



Te Ope Whakāora

# Public Private Partnerships

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## Alan Johnson asks whether PPPs are the new silver bullet for affordable housing?

The future of social housing in New Zealand may well lie in Bonnyrigg, a low-income community some 30 kms west of Sydney’s CBD. Bonnyrigg was, from all accounts, a fairly run down and unattractive public housing estate of around 800 houses, which was owned and run by the New South Wales State Government. Recently, it has become famous—at least in housing policy circles—because it is being touted as the way forward for public private partnerships in the provision of affordable housing.

Public private partnerships (or PPPs) are, as the name suggests, a partnership between a public agency such as the government or local council and private business. The broad purpose of such a partnership is the supply of public services, such as health care, education, roads and—in Bonnyrigg’s case—affordable housing. While there is no one model of PPP, they normally involve the private sector providing capital to build a facility, such as a hospital or school, which the government or council agrees to either fund the operation of, or pay rent for its use, for an extended period of 25 or more years. The investors get a more or less guaranteed return on their investment, and the government gets a facility or service without having to spend money up-front.

New Zealand’s first major PPP—the construction and operation of a 1000 bed prison in Wiri—was announced in November 2010, by the Finance Minister Bill English and Corrections Minister Judith Collins. At this time Mr English stated that ‘International experience suggests that using an appropriately structured PPP for the new prison will offer savings over conventional procurement methods. In addition, it is expected that this PPP will enhance public safety and improve rehabilitation outcomes’.<sup>1</sup> In other words, PPPs and the private investors and operators they bring, are expected not only to bring about savings but to provide better social outcomes than the tired old public sector can.



Critics, and indeed some advocates,<sup>2</sup> of PPPs argue that this is a form of privatization; while PPP advocates, who are normally banks or service providers, argue that PPPs are simply an alternative method of procurement. As a term, PPP is vague, and perhaps deliberately so. One reviewer of PPPs has suggested that this vagueness ‘may be part of a general trend with public management of needing to renew the reform buzzwords from time to time, or the practise of advancing the same policy, but under a different and more catchy name.’<sup>3</sup>

In 2007, the New South Wales State Government entered a PPP for the redevelopment of Bonnyrigg. This project, which is expected to take 12 years to complete, will entail the construction of 2332 houses; 30% of these will remain as public housing units and 70% will be privately owned.<sup>4</sup> The PPP involves Westpac Bank as the financier and equity partner; Becton as the developer and builder; and Spotless (better known in New Zealand as a catering company) as the facilities manager responsible for the day-to-day operation and maintenance of the completed housing estate. As a sub-sub-contractor to the project, the St George Community Housing is the tenancies services contractor, which is responsible for all aspects of managing the tenants in the social housing units of the new Bonnyrigg.<sup>5</sup>

→ This paper does not necessarily represent the official views of The Salvation Army.

The first stage of Bonnyrigg has been finished with 95 dwellings completed, 56 of which have been sold to owner-occupiers or rental property investors in the price range of SA290,000 to SA470,000. The remaining 39 units are social housing units, which are re-housing the existing public housing tenants in Bonnyrigg.

In New Zealand, one of the main promoters of PPPs, the New Zealand Council for Infrastructure Development, is already offering Bonnyrigg as the way forward for social and affordable housing, having focused on the project at a conference in Wellington in April.<sup>6</sup>

This organisation is also leading a fact-finding delegation to Australia in May, which will include banking and construction interests, as well as Government and community housing representatives.

It may seem ironic that the private sector is being offered as the solution to our affordable housing problems in an era where Government is having to bale out investors in bankrupt finance companies, and is providing capital backing to New Zealand's only insurance company so that it can remain viable. For tens of thousands of homeowners trying to deal with leaky and rotting homes because of the poor design and construction standards of the building sector, the representation of this sector as the answer to our current housing shortage might seem incongruous. The profits have been made and taken, and the mess has been left for the taxpayers and ratepayers to clean up—so why trust private business again?

One of the key questions for deciding the value or otherwise of PPPs, is that of risk. While there is no universal PPP model, the complex contracts and organisational structures behind them are principally about who bears what risk, and how they are rewarded for this risk-taking. Promoters of PPP argue that those in the private sector are better at taking risks than public sector bureaucrats, because they run the risk of bankruptcy and unemployment if they get it wrong. As a consequence, the private sector has a greater imperative to get it right, and it is merely only a question of how contracts are written and the incentives offered for the private sector to willingly, and ably, provide public facilities and services.

