

## DESIGNING STATE-PRIVATE PARTNERSHIP IN MODERNIZED ECONOMY

*This paper discloses the essence and main forms of public-private partnership; the prospects for public-private partnership in the Russian economy at the stage of its launched modernization are estimated. Positive and negative aspects of public-private partnership implementation in Russian regions are revealed.*

The accumulated global experience in the practice of public-private partnership (PPP, concession) allows us to suggest that PPP is one of the most common forms of strategic projects worldwide, both nationally and at regional and municipal levels.

Public-private partnership starts with pooling of resources of the state or local government and the private sector of economy at a long-term and mutually beneficial basis for the creation of public goods or public services. As some scientists have fairly concluded, PPP is an institutional and organizational alliance (strategic contract) between government and business in order to realize projects of highest importance [1, p. 120; 10, p. 41; 6, p. 47; 12, p. 28-30]. At the same time significantly is that PPP allows to avoid, on the one hand, the drawbacks of direct state regulation, on the other hand the «market failures» [15, p. 6]. The main argument in support of PPP is that both public and private sectors have their own, their inherent unique (distinctive) features and benefits which together create the possibility to act more effectively and achieve better results in those economy sectors or economic activities where «market failures» or weak governance are particularly noticeable. The key point of the strategic government and business alliance serves the objectives and needs of each party.

Public-private partnership is a relatively new but very promising tool for implementing strategies of territorial development, whose effectiveness is determined, first of all, by systematic structure and strategic focusing. Moreover, PPP projects are implemented mainly in supportive (infrastructural) sectors of regional economy, these sectors act as a factor of regional competitiveness which largely determines modernization of the economy in general and individual economic activities in particular.

Cooperation between government and private sector has a long history. Roman civil law already provided the possibility of granting concessions to

private individuals for the supply of the population with clean water. At the end of the XIX century a prominent Russian thinker of liberal-conservative orientation, B. N. Chicherin (1828-1904) emphasized: «The government only helps it (private activity — authors' note) and fills it in to the possible extent where it is not enough» [16, p. 224]. The state «should not take on something that may also be done well by private forces» [16. 229].

In the process of developing a market economy as well as of developing the privatization process in today's Russia, a significant number of large private companies with subsidiaries in many regions and municipalities were established. Private business has now become an important component of Russian economic policy. Thus, there is an urgent need to harmonize the interests of government and business at an early stage of economy modernization, including the regional level [5, p. 40; 2, p. 105-108, 186-193].

Partnership between business and government in the majority of infrastructure sectors is currently considered as a basic compromise which essence is to preserve the public (state or municipal) ownership of infrastructural facilities and, at the same time, to involve private business into creation, modernization and management on the basis of relevant contracts. In addition, we should note that if the traditional global experience is represented by public-private partnership having an infrastructural character, in Russian conditions, as highlighted in the report «On the mechanism of interaction between federal and regional executive authorities in the designing of integrated socio-economic development of regions» [14, p. 51-63] prepared by a workgroup of Russian Federation's State Council on the integrated socio-economic planning and regional development (July 2006), we should actively implement the principles of PPP into the real sector of economy to accelerate development of industrial areas, both raw materials and high-technology-related. It is important that both private businesses and joint public-private partnerships projects and (or) municipal-private partnerships were of strategic importance not only for business groups but also for Russia as a whole, for specific regions and municipalities.

It is becoming increasingly clear that ensuring high and sustainable rates of territorial develop-

ment, achieving ambitious strategic goals of the Russian Federation's subjects and municipalities cannot proceed without a committed partnership of government and municipal authorities with business representatives. Policies and programs that are guided only by the use of limited budgetary resources do not allow the authorities to carry out large-scale and strategic projects that are the basis of territories with high competitiveness.

We can't but agree with V. Samarina that our economy could grow much faster and the modernization processes could be carried out more intensely if partnership between business and government would be developed rapidly and effectively without undue restrictions [11, p. 83]. There seems to be no mistake that the report of the XV Congress of the Russian Union of Industrialists and Entrepreneurs was accentuated on the fact that «the economy and business communities receive mixed, contradictory and not always predictable signals from the state, that increases the uncertainty in projections of economic agents and worsens the conditions for long-term projects. This is the reason for a relatively low (in comparison with the generally favorable economic situation) entrepreneurial activity and a sense of growing medium-term risks of Russian business» [3, p. 49]. We should agree with the conclusion that in order to improve efficiency of the state economic policies «not only «a flow» of bills, resolutions and ordinances is necessary, but, above all, predictability of the environment, legal protection, a system of partnerships, taking into account the objective interests of the major parties on the development and public decision-making regarding the business environment and investment climate» [10, p. 50].

