chen, 2010). The Special Purpose Vehicle consists of two separate organizational structures and several organizational structures on either side of the negotiating table. Several ministries and agencies working together on a specific project may represent the public sector. On the other hand, the private sector may consist of the parent organization's representation together with several other contracted organizations. When we add financial institutions (banks and financial investors), lawyers who supervise contracts, and various consultants prepared to solve technical problems, a large number of organizations involved in the partnership emerge (Greeve & Hodge, 2010: 154).

The tools preferred to balance and regulate the relationship between the public and private sectors need to be more comprehensive to ensure effectiveness. In the PPP process, interdependencies and the conflicting personal interests of the partners may lead to tensions. Therefore, mechanisms and rules that support a collaborative interaction should be developed, the parties should focus on "process" management as well as "project" and ultimately update and redesign these processes (WB, 2009). PPP investors need predictability and security in legal frameworks. Realization of this principle requires priorities such as protecting the rights of investors to dispose of their property and assets, promoting better quality legislation under the banner of fewer, better, and simpler rules, making enforcement more responsive to the business sector, improving the efficiency of the judiciary in enforcing contracts, and developing the legal framework for PPPs based on comprehensive negotiation in areas that directly affect project initiation and operation, including concession, tax, competition, procurement, and company laws (UN, 2008). Standardizing PPP contracts is an important key to increasing the public's PPP governance capacity. Although this may seem restrictive, it increases the transparency and repeatability of the preparation process and reduces costs (Casady et al., 2017: 18).

Another critical issue regarding the process is effective risk sharing. One of the most important aspects of risk assumption is ensuring that value for money remains positive at every stage of the project process. Encouraging as many projects as possible and implementing them efficiently (prioritizing strategic projects) does not always mean that projects with a positive value for money are carried out. PPP projects should be monitored and evaluated according to their economic and social returns so that potential renegotiations do not affect the value for money proposed at the beginning of the project (Prats, 2019). The OECD has itemized several requirements so that value for money can be maintained at positive values throughout the project period.

According to the OECD, all investment projects should first be given high political priority so that value for money is considered in selecting PPPs. Since there are many competing investment priorities, it is the responsibility of the government to set and pursue strategic objectives. The investment decision should be based on a holistic public perspective and be separate from how the project will be procured and financed. There should be no institutional procedures or accounting bias in favor of or against the PPPs. Secondly, which investment method will maximize value for money should be carefully explored. The main risk factors and characteristics of specific projects should be assessed through pre-testing before procurement. Thirdly, risks should be transferred to those who best manage them.

Fourth, securing value for money requires the same intensity of attention and effort as is required in the pre-operational phase. Fifth, value for money must be preserved during renegotiation. The government should consider compensating the private sector only if circumstances change due to voluntary public policies. Any renegotiation should be done transparently, and PPP approval should be subject to the usual procedures. Precise, predictable, and transparent rules for conflict resolution should be in place. Finally, the government should ensure sufficient competition in the market by structuring a competitive bidding process and the PPPs program as an ongoing functional market on equal terms for each market agent (OECD, 2012).

In the PPP process, the selection among bidders should follow a transparent, impartial, and non-discriminatory selection process that encourages competition and strikes a balance between the need to reduce the time and cost of the bidding process and the need to obtain the best offer (UN, 2008). After the selection stage, the transparent use of the budget process requires some specific rules. First, in line with the government's fiscal policy, the central budget authority should ensure that the project is affordable and that the overall investment envelope is sustainable. Secondly, the project should be treated transparently in the budget process. Budget documents should disclose all costs and contingent liabilities. Care should be taken to ensure that the budget transparency of the PPPs covers the entire public sector. Finally, the government should take measures against waste and corruption by ensuring the integrity of the purchasing process. The necessary procurement skills and authorizations should be provided to the relevant authorities (OECD, 2012).

Although not often found in practice, the need for the PPP process to put people's needs first is also considered one of the basic principles of governance in PPPs. This is possible by increasing accountability and transparency in projects and thereby improving people's livelihoods, especially those who are socially and economically disadvantaged (UN, 2008).

Lastly, for an effective governance process in PPPs, it is often emphasized that the PPP process should integrate sustainable development principles into PPP projects by reflecting environmental considerations in the project's objectives, setting specifications, and awarding projects to bidders who fully meet the green criteria (UN, 2008).

