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### An entrepreneurial state in India?

*Investigating public-private partnerships, incomplete contracts and risks in the transport infrastructure sector*

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## Chapter 05: Institutional Arrangements and Relationships in the PPP Project

The previous chapter provided insights on the entrepreneurial Indian State's dedicated efforts to institutionalise the flow of private capital in airport and highway infrastructure development, albeit through a pro-business approach. Continuing at the macro level of policy analysis, this chapter examines the economic relationships between the State and the private sector at the overall level of a project. The specific research question this chapter addresses is, 'What strategies do the heterogeneous stakeholders in a PPP arrangement employ in order to interact with regulatory processes at the macro level of the project?' Focusing on 'varieties' of economic organisation involved in a PPP project, this chapter examines the evolution of intra-State, inter-firm and State-firm relationships in market creation.

The chapter has three main sections which explore how laws (or the absence of them) have affected the strategies stakeholders develop. The first section analyses the absence of a cohesive PPP law at the national and state government levels, in lieu of which PPP guidelines were framed. It examines how legal ambivalence through guidelines shaped relationships of delegation between the national and sub-national states. This is followed by a discussion on strategies of collaboration and competition that private firms deploy in order to enter the market, gain control of the project cycle, maximise stakes and sustain their involvement. The second section focuses on insights on intra-State, inter-firm relationships, which set the foundation to study cooperative and conflictual power relations between the State and the firm within the stages of the project cycle. The analysis explores strategies actors employ to shape rules of the game by using the project cycle instrumentally to their gain. Key among instruments of the project cycle are PPP contracts. Going deeper into specific roles of transacting parties in a project cycle, the third section outlines the strategic purpose of three main types of contracts--Concession Agreement, State Support Agreement and Operation and Maintenance Agreement--focusing on how conditions of ownership embed bargaining power. The chapter concludes with questions on the nature of 'State-firm' relationships and the politics behind rule-making, at the macro policy level as well as the micro level of the project.

### 5.1. Understanding Intra-State, Inter-firm Relationships

The first section of this chapter draws on the theory of 'state rescaling in India' to understand intra-State power relations as they affect PPP projects directly. A lens of collaboration among transacting agencies, despite the divergences in their primary goals, informs analysis of inter-firm and State-firm relationships at the overall level of the project. Preceding these, the section below establishes the flexible regulatory context within which these project-level relationships are shaped.

#### 5.1.1. Regulatory Flexibility

Across the world, there are no unified models for the PPP framework. PPP models are a plural conglomerate of laws, policies, procedures, institutions and rules. Together they legitimise the purpose with which a government employs the model for infrastructure development.

International case studies<sup>42</sup> have consistently shown that a government's PPP framework generally evolves over time in response to specific risks in the national and local context. The credibility of regulatory frameworks to facilitate private investments varies by country [Levy and Spiller, 1994: 202]. The effectiveness of a regulatory framework depends on its ability to facilitate private investment, respond to a country's political institutions and mediate economic-social institutions [ibid]. Examining this macro level intent, Chapter 04 explored how political elites in India instrumentalised a regulatory paradigm to channel private finance at national and sub-national levels of the government. Moving deeper into the governance framework, at the project level, where a basic PPP framework intersects

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<sup>42</sup> Brazil, Chile, Colombia, France, Indonesia, Mexico, Peru, Philippines, South Africa and Tanzania are countries with PPP Laws (See, The World Bank, 2017, Annex, PPP Reference Guide Version 03, PPP Knowledge Lab).

with multiple laws, actors and sectoral specificities, interactive dynamics were complex. Actors in a project cycle were required to navigate laws on multiple fundamental issues, including transparency in public procurement, equal treatment of prequalified bidders, contentions of land ownership, land acquisition, resettlement and rehabilitation of project affected people and environmental laws. Laden with divergent institutional values, public-private partners interpreted regulatory mandates in differing ways, complexifying the process.

In the Indian context, the optimism of the initial policy formulation phase soon gave way to operational risks, particularly for the highways sector [Mohan, 2004: 40]. As was the case in other countries, projects across sectors navigated a multitude of laws and rules, including administrative laws, environmental laws, land acquisition laws, stipulations for property rights, licensing laws (particularly for international firms), tax rules, codes for bankruptcy, monetary policies, employment law and insurance laws<sup>43</sup>. Multiple contracts exacerbated this regulatory variety. Project approval requirements, including budgeting, expenditure and reporting, are all prescribed through contractual agreements.

However, the national and sub-national States led no dedicated efforts to combine the multiple pre-existing legal, regulatory frameworks through a consolidated PPP law. Instead, the central government worked with internationally established paradigms to develop guidelines. The main purpose was to streamline processes in order to regain the confidence of the private sector [PPP Guidelines, Government of India (GoI), 2013: iii]. The State's challenge was to respond to a heterogeneous stakeholder group: international organisations, the State (sectoral ministries and national and state governments) and firms (international, domestic, large, medium and small). To what extent did PPP guidelines address diverse expectations? Now bound in a PPP agreement for public infrastructure development, to what extent did the stakeholders meet public purpose goals?

