

Auditing of public procurement at a regional and municipal level

Panel 2

Problems associated with the awarding contracts for PPP projects

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1. Rhineland-Palatinate / Court of Audit



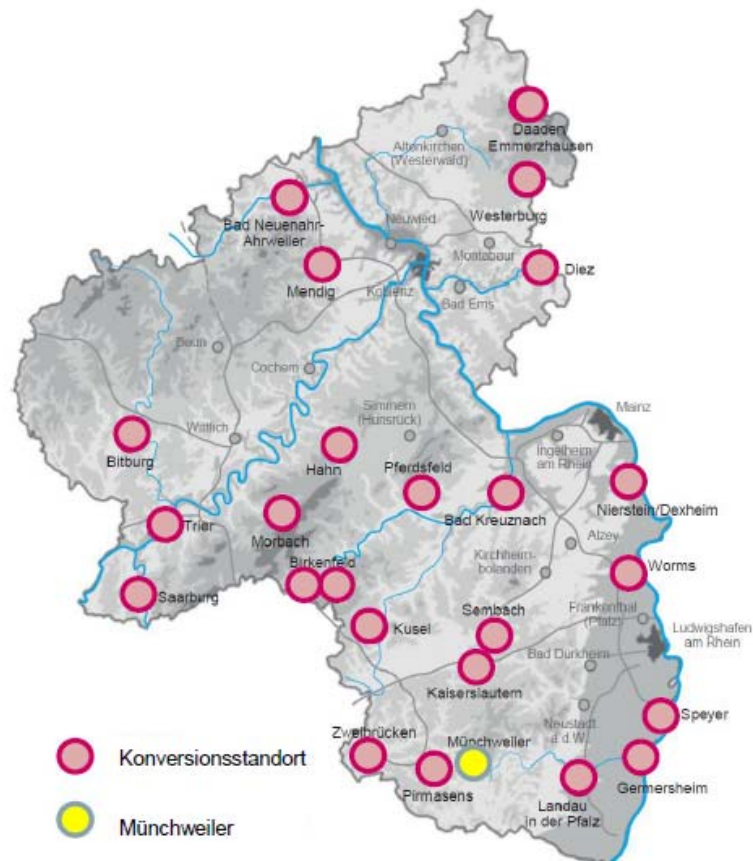
Rhineland-Palatinate:

- Inhabitants: 4,000,000
- Surface area: 20,000 sq km
- Civil servants at state level: 98,000
- Civil servants at municipal level: 65,000
- Budget for the state: €24.5 billion
- Budget for municipalities: €13 billion
- Economy:
Agriculture, viticulture, forestry, tourism (castles), industry (BASF), TV stations (ZDF and SWR)

Court of Audit:

- Employees: 180
- Auditing of budgetary and financial management at state / municipality level and their companies; public broadcasting

2. Conversion in Rhineland-Palatinate – key facts



Rhineland-Palatinate: 'a NATO aircraft carrier'

1980s:

- Soldiers: 127,000 (70,000 Americans, 40,000 Germans, 17,000 French)
- Civilian staff: 50,000

2013:

- Soldiers: 44,000 (27,000 Americans, 17,000 Germans)
- Civilian staff: 16,000

1992 to 2013:

- 680 military properties covering a surface area of 14,000 ha made available
- Amount of funding since 1992: approx. €2 billion
- Amount of funding for 2013: €34 million

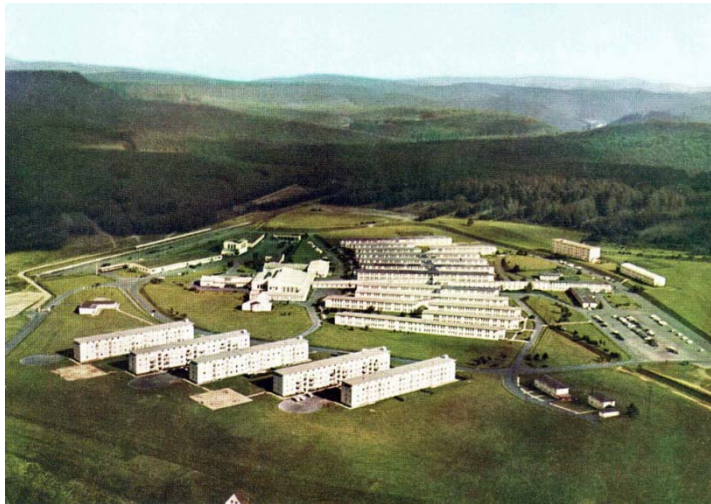
2. Conversion in Rhineland-Palatinate – examples



