Public-Private Partnerships (PPPs): A Cure for Government Failures?

By, Dr. Yin Wang
Ph.D: Policy, Planning, & Development
University of Southern California

Abstract:
Based on reviewing Krueger's "Government Failures in Development", this paper argues that Public-Private Partnerships (PPPs) can be a good cure for government failures by easing the pains from government failures and keeping the advantages of government intervention. After discussing three major causes of government failures, this paper will elaborate why partnership can relieve the government of the risks of these causes. Nevertheless, it should be noted that partnership can't effectively solve the problem of the self-interest of public employees, and that it actually raises another concern about the accountability of private actors.

Due to the breakdown of the markets and the emergence of market failures in many developing countries in the 1970s and 1980s, development economists believed that there was a strong case for government to intervene in the markets to compensate for the market failures (Krueger 1990). However, experience with development over the decades has showed that government intervention has not worked out as economists expected. The rising of all kinds of government failures has led to considerable skepticism about the effectiveness of government intervention.

According to Krueger's understanding, there are two types of government failures: commission failures and omission failures. The former, activity at government's "comparative disadvantage", include state-owned retail shops for the distribution of essential products, state-operated mines and manufacturing activities, state enterprises with monopoly rights for importing commodities, and etc. The latter, no activity at government's "comparative advantage", are relatively more visible: deterioration of transport and communication facilities, failure to maintain existing infrastructure facilities, and insistence upon nominal rates of interest well below the rate of inflation with credit rationing (Krueger 1990).

Causes of Government Failures

Through government intervention, government takes a leading role in the allocation of investment, controls the "command heights" of the economy and produces certain goods and services at its "comparative advantage". However, some of the governmental products and services have long been questioned due to unprofessional performance, low efficiency and high costs. Krueger believes there are three main reasons why government intervention has not been as effective as expected, and instead, caused government failures:

- Administrative difficulties are prohibitive. The governments of many developing countries find themselves unable to perform their duty well because of public administrative difficulties, such as lack of trained personnel, a shortage of capital and out-of-date technology, which have resulted in severe government failures.

- Decision makers might not be professionally suited for the job. Most of the policies are made by neither economists nor technocrats, but politicians, who might not be professionally suited to make the best decisions. Moreover, politicians, with the concern regarding their political careers, will have to seek political support and take political pressures. Their decisions could be highly affected by various interest groups and political authorities. Therefore it won't be surprising that many of the public policies are the product of compromise between politics and effectiveness.

- Public servants are self-interested. There is no doubt that some of the public employees are inspired by altruism, but it should be recognized that most individuals working in government are as self-interested as those in the private sector. Public employees' self-interest might be concentrated on political survival, on promotion or on other rewards. They might try to maximize their personal gains or to increase the interests of the group they belong to by compromising the public interest. In extreme situations, public employees might involve in illegal conduct, such as rent-seeking and bribery, to pursue self-interest.

The Promises from Public-Private Partnerships

Public-Private Partnerships (PPPs) can be a good cure for government failures. PPPs can effectively ease the pains from government failures by providing quality public products/services at low costs, on one hand, and won't affect the strengths of government intervention by keeping government's leading position in the allocation of investment and maintaining its controls over the "command heights" of the economy, on the other hand.

A Public-Private Partnership is defined as a cooperative venture between the public and private sectors, built on the expertise of each partner that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards (Canadian Council for Public-Private Partnerships 1998). It is noteworthy that the essence of PPPs is the creative combination of private and public resources toward mutually desired ends by using agreed upon tools, strategies and resources in a concerted, coordinated fashion.

As a matter of fact, PPPs can well alleviate the pains from government failures by: 1) providing quality public services at low costs; 2) accessing private resources to compensate for public administrative difficulties; 3) helping politicians with expertise, technology and sensitive political issues. The following will discuss five major purported advantages of PPPs in detail.

1. Quality improvement

Empirical qualitative research shows that in PPPs, both the public and private have better incentives to perform. To the public sector, partnership is a useful vehicle for increasing their familiarity and direct interaction with private actors. Therefore public agencies are able to adopt more advanced managerial skills and expertise from their private partners. Also, partnership offers a good opportunity for government to closely communicate with clients – citizens or other particular service receivers – so as to better understand, determine and meet their needs (Allen 1999).

To private actors, PPPs also provide strong incentives for better performance. Risk sharing is the greatest incentive for good private performance. In many partnerships, payment is conditional upon the initiation of the actual provision of public services, or the quality of the services delivered. Plus, a private actor usually has access to a range of performance-based payment arrangements, which are rarely available in the public sector. Another reason why private involvement can increase efficiency is private actors are usually free from bureaucratic "red tape" and relatively isolated from political intervention, so that they are able to work more flexibly and effectively than a public agency (Allen 1999).

2. Cost reduction

One of the crucial benefits of using PPPs is to save costs. Cost savings can be achieved mainly through increase in efficiency and reduction in staffing and employment conditions (Skelcher 2005). Cost savings are also the result of improved management due to lack of red tape, increase in flexibility, and speedy implementation (Seader 2002). Support comes from David Seader Associates' research (2002), reporting that the U.S. experience with public service outsourcing results in 10%-20% savings over the traditional public delivery system and in some cases savings as high as 40% have been achieved. Domberger and Jensen's research (1997) on the UK and Australia supportively demonstrates that contracting-out in these two countries has resulted in mean savings of about 20%.