### ***5.1.2 Centralised Decisions: Intra-State Relations***

This section explores conditions that led to the framing of PPP guidelines, roles of transacting parties and expectations of stakeholders. The processes of development of the PPP project cycle reflect power relations between national and state governments.

#### *Ministerial Guidelines*

By the early 2000s, PPP projects under several ministries had started to face constraints. Chapter 04 discusses how paucity of funds led the central government to activate National Highways Authority of India (NHAI) to develop the National Highways Development Programme (NHDP) through PPPs [Haldea, 2002]. Faced with resistance from incumbent officials at the NHAI and inadequate capacity to handle complex processes, initial efforts of the NHAI towards adoption of the PPP mechanism suffered setbacks (Kishengarh section of NH 08) [ibid]. However, resorting to pre-existing models of contracting was unsustainable due to the magnitude of loans the government had accessed from commercial banks and international finance institutions.

At the sub-national level, several states implemented state highway projects<sup>44</sup> through a Build Operate and Transfer (BOT) mode under PPP [ibid]. This process initially gained traction. However, BOT contracts revealed over time that they were deliberately structured in biased ways to facilitate monetary interests of contractors as opposed to inducing efficiency in investments or catering to user convenience [ibid]. While the mainstreaming of PPPs in airports occurred later, similar challenges exacerbated tensions in the power sector and, to some extent, the water sector. In response, the central government developed an elaborate policy, regulatory and contractual framework for PPPs in

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<sup>43</sup> This thesis does not cover a complete analysis of all laws and policies related to PPPs.

<sup>44</sup> Executed with no involvement from central government.

2004, in an attempt to enhance transparency, fair competition and efficiency in implementing the policy [Haldea, 2015: 03].

### A Centrally Led Process

Despite being a partnership effort between national and state governments, the process of policy formulation was largely restricted to the central government level. The Cabinet Committee on Economic Affairs (CCEA), under the Ministry of Finance (MoF) Department of Economic Affairs (DEA), in a Cabinet meeting of October 27, 2005, gave directives to constitute a Public-Private Partnership Appraisal Committee (PPPAC), involving several members from the national government<sup>45</sup>. Given the significance of contractual governance for PPPs, the Ministry of Law and Justice's Department of Legal Affairs played a key role in the PPPAC, carefully scrutinising contractual agreements. While national level bureaucrats and experts dominated the committee, it lacked direct political representation (elected officials). Formal representation from sub-national levels of the government was also absent, depicting a national State desirous of preserving decision power, despite devolved power relations that PPPs solicited.

The government remained committed to streamlining the PPP process to augment private sector participation. The CCEA purposefully permitted the PPPAC to 'co-opt experts as necessary'. Consulting the private sector at the strategic stage of framing guidelines would reconcile the differences of public-private parties along the course of the project cycle [interview, PPP expert, Gol, 2017]. However, private representation was not systemically designed to garner partnerships towards innovation in the PPPAC, but remained subject to the discretion of its members.

Building on the approach of multiplicity, the DEA prepared 'Guidelines for Formulation, Appraisal and Approval of PPP projects in India' (PPP Guidelines, Gol, 2013), which lays out broad institutional arrangements for administering key stages of the PPP project cycle. The guidelines reinforced the Indian government's intent: 'by leveraging public capital to attract private capital and undertaking a larger shelf of infrastructure projects, PPPs bring in the advantages of private sector expertise and cost reducing technologies and efficiencies in operation and maintenance.' [PPP Cell, Gol].

Given the vital role ascribed to it, in enhancing quality at optimised costs, the private sector demanded predictability of process as well as clarity on public sector accountability, since multiple contractual adaptations pursued by sectoral departments often caused uncertainty and risks [Highway SPV managers, 2018]. The document responded by outlining the project cycle, institutional composition, roles and responsibilities of public sector agencies, clearly vesting ownership, control and responsibility as well as liability with the national government [PPP Guidelines, Gol, 2013: iii]. Duties such as project identification, project agreements, inter-ministerial consultations, procurement processes, appointment of concessionaire and appraisal processes were conferred to the national level sectoral ministries. While not overtly affirming the state government's role, PPP Guidelines elicit 'clearance' and 'support needed from state governments' [PPP Guidelines, Gol, 2013: 06]. Conducting feasibility studies was unambiguously included. However, no political engagement was suggested at this stage. Political vision, economic growth targets, employment generation and financial viability of the project were only implicitly entrenched in the process. The delineation of institutional roles, responsibilities and relationships between actors was incomplete in the guidelines.