With international organizations underscoring the importance of governance principles for PPPs to achieve their objectives, interest in the subject has started to increase in the academic literature. However, there are more studies on the relationship between infrastructure investments and institutions than on the relationship between PPPs and governance. One of the most frequently cited studies is the empirical analysis of Esfahani & Ramirez (2003), which considers institutional and economic factors in the relationship between the energy and telecom sectors as well as infrastructure types and growth. The study emphasizes the importance of institutional capacity as a factor that strengthens the positive relationship between infrastructure and growth. Gasmi et al. (2009) empirically analyze the effects of political accountability on the performance of telecommunication regulations in developing countries. According to the results, governance in infrastructure industries has a positive effect. It is also concluded that the effect of political accountability on regulatory performance is stronger in developing countries. The study by Zergawu et al.

(2020) is one of the most recent studies on the subject. In the study, the impact of infrastructure and institutional quality on economic growth is empirically analyzed, and it is concluded that both have a positive impact on economic growth. In addition, it is stated that institutional quality should be improved in order to get maximum efficiency from infrastructure.

There are quite a few theoretical and empirical studies on the relationship between PPPs and governance. Among these studies, Demirağ et al. (2004)'s study, which evaluates the effects of accountability and value for money objectives on PPP projects defined as PFI in the UK, from project inception to establishment, implementation, and internal and external monitoring, stands out. The study concludes that managerial and parliamentary forms of accountability are crucial to ensuring the achievement of PFI objectives. Casady et al. (2017) argue that if institutional maturity in public sector governance is accelerated, the use of PPPs in infrastructure delivery will become more widespread. Hammami et al. (2006) empirically examine the relationship between PPPs, corruption, and rule of law. According to their results, when corruption decreases and rule of law is ensured, the number of PPP projects increases. The empirical results obtained by Lee et al. (2018) show that increasing the ratio of PPP investments to GDP increases access to and quality of infrastructure services, and economic growth will potentially be higher. However, this optimism depends on efforts to further develop technical and institutional capacity to handle complex PPP contracts.

Considering the theoretical and empirical studies conducted both by international organizations and in the academic literature, the implementation of governance principles in PPP processes will create an effective result. On the other hand, it is observed that many of the principles discussed under this heading are not taken into consideration in the process. A discussion of these reasons will be made in the next section.

## 5. Governance Challenges in Public-Private Partnerships

PPP governance consists of rules and procedures that define the incentives and constraints that guide the strategies of the various stakeholders involved in the PPP project cycle. Hence, governance in PPPs is expected to encourage PPP projects that create social value and positively affect value for money. According to Prats (2019), avoiding two types of fundamental mistakes is important. The first is to carry out a project that should not be done (Type 1 error). When projects that should never be undertaken are completed, as seen in Table 1, the net present value of the projects becomes negative, and social inefficiencies arise due to white elephant<sup>5</sup> projects. The second is the execution of the projects by choosing the wrong methods (Type 2 error). For example, when projects that should be done through traditional public procurement are carried out through PPPs or vice versa, the value for money becomes negative, which creates financial inefficiency. Likewise, social inefficiency arises in projects with a non-positive cost-benefit ratio.

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<sup>5</sup> White elephant projects refer to investments whose costs are higher than the benefits.

**Table 1: Ineffectiveness in the Decision to Maintain PPPs**

		Has public investment been made?		
		No	Yes, Traditional Public Procurement	Yes, PPP
Public investment should it be done?	No	Appropriate incentives	White elephants (NPV<0) Type 1 Error	White elephants (NPV<0) Type 1 Error
	Yes, TPP	Social inefficiencies (opportunity cost) Type 2 Error	Appropriate incentives	Financial Inefficiency (VFM<0) Type 2 Error
	Yes, PPP	Social inefficiencies (opportunity cost) Type 2 Error	Financial Inefficiency (VFM<0) Type 2 Error	Appropriate incentives

NPV: Net present value, TPP: Traditional public procurement, VFM: Value for money

Source: Prats, 2019

One of the main reasons why wrong methods are preferred in public service delivery is the behavior of the actors in the process, which will protect their personal interests rather than the public interest. Boardman & Vinning (2012) see the conflicting goals and motivations of the public and private sectors as the basis of PPP problems. The government pursues political interest and vote maximization; the private sector, on the other hand, seeks profit maximization. Therefore, the preferred method of service delivery can be determined according to these trends.