The existing Russian regulatory framework for the implementation of PPP projects remains imperfect. Gaps and shortcomings in the legislation will always be, any law is not ideal and can be improved infinitely. Federal law «On concessional agreements» is no exception. The absence of many standard concessional agreements, difficulties in forming a consortium for the concessionaire, the uncertainty in the order of agreement management — these and other widely discussed shortcomings of the legal framework in the field of PPP are likely to be largely eliminated with time. However, many legal gaps which are characteristic for the existing regulatory and legal framework for PPP can be eliminated or narrowed by a more detailed project preparation. The industrial peculiarities of PPP, preparation of concession agreements, maintenance contracts and

procedures for cash calculations etc. need to be especially clarified.

For justice' sake it should be stressed that the legislative framework of public-private partnership in Russia is now undergoing the process of development. For the short term a set of modern tools of public-private partnership appeared at the federal level:

- Special economic zones of three types (industrial production, technology development, tourism and recreation);
- Investment Fund of the Russian Federation;
- Law on concessions;
- Venture Fund of the Russian Federation.

It is notable that the applicable state investment instruments (the Federal targeted investment program and the Federal fund for regional development) are already undergoing some particular upgrade [9].

At the regional level, more than 90% of today's Russian Federation's subjects are equipped with the investment laws of a particular quality. 73 regions have tax benefits, 61 regions have state guarantees on loans, 60 regions practice co-investment into commercial projects, 50 regions provide investment tax credits, 43 regions subsidize interest rates on companies' loans etc<sup>1</sup>. In some of Russian regions there already are new laws governing the relations which develop in public-private partnerships in a specified area. In particular, in 2006 the Legislative Assembly of St. Petersburg adopted a law «On participation of St. Petersburg in public-private partnerships» and the regional Duma of Tomsk region adopted a law «On the basis of public-private partnership in Tomsk region». To date, ten Russian regions have already adopted regional laws on PPPs.

In modern Russia, private companies are significantly ahead of the state in ensuring development strategies. However, as the realities of today have shown, the realization of only 1 out of 10 long-term plans of big business does not experience serious difficulties caused by underdevelopment of many components of both productive and social infrastructure. One must agree with the position of those economists who believe that an important

<sup>1</sup> Conference «Investment opportunities in Russia. Principles and risks of public-private partnership» (21st of November 2006, Moscow). Report of the Institute of Regional Policy in a consortium with the analytical center «Expert» and the agency «Lobbynet-GR» (Electronic resource, <http://www.regionalistica.ru>).

feature of public-private partnership in Russia may become the concept of «the state follows business», referring to the joint efforts to overcome the infrastructural constraints in the implementation of specific strategic projects. However, in the traditional understanding of public-private partnership demonstrates the opposite situation, i.e. it is characterized by the concept of «the business follows the state», based on which the state is making some efforts to attract private capital into infrastructural development.

Russia has already formed a certain set of problems and risks in establishing public-private partnerships; these problems and risks not only form some of PPPs' specific content but also inhibit its extension across the country. Professionals identify the following points more often than other ones:

- High level of corruption at all levels of government, which determines a significant risk to compliance with the partnership relations;

- Significant business superiority over the state in staff training, preparing and implementing projects through public-private partnership;

- Adverse and imperfect legal environment for the formation and development of public-private partnership;

- Low willingness of the state apparatus to comply with business agreements and high level of the political situation impact on the selection and implementation of economic projects;

- Low level of confidence in the economy and in the society as a whole [13].

As the practice shows, there is a lack of trust between key players inside PPP—this is one of the major problems hindering the development of partnerships. In 2010, the Center for Development of PPP in conjunction with the Institute of Contemporary Development did a research in 18 regions called «Development of PPP in the regions of Central Federal District: investment and infrastructure». The survey showed that PPP is often perceived by officials in the region only as a way to shift a detrimental object onto the private partner and, thus, to solve existing problems through a private partner. Business, on its turn, wants profits and expects from the state to receive an attractive object into management (or ownership) or to create a profitable business. Among the reasons for this situation is lack of tradition of such partnership. Trustful relationship does not appear immediately, it builds up gradually during many years. Lack of necessary trust between partners emerges as a result of continued communi-

cation barriers between the main key players inside PPP.