Types of conversion:

- Commercial development
- District development
- Renewable energies
- Housing development
- Higher education development

3. From US Army Hospital in Münchweiler to Gräfensteiner Park – background (1)



Site:

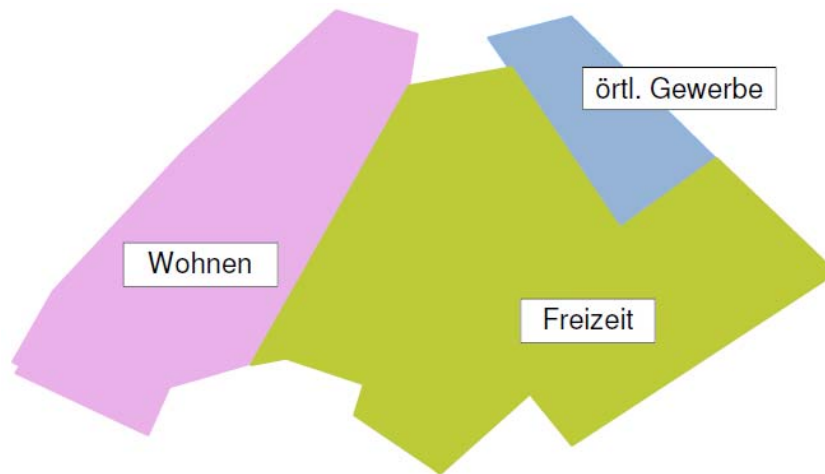
- Münchweiler: 3,000 inhabitants
- Nearest major town: Pirmasens, 40,000 inhabitants
- Distance: 8 km

US Army Hospital in Münchweiler:

- Built: 1955
- Capacity: 1,000 beds
- Surface area: 44 ha
- Important employer in an underdeveloped region
- 1993: Operations ceased; property handed over to the Federal Republic of Germany
- 1993–2002: Unsuccessful search by the municipality for a serious investor to create jobs with private capital

3. From US Army Hospital in Münchweiler to Gräfensteiner Park – background (2)

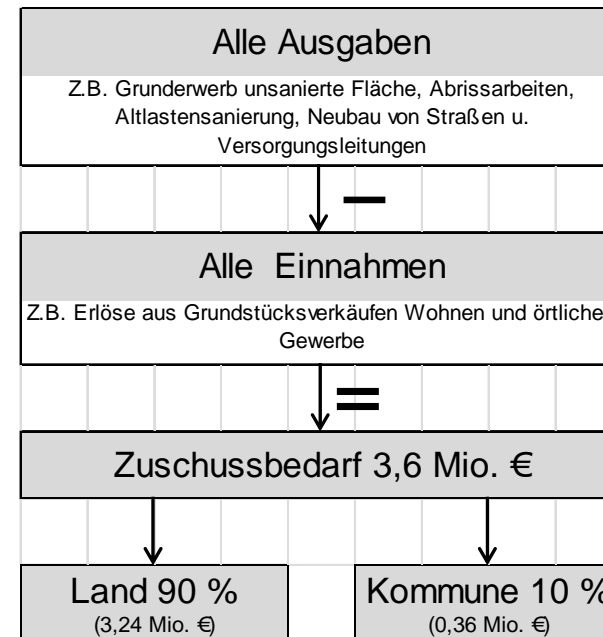
Municipality concept:



End of 2002:

- 18 ha for house building and small local businesses
- 23 ha for leisure use
- Funding based on the comprehensive rehabilitation process

