



# Long-term performance monitoring in public private partnerships

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**P**ublic private partnerships (PPPs) are a sophisticated form of complex international contracts where the focus is the payment for delivery of services rendered satisfactorily and the transfer of the performance and project-related risks from the government to the contractor. They fall under the concept of privately financed infrastructure projects and have only appeared recently. Such type of project is characterised by a further shift of risk to the contractor as compared to the traditional build-operate-transfer (BOT) projects and the inevitable need to increase private participation in the construction of infrastructure.

An essential element of the successful performance of a PPP is professional contract and risk management, in particular, through the long-term performance monitoring of a PPP project.

## **Role and function**

The term 'long-term performance monitoring' is commonly used for the contract management carried out by the government during the operation phase of a PPP; that is, the so-called public sector risk management. Effective performance monitoring requires a well drafted contract that includes effective means for simultaneous conflict prevention and resolution, such as dispute boards, and an adequate quality management system.

Performance monitoring is necessary in order to determine whether the service has been rendered 'satisfactorily' under the contract; that is, whether (a) the service is available and (b) the quality of the performance meets the established requirements under the contract.

As a general rule, the government is liable to pay for a service, if it is available, which is typical for the provision of a building-based service such as a hospital, school or prison. The unavailability of a service would normally result in a reduced payment by the government to the contractor. The same occurs in case the services are not delivered according to the quality requirements established in the contract.

Therefore, performance monitoring is intimately related to the price and payment mechanism of the contract. Such mechanism has to establish the incentives for the contractor to deliver the services required.

### **Performance monitoring**

In order to allow for performance monitoring, it is necessary that the contract establish the following:

- the level of performance required;
- the method by which the authority will monitor the contractor's performance; and
- the consequences of the contractor's failure to meet the performance requirements.

### *Performance requirements*

As a general rule, the required performance should be established through output requirements such as different service standards which may be established and amended over time through benchmarking and/or market testing. It is important that the performance levels are reasonable and objectively measurable in order to provide sufficient comfort to private sector lenders that depend on the revenue stream of the project for repayment of debt.

### *Monitoring*

The contract has to establish a mechanism to enable the authority to monitor the contractor's performance against the requirements specified. Such requirements and the methodology behind them should be included in the public tender documents.

Monitoring should occur at the following levels, subject to considerable cooperation between the authority and the contractor:

- a systematic monitoring by the contractor through quality management systems established under the contract;
- a review of such quality management systems by the authority;

- planned and random spot checks of the authority;
- a reporting system for users (teachers, doctors, motorists, etc).

As a general rule, performance monitoring should commence at the moment the services are being provided on a normal and regular basis. The cost of monitoring should usually be borne by the party undertaking such monitoring. However, such cost should be proportional to the consequences of service failure. The contractor's quality management systems should be of an ISO 9000 or equivalent standard.

It will be necessary to establish a reporting system that meets the needs of all parties involved (authority, private sector lenders, etc).

### *Consequences of poor performance*

Performance monitoring is tied to the payment mechanism under the contract. Payment is normally due upon the availability of a service but not its actual use (for example, theatres in a hospital being available, irrespective of whether they are used for clinical procedures or not, as that is not within the contractor's control). Therefore, in a PPP there is normally a single so-called unitary charge to be paid once the service is available. Deductions are made from such unitary charge according to the severity of failure of performance.

The consequences of poor contract performance must be clearly established in the contract. One method is the use of performance points according to the seriousness of the failure of the contractor to meet the performance criteria. The seriousness of the failure should be the measure for the potential consequences for the contractor. Such consequences may range from a formal warning, through financial measures such as deductions from the payment to be made for the services, to the termination of the concession for breach of contract.

### **Conclusion**

Long-term performance monitoring under a PPP contract is essential for the success of the project and the provision of 'good value for money'.

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