There may be situations where the private sector, one of the parties to the PPP process, tries to defeat the public sector and other public partners and fails to fulfill its obligations (Greve & Hodge, 2010). Private companies may underestimate the costs of investments and exaggerate the expected demand for services. For example, a water treatment plant project is more likely to be approved if a municipality is convinced that much more water is needed than it can supply with its current resources, or a toll road is more likely to be approved because of a prediction that the future traffic flow will be much greater than the existing roads can handle (Hall, 2015).

It is frequently emphasized within the framework of good governance in PPPs that citizens should contribute to sustainable development and the protection of the environment by keeping a balance between their current needs and their responsibility towards future generations. However, while deciding on the projects to be implemented by the public sector, it is seen that projects are not carried out of necessity; on the contrary, projects that are not needed are implemented primarily due to political concerns (Cangöz et al., 2021). For example, the fact that the responsibility of a PPP project that aims to protect the environment and sustainability usually belongs to the ministries of finance and transportation rather than the ministries of the environment has a significant impact on the deviation of the project process from the target (UN, 2008).

In addition to these primary challenges regarding the governance process in PPPs, one of the most frequently discussed challenges is complex contracts. Due to these contracts, involving the public in the discussion is impossible. In practice, it is also not seen that the public or other

partners are included in the discussion processes of the contracts. According to the UN's 2008 report, it is noteworthy that the public is generally consulted insufficiently in the PPP process, and the interests and needs of the citizens are not addressed.

Lack of transparency and accountability is another crucial governance issue to face. One of the fundamental reasons that undermine transparency and accountability and limit our adequate access to information on many PPP projects is the inclusion of most arrangements in contracts as trade secrets. For example, in the Eurasia Tunnel Project Report in Turkey (2022), it is stated that sharing all technical data of companies competing in tenders is against the principle of competitive competition, and it is supported by the opinion of the European Union Commission that projects can be shared with the public by hiding some information in these projects. This issue, which is one of the most important reasons why we do not have enough information about PPPs, has been put on the agenda of the UK Parliament. The Parliament underlined the need to broaden the freedom of information, stating that transparency regarding the benefits and costs of PPPs has been overshadowed by the relevant Ministries and investors who rely on trade secret justification (House of Commons Public Accounts Committee, 2011).

Incomplete drafting of contracts and, consequently, frequent amendments to contracts are also one of the critical problems that arise in PPP contracts that are drafted without considering the principles of transparency and accountability. This process leads to delays or interruptions in projects and a sharp departure from the value for money approach, which is one of the essential governance principles.

Another problem caused by the complex contracts in PPPs is that legal decisions can be manipulated to fit predetermined parameters using unreliable information. This, on the other hand, creates consequences that do not account for social problems, protect the interests of certain groups, and lead to corruption (WB, 2009).

The maintenance of PPPs through long-term contracts also creates governance problems. Due to long-term contracts, it becomes difficult to evaluate the output and results of PPPs, and it may become impossible to predict the factors that may affect the governance environment in the process (Greve & Hodge, 2010). Difficulties experienced in this regard may lead to conflict and/or additional costs between the parties to the contract.

In order to realise the governance in PPPs, as mentioned before, the principle that "the risk is undertaken by the party that can manage it best" should be applied in the emergence and control of risks throughout the entire process, from the preparation stage to the implementation of PPPs (Cangöz et al., 2021). However, while the risk should be assumed by the party that can best manage it, it is seen that in many PPP projects, the projects often fail because the parties cannot agree on the risk allocation and both parties try to shift the risk to the other (UN, 2008).

As a result, the main reason behind the governance challenges in PPPs is the level of institutional development that determines the relationship between PPPs and governance. Governance is an indicator and tool of institutional development. Therefore, first of all, an analysis should be made about whether the service will provide public benefit with the traditional public procurement method or the PPP method. If the PPP method is preferred in



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the next stage, it will be possible to overcome the governance challenges mentioned in this section by conducting a process that focuses on governance principles.