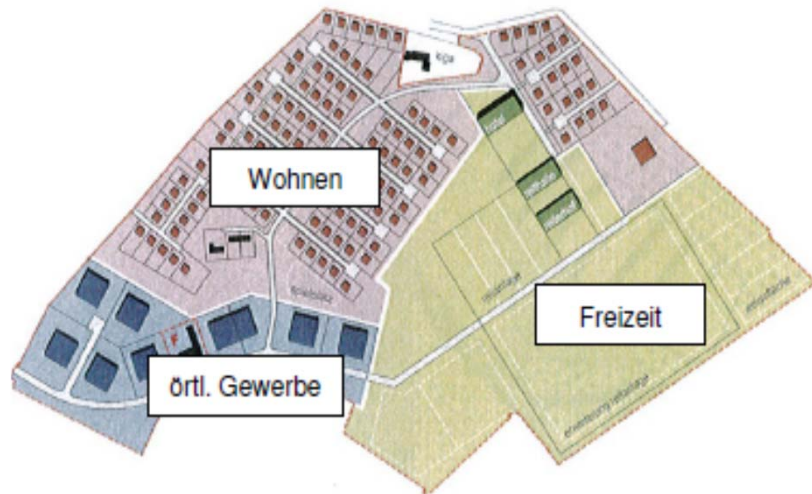
- Comprehensive rehabilitation process / measures increase the value of the land significantly. Public funds for demolition work, roads, and utility pipelines are partly replenished by revenue from the sale of land



- Simplified rehabilitation process / measures do not increase the value of the land significantly. Public funds not replenished by revenue from the sale of land

3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (1)

Investor concept (PPP):



Mid-2003:

- Leading official at Ministry for Internal Affairs introduces investor for PPP project

Use of space comparable with municipality concept:

- 18 ha for house building and small local businesses
- 23 ha for leisure use

Investor commitment to leisure use:

- Equestrian centre
- €45 million of private investment
- 450 new jobs

Ministry's decision:

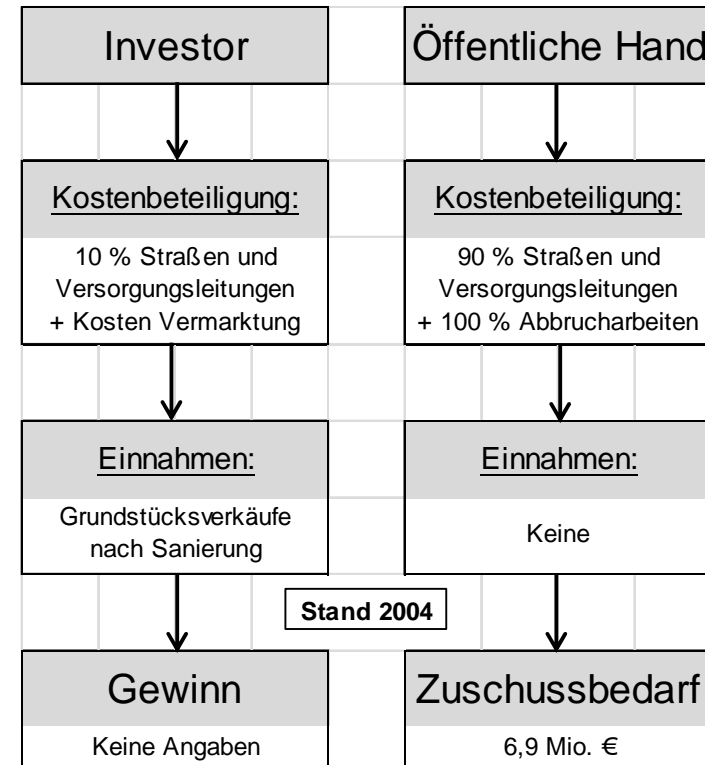
- State funding for PPP project only

3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (2)



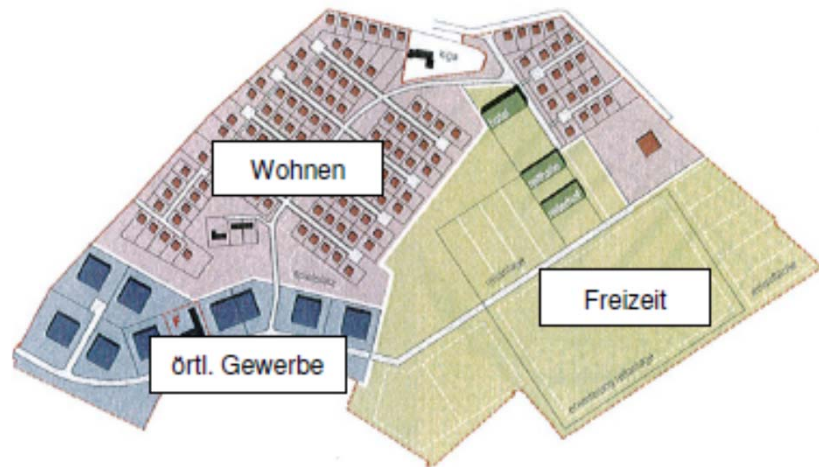
Investor demands during contract negotiations:

- Transfer of project management
- Transfer of planning and demolition work
- Funding based on the simplified rehabilitation process



Investor and ministry justify the need for higher subsidies (worth an extra €3.3 million compared with the municipality solution) by pointing to the commitment made in terms of private investment.