Some positive experience of partnership between the state and the private sector, cooperation between business and government has been gained in Europe, where in 1980–1990 a correction of the government role was noticed — from the perception of it as a structure self-generating certain services to the perception as a structure guaranteeing provision of those services by the private sector, for which it creates the necessary framework conditions for running relevant business. The accumulated experience of public-private partnership, which became widespread in many countries, contains both stories of success and failure.

In accordance with international practice, the following forms of PPP are considered perspective:

- Contracts as an administrative agreement between the state or local governments and the private firm to carry out specific activities. In such contracts, property rights are not transferred to the private partner, the costs and risks are fully carried by the state. Interest of the private partner is to get the right to the revenue share which is stipulated in the contract;

- Rent in its traditional form and in the form of leasing. Traditional rental agreements require recurrency of the subject of leasing relations, authority (of powers) of the property are reserved to the owner and not transferred to the private partner;

- The concession is a specific form of relations between the government and the private partner. The state in the frames of partnership remains the property owner and authorizes the private partner to perform certain functions during a certain period of time and delegates certain authority of powers;

- The feature of joint ventures is that the state is constantly involved in ongoing production, administrative, economic and investment activity;

- Outsourcing.

The main form of public-private partnership recognized in today's global economy is concession. One of the explanations for its widespread usage in various strategic projects is the interest both of the state and private business. The interest of the state while transferring objects in the concession can be traced in the following areas:

- Reduction of budget spending on infrastructure development as the government shifts the burden of expenditure on construction and maintenance of relevant facilities onto the business;

- Increase revenues from taxes and other payments into the budget since concession payments

reach the budget as well as the load of complex financing of public facilities is removed;

— Solving the most critical socio-economic problems by attracting substantial funds and resources to implement large-scale projects;

— Mobilization of modern management technologies, innovative solutions and elements of effective competition into infrastructural industries.

The attractiveness of the concession projects for the private capital is as follows:

— The business gets state assets (which do not belong to it) into long-term management, often on preferential terms of payment for the concession;

— Private investors acquire additional guarantees of return of their money as their partner (the state) also carries some risk;

— The concessionaire has a real chance to earn money in sectors that are traditionally dominated by state-owned companies if implementing more productive and innovative activities.

In the late 1990s subsurface objects have been actively transmitted into the concessions and power generation facilities, transport facilities, ports, airports etc. to a significantly lesser extent. However, this process is not as strong as needed for economic development. The main reasons for the inhibition, as a rule, are the weakness of the legislative framework, the instability of state-business relations plus other reasons. In addition, government, business and society have limited and sometimes even distorted view of the nature of concessions, practice of their application and the possible economic and social consequences. The analysis shows that the profitability of business in the form of concessions is small — 5 to 20%. However, the multiplicative effect of the concessions could be hundreds of millions of USD taking into account the large amounts of capital expenditure into major projects [5, p. 37].

The effectiveness of partnership relations within the frames of different PPP projects (deals) will be as higher as more the progressive institutional environment will be, the more transparent the concessional activities will be and the more effective control over it will be. The problem of the image of the state as a strategic business partner is also important both in the process of selection for PPP projects and in discharging of its contractual obligations.

In Russian practice PPP mechanisms are usually used in large-scale investment projects. An example of this is the formation of the Russian Federation's Investment Fund which is supporting business

projects worth at least 5 billion rubles. Public-private partnership projects have a wide range of implementation: transportation, housing and public utilities, construction, finances, social affairs etc. However, in Russian conditions the active implementation of PPPs is also vitally important in subordinate entities of the Federation and municipalities. This is due to the fact that the main purpose of PPPs for the authorities is likely to create a more efficient system of public goods (services) production than just to finance the investment needs.