## 5. Discussion of Public-Private Partnerships and Governance through Case Studies

In PPP projects, it is possible to give examples of PPPs showing that, under the condition that the principles of governance are implemented, results that are suitable for their purpose can be achieved. One such example is Canada, a developed country with strong governance. The Vancouver Landfill Project in Canada is a PPP project that has achieved sustainable development and environmental goals. The municipality, which went out to tender in 2001, received five bids, each of which approached the use of landfill gas differently, and one of the bids evaluated by the City Council was selected. The importance of this project lies in its contribution to the reduction of greenhouse gases. The city of Vancouver, as a public partner, owns and operates the landfill located on public land. The Canadian energy company is responsible for designing, financing, constructing, and operating the cogeneration plant. BC Hydro, a British Columbia company under the Ministry of Energy and Mines, buys and distributes the electricity produced by the cogeneration plant. The other partner in the private sector is an agricultural enterprise that purchases heated water produced by the electricity generation process and uses it to heat the greenhouse complex. The public sector does not pay the private partner but guarantees the supply of landfill gases for the 20-year contract period. The revenue from energy and thermal sales goes to the private sector, and 10% of the royalties are paid to the municipality. The operating cost for the municipality to supply landfill gases is approximately \$250,000 per year, and the royalty paid to the municipality is \$400,000. Therefore, besides providing an environmental benefit, the project also serves the public interest in financial terms (UN, 2008).

Another example that has achieved its goal is Colombia, which, unlike Canada, is far behind in the governance world ranking and is in the category of developing countries. The TransMilenio (TM) rapid transit bus system project plans to activate bus routes by constructing special bus lines in critical areas of Bogota and using a side route system to complete the main lines. A public company, TransMilenio SA, was established to manage the project. The company has undertaken the planning and contract preparation stages, as well as the tender to select the private partners who will build the infrastructure and operate the main roads, bypass, ticketing system, and payment system. TransMilenio SA has also assumed the role of an observer in order to provide customer service and quality performance. In this context, it applies a penalty system for private sector partners who do not comply with their contractual obligations, responsibilities, and investment requirements. The public sector, which is responsible for financing the investment in infrastructure, retains the financial risk of the project by entering into a contract with selected private contractors on a competitive basis. The bus companies operating the bus routes are selected through competitive bidding. The factors that make the company a reason for preference are based on a point system that bidders receive according to their experience, bus quality, and emission levels. Thus, TM encouraged bus operators to provide an efficient, modern, and non-polluting vehicle fleet. For these reasons, bus operators had to invest in new buses, so

the financial risk was transferred to them. The payment system implemented in the TM project means that the demand risk is assumed jointly by the bus operators since all the collected revenues are distributed among the bus operators. Shortly after the implementation of the TM project, significant improvements were made in terms of the efficiency, safety, and environmental impact of the system (WB, 2009).

In the case studies, it is seen that when governance principles such as strong risk management, sustainable development, and environmental objectives are taken into consideration, PPPs that provide public benefits and achieve their objectives can be achieved. On the other hand, the positive PPP experience in Colombia is contrary to what might be expected, as it is a weak country in terms of governance.

In countries with strong governance, it is also possible to come across PPPs that have deviated from their purpose. The London Underground project in the United Kingdom is one of the projects that is frequently discussed in public opinion. Problems such as high-cost consulting services, uncertainties in contract negotiations, and delays in the finalization of the tender started to emerge at the very beginning of the project. The shortcomings of the PPP contract also created uncertainty as to who would bear the resulting cost overruns. This uncertainty subsequently led to complex contracts in which project partners determined their responsibility for cost overruns and their impact on project financing. Metronet, a private sector partner in the project, requested £992 million from LUL (London Underground Ltd.), a public sector company, for other committed expenditure, including past expenditure, but was only given £121 million to cover expenditure over the year ahead. This process resulted in the bankruptcy of Metronet, which placed a significant financial burden on the public sector as lenders were guaranteed 95 percent of the £2 million debt (WB, 2009).