3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (3)



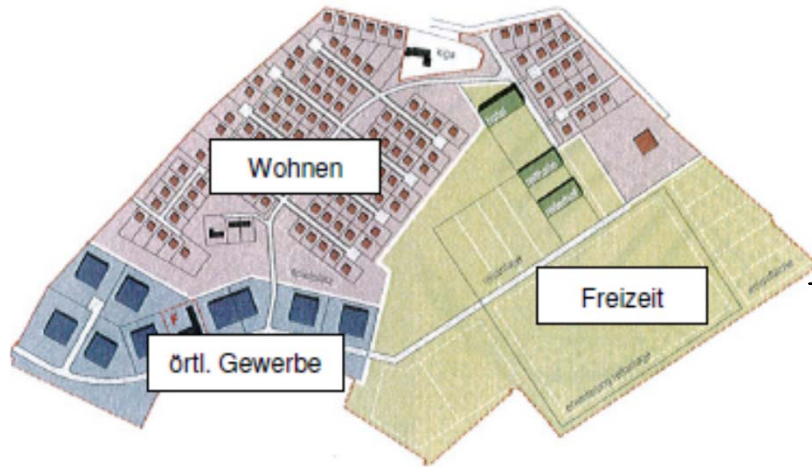
- Equestrian centre with 4-star hotel (200 rooms) including a 1,800 sqm spa area
- Equestrian facilities; including for polo matches (50,000 sqm)
- 'Horse-related' retail outlet (2,500 sqm)
- Horse clinic

Development scenario for houses / local businesses:

- House building
- Small local businesses



3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (4)



Actual development for leisure:

- Brownfield



Actual development for houses / local businesses:

- House building
- Small local businesses



3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (5)



Evaluation of the PPP project:

- Hopes not realised in terms of **infrastructure** (no equestrian centre, no 450 jobs, no private investment worth €45 million)
- Investor made private investment - e.g. 4-star hotel - conditional on additional public funding
- Feasibility or financial studies were neither provided nor demanded
- Simplified rehabilitation process not **permitted** (because of significant increases in land value associated with housing plots – from €3/sqm to €56/sqm)
- Public purse exposed to all the risk
- Privatisation of profits / socialisation of losses

3. From US Army Hospital at Münchweiler to Gräfensteiner Park – funding (6)

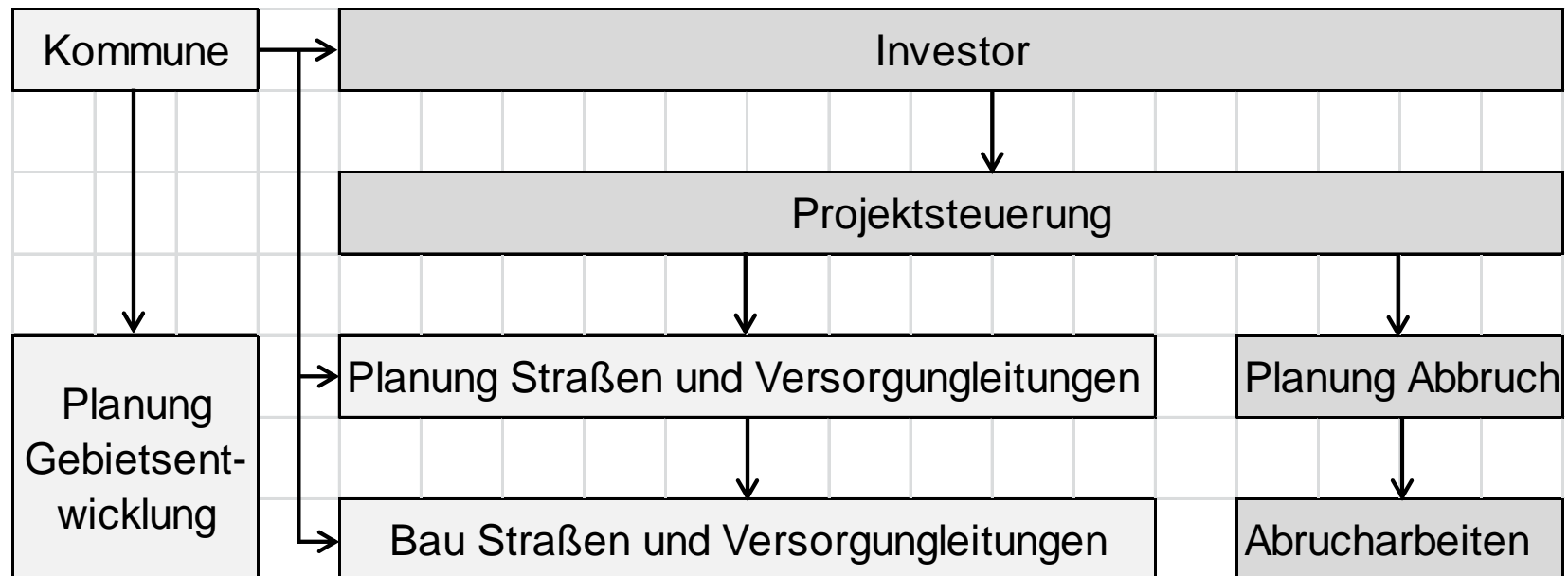
Financial consequences of the change of model:

