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Comment

Keith Hennessey

Chapter 6 is excellent both as a primer on public-private partnerships (PPPs) and as a guide to effective PPP policy design.

Engel, Fischer, and Galetovic taught me some basic facts about PPP usage around the world:

1. Relative to total world infrastructure spending, the use of PPPs is quite small, on the order of 6–10 percent of total privately financed infrastructure and 2–3 percent of total infrastructure spending. I do not know whether this means that (a) there is significant upside potential and room for increased use of this tool, or (b) its use is small because it does not work well or is hard to do.
2. In Europe, PPP usage is almost entirely about transportation infrastructure, with a little health care thrown in. As the authors tell us, "For Europe, PPPs are a complement and not the main source of transport investment." They cite an example of a significant increase (65 percent) in Portuguese highway investment, but so far it seems that in Europe, too, PPPs have not caught on more broadly.
3. In developing countries, half the PPP dollars are going to roads, with the rest split roughly evenly among airports, railways, and ports. This makes intuitive sense, as each of these can generate a somewhat predictable revenue stream to justify private financing.

Having established some important facts, the bulk of the paper provides a helpful framework for how to think about whether and when to use a PPP. I would like to compliment the authors for their intellectual honesty. At the same time as they summarize policy design best practices and conclude that "PPPs can be a useful instrument of public policy," they are honest and direct about both the weaknesses in this policy tool and especially about the misconception that forms "the main motivation for their use." The misconceptions they describe are quite familiar to me from past American debates about PPPs, and if future debates were fully informed by this chapter, the likelihood of policy makers choosing wisely would increase substantially.

The authors emphasize that PPPs "have been attractive to policy makers because they promise to relax the fiscal constraints that limit resources for infrastructure projects." To me, the core lesson of the paper is that well-designed PPPs can make infrastructure spending more efficient, but they are usually pursued because policy makers mistakenly perceive them as a source of "free money."

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At the federal level in the US, this misperception is common. US federal budgeting works with a fixed-length, short-duration budget window: 1, 5, or 10 years. Almost all federal budgeting is done on a cash-flow basis over one of those time frames, always measured in nominal dollars. Federal budget rules score and bind fiscal impacts on the federal fisc only, ignoring both state and private sector impacts. US legislators often have short time horizons, with members of the House of Representatives facing reelection every two years, and senators every six. A policy tool that purports to leverage federal tax dollars for greater total spending, with the lion's share of the spending and financing off budget, is tempting to legislators. Since their budgetary constraints apply to only a portion of the true accounting, their decision-making incentives are easily distorted.

This budgeting structure interacts with the chapter in three ways.

1. If you wanted to implement the authors' methodology at the federal level in the US, you would have to change budget scoring rules. The authors recommend an all-in, long-time-frame, expected-present-value accounting approach that would move onto the government balance sheet the private borrowing and subsequent revenue streams within a PPP. That makes good policy sense but would be difficult in terms of the federal budget process. Would legislators be willing to devote the time and legislative capital to setting up such intellectually honest budget process changes to limit the use of a rarely used policy tool that would be more attractive without the reforms?

2. The authors correctly point out that policy makers' desire to evade fiscal constraints is one reason PPPs have been attractive to policy makers outside the US. This is also true in the US. Some US legislators think they can "lever up" federal tax dollars to get more total infrastructure spending. Part of the reason is just that they do not understand the full accounting in this chapter. Part of the reason is that the forgone revenues would not have accrued to the federal government anyway, so federal policy makers ignore these revenues. And part of it is willful ignorance or, if you prefer, overoptimism—an intense desire for a magic wand that will generate free money for them to spend.

3. The problem, then, is that when these scoring difficulties combine with policy makers' desire to use PPPs to simply spend more, by far the most likely outcome is that, if budget rules are changed, they are changed in a manner that unfairly advantages PPPs so that more money can be spent without policy makers getting "charged" for it.

The project selection and avoid-the-white-elephants arguments cited by the authors have also been present in US PPP policy debates. The most common form of this argument is that legislators make poor decisions about which projects to finance, because they are either unwise or skewed by political concerns. As the authors correctly note, "pork barrel projects and poor planning often build white elephants." Allowing "the market to

decide" which projects to finance will insert some discipline into the project selection process, advocates claim.

By "white elephant," it appears the authors mean projects with a low social return. Members of Congress look at this spending differently. Their focus is almost always limited by the geographic boundaries of the area they represent, and they are maximizing for some other measure of perceived benefit to the people and area they represent (weighted by their own preferences). Any effort to use PPPs to fight the desire of policy makers to allocate spending based first on geography would legislatively fail. If PPPs exclude projects with low social return in their districts, decision-makers will consider that a bug, not a feature.

The authors argue that government should use PPPs when they provide sufficient efficiency gains and that efficiency gains do not arise from private participation per se, but from the different incentives under both organizational forms. These may be the result of differences in risk allocation, contract design, financing, and political economy.

The authors describe seven efficiency claims for PPPs over public provision. I was convinced by the "narrow focus and dedicated management" claim, as well as the "bundling" and "fewer construction delays" claims, the latter of which I hope would be a high priority for US policy makers. As described earlier, I think the "filtering white elephants" argument is flawed because there are multiple legitimate criteria for deciding which projects are good. I found the "avoiding the cost of bureaucracies" and "advantages of private financing" arguments less persuasive. To me the most attractive potential efficiency gain associated with PPPs is "better and less expensive maintenance." In an American context, a policy tool that results in better-maintained transport infrastructure and addresses congestion externalities is exciting.

I also found the authors' principal policy design recommendation convincing: the use of present-value-of-revenue (PVR) contracts instead of fixed-term contracts. The US examples cited by the authors (the Dulles Greenway and Orange County's State Route 91) are good examples of the downsides of combining demand forecast uncertainty with fixed-term contracts. It would be interesting to see whether offering PVR contracts in the US would increase the number and quality of bids for a given set of transportation infrastructure PPP projects.

Despite good arguments made by Engel, Fischer, and Galetovic, I remain skeptical of the PPP as a tool for US infrastructure spending. Four questions merit further discussion.

1. How robust is the PPP design? This is the whiteboard problem. Suppose one begins a policy making process with an ideal PPP structure on a whiteboard, designed by the authors. Suppose further that design is modified by legislators, bureaucrats, and judges as it makes its way through the demo-

cratic process. Can the model still work, even though some of its features have been changed? It is of course impossible to answer this question in the abstract, but for a policy design to be worth pursuing, it should be legislatively and bureaucratically robust. It must work even when it is imperfectly implemented. There are a lot of moving parts in the design described by the authors and lots of points of potential failure. Is the PPP still worth pursuing if the implementation is only 80 percent faithful to the original design?

2. Managing the different elements of risk, the structure of the contracts, and the long-term relationships with private firms is, in the US context, the task of experts in the executive branch (specifically, the US Department of Transportation). The tasks described by the authors are conceptually challenging and may be bureaucratically even more so, especially if Congress is occasionally trying to interfere to "help." Is it worth developing the long-term expertise and skill set within the bureaucracy to effectively manage this when the aggregate size has so far been quite small?

3. Related to point 2 is the question whether it is worth the effort. Are the hypothesized efficiency benefits large enough, especially relative to just pursuing contracting reform?

4. Finally, does it make sense to improve and refine this policy tool if the "wrong reasons for PPPs" problem remains unsolved? That is, does it make sense to have a well-designed PPP tool if Congress is likely to use it for the wrong reason?

I thank the authors and NBER for the opportunity to comment and hope this input is helpful.