The corruption scandal involving the Odebrecht company, which is the executor of many PPP projects in Latin American countries that lag behind developed countries in terms of governance, is an important example of the relationship between PPPs and governance. It was revealed that Odebrecht had distributed bribes of about 3 percent of the tender value to politicians in power in order to obtain billions of dollars in public tenders for Petrobras in Brazil. In Peru, where the highest bribes were found to have been distributed after Brazil, it was revealed that Odebrecht distributed a total of 29 million dollars in bribes to politicians in order to obtain tenders for projects such as metro, motorway, and pipeline construction, and after this scandal, all major public construction projects in the country were stopped (Erol, 2018). Due to the Odebrecht bribery scandal, 12 countries in Latin America and Africa postponed many infrastructure projects (Bajpai & Myers, 2020). According to WB records, between 1995 and 2016, Odebrecht was a partner in 51 PPP projects in the sectors of electricity, airports, ports, railways, roads, operational water, and treatment plants, including 6 in Peru, 2 in Mexico, 1 in Colombia, and the rest in Brazil (Private Participation in Infrastructure (PPI-WB). Luis Alberto Moreno, former president of the Inter-American Development Bank, told reporters that "there is no doubt that the Odebrecht case has caused enormous damage to the company and many governments, but the biggest damage caused by this scandal is the idea that public-private partnerships are bad" (Reuters, 2017).



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It is not possible to draw a general conclusion on the relationship between PPPs and governance based on positive and negative case studies of countries with different governance levels. For example, favorable PPP processes can be found in Colombia, a country with weak governance. On the other hand, as seen in the Odebrecht scandal in this country, the PPP process can also be damaged due to corruption.

The governance challenges in PPPs discussed in the previous section provide various reasons for the failure of PPP processes within a governance framework. However, it is insufficient to explain why PPP problems are experienced in countries with strong governance or how effective PPP projects can be realized in countries with weak governance. The answers to these questions can be sought under three headings. The first one is the debate on the measurement of governance. Accordingly, institutional variables are often indicated by indexes created by consulting firms and research institutes as a result of surveys conducted among professionals and business people. According to Chang (2011, 2015), these indexes exclude institutions that are incompatible with liberalization, such as the welfare state. The package of "right institutions" includes mostly democracy, a clean and transparent bureaucracy and legislature, strong protection of property rights, including intellectual property rights, corporate governance institutions, especially rules on information disclosure and bankruptcy law, and advanced financial institutions. It is rarer that a good public finance system, social welfare, and labor institutions that provide a safety net and protect workers' rights are included in the package, although they are important. According to Aron (2000), who provides an extensive discussion of the reliability of institutional indicators, the evidence for a link between the quality of institutions and investment and growth is by no means robust. On the other hand, the scarcity and weakness of both macroeconomic and institutional data for many developing countries preclude sound policy interpretations on a country-by-country basis. The second argument is that governance indicators are not linear across countries. Accordingly, mainstream institutional theories view the relationship between institutions and economic development as linear and uniform across time and space and do not recognize that this relationship varies across and within societies over time (Chang, 2011). On the other hand, international financial institutions may be too demanding towards developing countries with regard to the obligations of developed countries regarding institutions, finance, and human resources (Chang, 2015). According to Chang (2015), the development of institutions takes decades, if not generations. In this context, demanding "world-class" institutions from developing countries in as little as 5 to 10 years and penalizing them when these demands are not met contradicts the historical experience of the developed countries themselves. Finally, from the perspective of the approach that considers PPPs as a model developed in line with the interests of the private sector, the loss of the importance of governance principles will also be an expected result. According to Fine (2020), the starting point of the debate is the globalization, neoliberalization, and financialization of economic and social reproduction. PPPs, which emerged as a result of the neoliberal transformation stages, can be understood as a mixture of public and private, market and state. However, PPPs can be better analyzed analytically within the framework of commodification. According to Bayliss & Waeyenberge (2018), PPP policy is now driven more by the availability of global finance than by the previously perceived potential for efficiency gains through privatization. This has led to the institutional restructuring of

infrastructure to facilitate the entry of financial investors and is underpinned by a policy framework that strongly favors private sector participation over alternatives based on public sector procurement. Studies that examine PPPs on the basis of private sector needs and financialization also emphasize the transformation of infrastructure into assets that generate income streams for private actors and the creation of an infrastructure asset class (Romero 6 Waeyenverge, 2020; Arezki et al., 2017).