Year	Model	Subsidy required (million €)	State share (million €)	Municipality share (million €)
2002	Forecast for municipality model	3.6	3.24	0.36
2004	Forecast for investor model	6.9	6.21	0.69
2014	Actual costs for investor model	9.3	8.37	0.93

- The requirement for public subsidy has almost tripled as a result of the investor model
- The municipality solution would have been €5.7 million cheaper without the increases in construction costs
- The investor, having incurred costs of around €2 million, has realised some €6 million through the sale of land
- Profit comes to some €4 million

3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (1)

Those involved in implementing the concept:

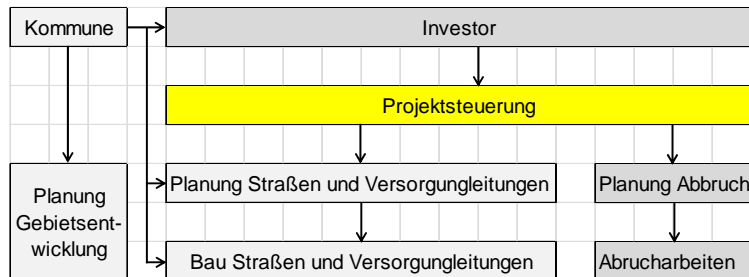


3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (2)



Project management:

- Investor commissions itself to take on project management work itself
- Investor awards itself a higher-than-average fee
- Public purse pays for fee
- Commissioning of project management is superfluous and overpriced – investor itself has the expertise
- Avoidable costs: €180,000

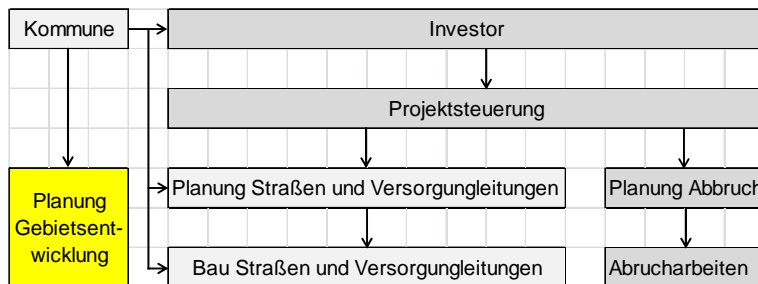


3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (3)



Development of the area:

- Municipality invites tenders for planning work
- Shortly before submission of tenders – renegotiating concerning work involved with subsequent planner – significant reduction in work involved
- Tenders are not comparable
- Pressure from investor and ministry influences municipality, which decides to award contract to subsequent planner
- Once contract awarded – work involved increased back to original level and final amount charged was twice as high as for the cheapest bidder
- Loss of €95,000



3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (4)