Today it is still too early to speak on how successful or not successful the PPP experience in the Russian regions is. Nevertheless, the process is developing. Among the successful regional projects, the projects in St. Petersburg gained fame above all others: construction of the Western High Speed Diameter, construction of Orlovsky tunnel, reconstruction of Pulkovo airport. In modern Russia the practice of PPP has just started gaining experience and we have a unique opportunity to use rich international experience of PPP which is actively implemented into a wide variety of projects both in economic and social spheres, both at federal and regional plus municipal levels. The interests of various territories in this area might differ. The first goal is to overcome systemic or sectoral crisis. The second one is diversification and restructuring of the economy to reach sustainable development. The third one is reaching the state of a prosperous region on the new stage of economic development.

Of course, there are still many issues in the way of PPP formation and development in Russia and some of Russian regions including the Urals. It is noteworthy that public-private cooperation is already showing real results. Thus, in early 2007 in the oil industry workers' city of Noyabrsk began the construction of the first combined-cycle power plant with capacity of 124 MW at the expense of private capital<sup>1</sup>. Another example is designing of «Project of South Yakutia's development» which aims to create a major new industrial area on the principles of public-private partnership<sup>2</sup>. Investors of this project are HydroOGK, Tekhsnabeksport, East Siberian Metal Mining Company, «Polyus Gold» and others; the customer is the Ministry of Economic Development of Sakha (Yakutia) Republic.

An example of partnership between the state and private capital will also be the thermal power

<sup>1</sup> According to the data provided by <http://www.invur.ru/>

<sup>2</sup> According to the data provided by <http://redionalistica.ru/>

plant TPP-3 in Tyumen<sup>1</sup>. In 2007 Tyumen region has become one of the first areas where government and private industry have joined forces to create a municipal interconnected electric power system. The situation in municipal energy system in the Southern part of Tyumen region is now stabilized. This is largely due to intensive reconstruction and activation of repair activities which resulted in lowering the deterioration of the equipment; it has been reduced from 70 to 50%. It is also important that such lowering was achieved not only because of the tariff component, but, first of all, due to involvement of private investments. The project to build the thermal power plant TPP-3 in Tyumen with electric capacity of 324 MW and thermal capacity of 440 Gcal has good prospects; TPP-3 will be launched on the basis of public-private partnership. The area of this project has already been defined, design and exploration work together with environmental survey are being conducted, technical and economic parameters to support investments are being clarified.

It seems important to start developing projects based on the principles of public-private partnership at the municipal level. The law № 131 «On general principles of local self-government in the Russian Federation» which came into force on the 1st of January, 2006, gives significant opportunities to PPPs. This law confirms clear separation of municipal property and municipal budgets with their sources, establishes the ownership rights on land. It is therefore important to intensify the activities of local authorities in implementing the project «Industrial Ural — Polar Ural» by attracting businesses into municipal economy for providing the so-called public services. In this case a note should be taken of interesting and useful experience in the formation and development of PPPs at the municipal level in Europe [4, 7, 17]. Particular attention should be paid to the fact that the main factor which is limiting the interest of private business to participate in PPP remains high institutional and commercial risks as well as legislative and socio-economic constraints reducing the efficiency of private investments. An important factor for successful implementation of PPP is the presence of a predictable and stable market.

The project «Industrial Ural — Polar Ural» is largely targeted into the future and implementation of a public-private partnership will form the basis of economic diversification in Subpolar and Polar

Ural, reduce the dependence of Khanty-Mansiysk and Yamalo-Nenets districts as well as the whole country from oil and gas budgetary revenues. The impact of «Dutch disease», whose presence in Russia has been noticed reputable domestic and foreign experts [8, p. 78; 18, p. 42], might also be reduced.

We should agree with the position of those research scientists [6, p. 51] who are directly associate prospects of PPP development with strategic territorial planning which not only initiates the emergence of joint private and public sector projects but also acts as an effective institutional mechanism for developing and implementing these projects. It is crucially important that PPP is not a one-time arrangement between business and government for the supply of certain services but is by definition a strategic tool for building partnerships between business and government in a particular area in order to implement the socially significant projects and programs of a wide spectrum. In other words, the development of public-private partnership is not an end in itself but a way of solving strategic problems of a specific subject of the Russian Federation or a municipal entity.

The development of broad business competition to improve the effectiveness of public-private partnership in modern Russia is of particular importance. Conservation of the old relations, exclusive access to participation in the most favorable PPP projects will not stimulate the development of cooperation between business and government. Only healthy business competition in all phases of PPP projects will attract business to cooperate and contribute to the modernization of economy and enhance its competitiveness in today's economic environment.

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