## 6. Conclusion

PPPs are encouraged for reasons such as diversifying financing resources, reducing public debt, reducing service costs, saving investments and services, realizing a balanced risk distribution between the public and private sectors, maintaining a budget balance, and developing alternative management strategies based on the financing needs of the public sector (Guzelsari, 2009). However, the fact that many PPP projects have been postponed, cancelled, or incurred significant public losses has recently made PPPs increasingly controversial. In this environment, under the leadership of international organizations, the concept of "governance" is frequently emphasized as a tool that can solve the problems of PPPs.

The elements emphasized in the guides prepared by international organizations on how and within which framework governance can be implemented in PPPs are an answer to the problems experienced in PPP processes. It is known that realizing the projects that need to be realized with the traditional procurement method in public service provision with PPPs or the projects that should be realized with PPPs with the traditional procurement method causes significant public losses. For this reason, the first step to effective governance in PPPs is to make a cost-benefit analysis about which method will provide public benefit in service delivery.

A large part of the problems that arise during the process are due to the complexity of the contracts or incomplete or frequently changing contracts. These contractual problems can lead to wrong decisions by laying the groundwork for manipulation both at the beginning and later in the process. On the other hand, contracts not shared with the public on the grounds of trade secrets cause severe damage to transparency and accountability. Accountability and transparency in line with the principles of governance in PPPs regarding this issue should be considered throughout the process. In order to achieve this, it is vital to make the contracts clear, understandable, and standardized.

PPPs are long-term and high-cost projects, creating a large rent area. Therefore, tender processes must be carried out impartially and transparently. The care to be taken in this regard will also help prevent possible corruption.

The endeavor of the public and private sectors to attribute the risks that may arise to the other party also eliminates the validity of governance principles. In the definition given by WB (2017), PPPs are defined as projects in which the private sector assumes the financial and operational risk. However, in recent years, Treasury guarantees given in most of the PPP projects invalidate the risk sharing in the definition of PPPs, causing a large part of the risk to

be transferred to the public sector. The proposed solution offered in this regard is to perform a value-for-money analysis at the beginning of the PPP processes and to show the utmost care to ensure that value-for-money remains positive throughout the process.

The governance challenges that cause PPPs to deviate from their goals and the basis of the governance principles offered as a solution to these difficulties are based on the strong institutional structure and rules shaped within the framework of NIE and NPM. When the governance process is applied effectively on this basis, it is possible to reduce or eliminate many problems experienced in PPPs. More concretely, public service provision can be achieved by choosing the proper procurement method, ensuring accountability and transparency, and maintaining a positive value for money.

The other side of the possible favorable scenario for PPPs is the problems encountered in practice. The fact that these projects are megaprojects provides a large amount of profit to the companies that are awarded the tender. For the government, they are very advantageous because they can be left out of the budget. Thus, even though public investments are made, there is no increase in public expenditures in the short term. In addition, it is an issue that is frequently discussed in public opinion that PPP tenders are awarded to specific companies close to the government in many countries. When favorable or unfavorable PPP case studies are analyzed, uncertainty emerges as to whether PPP processes are directly related to the governance level of countries. There may be many reasons for this. However, in this study, the discussion is limited to only three topics. The first one is the debate on the measurement of governance. The second is the criticism that governance indicators are not linear for each country. The last one is, in a more general sense, the idea that PPPs are a method shaped according to the interests of the private sector. When this idea is at the center, it is inevitable that the relationship between PPPs and governance is weakened. It is possible to discuss the rents provided to the companies that receive the tender and are often close to the government and the bureaucracy's orientation towards PPP projects without considering the public interest within the framework of the last issue.

This study has examined the governance solution offered for the problems experienced in the PPP processes, together with the dimensions of the concept based on NIE and NPM. On the other hand, the relationship between PPPs and governance requires a more comprehensive discussion that goes beyond the limits of this study. The governance solution offered by the neoclassical economics approach of NIE and NPM is insufficient to eliminate the problems encountered in practice. In the neoliberal world, which centers on capital's need for accumulation, the governance principles defined for PPPs need to be examined in a much more dimensional and in-depth manner. In other words, when the public interest conflicts with the needs of capital accumulation, the question of which one will be preferred remains to be discussed.

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