The main incentive for the private sector and private investors to build public facilities like hospitals and schools, and to provide public services like running prisons or administering welfare benefits is, of course, money. There is nothing wrong with such a motivation, given that it already costs taxpayers billions of dollars each year to provide these facilities and to run these services. One of the key questions here is whether or not PPPs offer better value for money than more traditional models of provision, which rely on public ownership of facilities and the direct employment of public servants to run them. According to the Minister of Finance, in the case of prisons

this value case is proven, although to be fair to him and his colleagues, their support for PPPs is by no means universal or unequivocal.<sup>7</sup>

While it may seem a relatively simple question, the issue of better value overall, and better value for money in particular, is by no means an easy one to decide—either in favour of PPPs or against them. Complexity arises for at least three reasons:

Firstly, there is the question of timeframes. Because PPPs most often involve the private sector financing a facility or infrastructure asset, the investors expect very long-term contracts of 25-30 years in order to recover the value of their investment. This long-term emphasis leads to a focus on an asset's so-called 'whole of life costs', rather than just, for example, the capital costs of building it or the costs of operating year-to-year. 'Whole of life costs' include the cost of ongoing maintenance, refurbishment, renewal and perhaps of upgrading to meet new standards and technologies. The problem is that a lot can happen in 25-30 years—new ideas emerge, priorities shift and even the way we count costs and benefits can change. How do we develop contracts for such contingencies and who bears the risk of the uncertainty of these contingencies? New Zealand's experience of the privatization of our rail and telecommunications networks, which have subsequently required huge taxpayer subsidies, would suggest that the private sector does not bear these risks.

The second complexity arises around delivering social benefits. In the case of Bonnyrigg, the social responsibility of the New South Wales State Government to adequately house people has quite literally been contracted out to Spotless and St George Community Housing. Spotless has a profit to make and St George cannot afford to make a loss, but while both organisations have an incentive to avoid unnecessary costs, where is the incentive to get the right social outcomes? Contracts will only go so far in describing and defining the right social outcomes, especially for vulnerable people and communities. In part, this is because social need is often multi-faceted and interdependent. Where, for example, do the health



needs of a person start and their housing needs end, and who will be responsible for delivering on each of these if everything is tightly defined by commercial contracts and no one has any responsibility for the overall outcome? Of course, the best way to make a profit from such complex contracts is to avoid working with the wrong people—those with high and complex needs who will just cause you problems. In other words, subtly exclude the most vulnerable and make sure that ‘nice’ people who are grateful and easily-managed get into the housing that you manage.

The final complication is around political change. Long-term contracts may lock in the prevailing social values and political priorities of an era, and it becomes difficult to effect social and political change without the Government having to buy its way out of contracts. The prospect of such costs may limit the extent and direction of social change, and as a society we become captured by the past.

The status quo is unfortunate for those who are opposed to the idea of PPPs for philosophical or pragmatic reasons. Many public agencies that currently work under the traditional models of provision are hardly exemplary. For example, the public prison system has proved unable to address high levels of re-offending by discharged inmates, and our public housing estates have become places that no one wants to live in, or next to. The need for change is clearly apparent, although the need for solutions based on private investment and a profit focus remains questionable.

At the end of the day, the government and the state are not businesses, although they should certainly be run in a businesslike way. While the state clearly has a role in upholding property rights so that private investment is viable, it does not have an obligation to provide opportunities for private investors to make easy and safe returns from investment in publicly-subsidised assets like prisons, hospitals, schools and social housing. The state is there for all its citizens: rich and poor, vulnerable and powerful, and the role of government is to ensure that our various social, political and legal freedoms are maximised and not shackled by long-term commercial contracts that limit the public control and scrutiny of our public services.

- 1 See Bill English's press release [Prison PPP gets green light](#) from 3<sup>rd</sup> November 2010
- 2 Emanuel Savas (2005) *Privatization in the City—Successes, Failures, Lessons* provides a very useful description of public private partnerships and of the value in the vague use of the term as a way of avoiding political debates around privatization ‘The term “public private partnership” is particularly malleable as a form of privatization. It is broadly defined as an arrangement in which a Government and a private entity, for profit or nonprofit, jointly perform or undertake a traditional public activity. It is defined narrowly as a complex relationship – often involving at least one government unit and a consortium of private firms created to build large, capital intensive, long-lived public infrastructure, such as a highway, airport, public building, or water system or to undertake a major civic redevelopment project. Private capital and management of design, construction, and long-term operation of the infrastructure are characteristics of such projects, along with eventual public ownership. Despite the term’s ambiguity “public private partnership” can be politically useful because it avoids the inflammatory effect of “privatization” on those ideologically opposed.’ Pp.15-16
- 3 Hodge, G.A. and Carsten, G. (2009) *PPPs: The passage of time permits a sober reflection*. Journal of Institute of Economic Affairs, p.34
- 4 See details of the [Bonnyrigg project](#)
- 5 See the summary of the various [contract arrangements](#) at the NSW
- 6 See [PPP Principles and Practice](#)
- 7 For example in his speech to the NZ Council for Infrastructure Development in August 2010 Bill English said that the ‘Government will enter into PPPs only if they work and deliver value for taxpayers’ and he also indicated that it was unlikely that PPP would be of the same scale and the programme of the same extent as in Australia.