3. Access to private resources

PPPs provide government the access to private resources, including **specialized expertise, proprietary technology** and **private capital**, to overcome public administrative difficulties. Government should be aware that the private sector has some advantages that cannot be found in the public sector. The private sector owns know-how and advanced technology, and private laboratories accelerate change to an amazing rate, especially in high-tech fields like information and communication areas. In contrast, as a generalist, government can not afford to maintain know-how in-house, and it is more impossible for government to conduct research and development in every field. Partnership provides a great opportunity for government to access **specialized expertise** and **advanced technology** from the private so as to better serve the public interest (Seader 2002). Also, partnership serves as a vehicle for the injection of **private capital** in public service delivery. It may permit projects to proceed when there are no enough public finances available. Or with private capital coming in, government can devote its scarce resources to other high-priority areas of expenditure (Allen 1999).

4. Helping politicians in several aspects

Besides the professional help of the expertise and technology from the private sector, as mentioned above, politicians will also benefit from PPPs when partnership helps them address sensitive political and labor issues. When the political leadership can not directly take on a project because of its sensitivity, PPPs can be a great way to still accomplish politicians' objectives without having risks of stirring up serious controversy. The sensitive issue list consists of such issues as downsizing, regionalization, implementation of difficult policies, operation with cross border relationships, and coordination of political entities. Because of the flexibility and efficiency of the private sector, politicians sometimes can rely on their private partners to handle those issues more easily and less controversially (Seader 2002).

5. Risk sharing

The sharing of risks between the public and private can effectively prevent the happening of many government failures. Scholars firmly believe that partnership can efficiently distribute particular risk to the partner best suited to manage that risk, and therefore the overall probability of failure can be minimized (Allen 1999, Seader 2002, Skelcher 2005). Also, as we mentioned above, partnership offers the opportunity for the public sector to access private technology, and then a private partner will have to guarantee the effectiveness and efficiency of the technology it brings in. This will relieve the public sector of the risks of enormous costs associated with research, innovation, and performance. Furthermore, after signing the contract of a partnership, the private sector is obligated to perform with fixed or maximum costs for the operation of the project. This apparently relieves government of its open-ended financial risks in this particular public service area. In addition, in some cases where private actors are contracted to market on their own, the public sector is even free from market risks or rate/pricing risks (Seader 2002).

Accountability Concerns

Even though PPPs can effectively alleviate negative effects of government failures by providing quality services at low costs, accessing private resources and helping politicians in several aspects, the concern of self-interested public employees can't be entirely solved by undertaking PPPs. In fact, besides public accountability, PPPs actually raises another concern about private accountability.

1. The accountability of the public sector

Self-interest of public employees will still be a major concern in PPPs. Some scholars are worried that involvement of the private sector in public service delivery will worsen public accountability of public employees by providing them a "great" opportunity to seek rents from private actors who want to win a partnership contract.

To respond to this concern, optimistic proponents of PPPs argue that partnership can effectively improve the public accountability by imposing public scrutiny and increasing transparency in partnership. As partnership brings in multiple players in public service delivery, including private firms, community groups and other civil societies, it is in fact imposing more public scrutiny on governmental work and increasing the transparency in project operation. Therefore public employees have more pressures and incentives to work responsibly and accountably. Proponents of PPPs conclude that partnership can effectively prevent public employee's self-interested behavior and deter illegal conduct.

2. The accountability of the private sector

Involvement of the private sector in public service/facility delivery raises the concern of private accountability, which has long been the most controversial issue in PPPs. Not only skeptical scholars but also some citizens are worried that the private actors might be less accountable than government to provide public services. Unlike public agencies, having the goal of best serving the public interest, the private sector, especially for-profit organizations, aims at maximizing its financial benefits. Critics argue that private actors might have strong incentives to take short cuts in providing public services to achieve cost savings and financial benefits. It could get worse when private actors conduct illegal practices to win over government for a partnership contract by bribery, black-box operations and other corruptions.

To rebut the criticism, both public administrators and private managers argue that private actors involved in PPPs actually have a high level of public accountability due to outside public scrutiny and inside profit incentives. Outside public scrutiny involves multiple players: private companies have to answer to the public agencies that hired them, and also to various regulators, such as the Securities and Exchange Commission and congressional oversight committees. Actually, regulators tend to enforce regulations more tightly with private actors than they do with public agencies, because ordering public agencies to comply with regulations can mean increased budget and higher taxes (NCPPPS 2006). In some well-known and visible partnerships, the media plays a significant role in scrutinizing the private sector's performance.

Also, private partners have strong profit incentives to be accountable in partnership. The only way a company can achieve long-term success in business is to provide quality, value and dependability. Private partners have to establish a reputation of quality services and honest operations to win long-term contracts with government (NCPPPS 2006). If a private company reduces service quality or conducts illegal practices for short-term profits, it will actually lose in the long run.

In a conclusion, PPPs can be a great cure for government failures in that the alternative of public service delivery has the advantages on improving efficiency, saving costs, accessing private resources and helping politicians with several issues. However, the concerns regarding the public accountability and private accountability in partnership remain unanswered and deserve close attention and thorough study in the future.

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