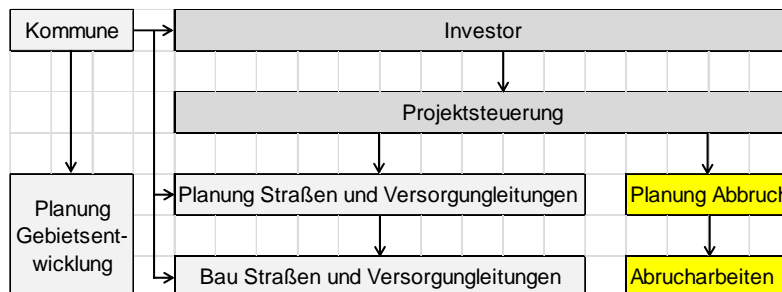


Planning for demolition work:

- Investor awards own company contract for planning demolition work (at almost double the fee / €45,000 additional costs)

Performance of demolition work:

- Investor rules out cheapest bidder unlawfully (a tender based on an all-inclusive price – as permitted in the documents for the tender process – is not assessed)
- Company chosen becomes insolvent before work already paid for is actually performed (at the time of insolvency 90% of the work had been paid for but only 70% had been performed)
- Allocation of uncompleted work also breaches conventions applicable to awarding of contracts (no public tender process, but a restricted one instead in which only parties who had not participated in the previous public tender process had been excluded from it, or had submitted a comparatively costly tender were invited to bid)
- Total final charge for both €600,000 higher than tender from cheapest bidder excluded

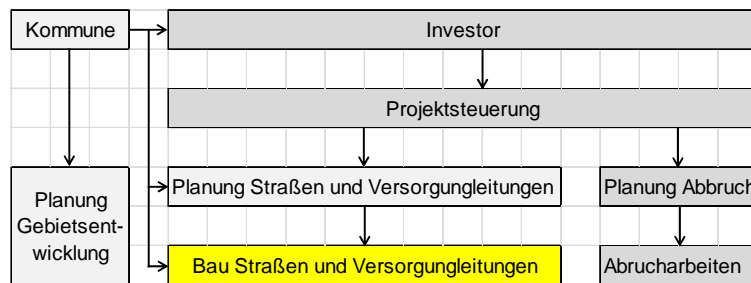


3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (5)



Building of roads and utility pipelines:

- Project management by investor
- Planning by external engineering firm (contract awarded by municipality)
- Three construction phases
- Work associated with two construction phases – total charge €3 million – unlawfully awarded by investor: information relating to subcontractors or equipment lists were not provided, even though specifically requested



3. From US Army Hospital at Münchweiler to Gräfensteiner Park – awarding of contracts (6)

Additional costs through profligate awarding of contracts:

Type of work	Additional costs (€)
Project management	180,000
Demolition planning	45,000
Planning for development of the area	95,000
Demolition work	600,000
Total	920,000

Work commissioned unnecessarily and excessive fees resulted in additional costs of €920,000

Major infringements in terms of contract awards:

Type of work	Total charge (million €)
Demolition work	1.5
Building of roads and supply pipelines	3
Total	4.5

- Construction work for which a total of €4.5 million was charged involved major infringements in terms of the contracts awarded
- Possible consequences: requests to have grants returned
- Ministry promises to look at reducing grants

4. Summary (1)



PP – public private partnership:

- The Court of Audit for Rhineland-Palatinate has audited various PP projects in the past
- None proved to be good value for the public purse
- Audits conducted by other German courts of audit echo these experiences

Basic problems with PP projects:

- High costs for external consultants
- Financial calculations often inadequate and overly focused on profitability
- Efficiency benefits mainly based on unrealistic assumptions
- Complex contracts are too much for public-sector partners
- Long-term contracts can be problematic if requirements change
- PP projects ultimately tend to be more expensive than conventional projects
- Debt not reflected in budget
- Financial burdens deferred

4. Summary (2)



Recommendations for PP projects involving private investors:

- Ensure there is competition for projects to be developed with the help of investors or the PP model
- Perform feasibility studies and risk assessments
- Conduct cost-benefit analyses for various development scenarios
- Agree monitoring / sanction options and obligations to provide information in contracts with private transaction partners
- Ensure costs and risks are shared fairly between partners from the public and private sectors

4. Summary (3)



Basic recommendations for awarding contracts:

- Lots of competition (public tender process if at all possible or another form of open process)
- Transparent awarding of contracts and transparent documentation (all bidders treated the same)
- To be performed by the public authorities:
 - Checking and sending of all tender-related documentation
 - Submission (opening of tender process)
 - Checking of tenders
 - Awarding of contract
- Associated checks (project manager accountable to public authorities)

4. Summary (4)



Thank you
for
listening!