If a system of rewards and punishments defines accountability [Rao and Singh, in Kapur and Mehta, 2005: 376], the guidelines made no provisions to invoke either for the central or state governments. Instead, in the old tradition, the DEA's PPP Guidelines centralised decision-making powers with the PPPAC. Considering the large value of projects and their country-wide visibility, PPP Guidelines places

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<sup>45</sup> Including the Secretary, Department of Economic Affairs (the Chair); Secretary, Planning Commission; Secretary, Department of Expenditure; Secretary, Department of Legal Affairs; and Secretary of the department sponsoring a project

the MoF at the helm of all strategic decision-making, including examining concession agreements from a financial perspective, deciding public sector guarantees, extending government contributions to equity, safeguarding concessionaires, assessing risks pertaining to government expenditure and seeking investments (from private party lending agencies).

The administrative ministries and/or the sectoral ministry executing the project are entitled to the extent that they can negotiate terms of the project with contracting parties in an inter-ministerial consultative committee<sup>46</sup> meeting. Consequently, at the level of PPP projects, the guidelines bestow ownership as well as key decision-making to sectoral autonomous authorities, during the process of project administration (such as NHAI). Table 5.1 is an interpretation of this distribution of responsibilities between government agencies across the project cycle.

	PPPAC	Planning Commission/ NITI Aayog	Sponsoring Ministry, Gol	Sector specific authority	State and local governments	Private sector	Lending agencies
Project identification	X		X	X			
Feasibility studies	X	X	X	X			X
Project agreements	X	X	X	X			X
Inter-ministerial consultations	X		X	X			
Approvals	X		X	X	X		
Request for Qualification	X		X	X	X		
Request for Proposal	X		X	X	X		
Formulation of contracts	X		X	X	X	X	X

**Table 5.1:** Roles and responsibilities of public, private representatives in a PPP project cycle

Source: author's corroboration of learnings from interviews and DEA's 'Guidelines for Formulation, Appraisal and Approval of PPP Projects in India'.

Enhancing the PPP guidelines, on request from state governments, the Planning Commission's PPP Cell drafted standardised norms among a wide range of financial structures. Model Concession Agreements (MCA) and standard procurement processes were drafted using international best practices. Streamlining the process, it was felt, would mitigate risks for public officials, private investors and lenders [Haldea, 2012: 44, 46]. My interviews with state government officials revealed that the MCA received critical acclaim from international finance institutions and state governments for inducing stability and transparency. However, ministries perceived its content as rigid and 'mandatory as opposed to recommendatory'. With little sense of ownership, they took no responsibility for adopting the document [Krishna, S, 2011<sup>47</sup>]. Private parties also remained sceptical of its adoption, while struggling with its 'onerous requirements and inflexibility' [ibid].

<sup>46</sup> According to these guidelines, the then-Planning Commission was to set up and monitor a PPP Appraisal Unit (PPPAU). Presently under the NITI Aayog (replaced the Planning Commission of India in 2015), Project Appraisal Management Unit (PAMD) appraises public sector projects. The PAMD plays a technical and administrative role in appraising and alerting elected representatives of complex contractual terms and risks.

<sup>47</sup> 11 December 2011

Some practitioners complained that the absence of a central law, combined with discretionary, selective adoption of guidelines increased possibilities for interpretation of contracts, in turn reducing predictability [interviews, 2017]. As a counterpoint, critics argued that regulatory flexibility is not a constraint to performance, when accompanied by complementary mechanisms to restrain arbitrary administrative action [Levy and Spiller, 1994: 202]. My fieldwork revealed that government's own internal administrative processes already accommodated the necessary checks and balances. For example, national and state governments routinely mobilise administrative laws and procedures to establish multi-layered committees involving elected representatives, sectoral officials, bureaucrats specialised in particular domains and private sector representatives in order to conduct scrutiny of proceedings in specific government initiatives. The heterogeneity of these committees in terms of roles, values and objectives helped foster checks and balances in decisions. However, their mobilisation with PPPs was often contingent on political motivations backed by business interests [interview, state government official, airport SPV, 2018]. Overall, an incomplete set of guidelines remained partially or opportunistically adopted, falling short of fostering partnerships across multiple scales of public and private institutions.

#### *Delegating Risks to the State Government*

Intriguingly, the PPP guidelines only make a cursory mention of state government's involvement in the process: one, on clearances and 'other support' required from the state government; and two, caveats (in contracts) to contingent liabilities that the national government has to bear by providing guarantees to their private partners (concessionaires) against non-performance on the part of state governments. While the state government is a partner in the PPP shareholding arrangement, the guidelines seem to place their contributions in a secondary role. The norms seem to treat state governments almost as a liability to the central government. Interviews with officials at the state level, however, revealed that the situation is more intricate.

State governments were anything but complacent. The context of a rescaled State persuaded competitive state governments to carve out their positions as major sites of regulation [Kennedy, 2014: 52]. Given this context, those state governments with greater capacity to generate and administer funds and land, co-initiated projects with the central government [interview, senior official, state government, 2020]. Often guided by sub-national, regional political demands, these states actively determined scale, scope and location of projects. Multiple state government departments are involved and in fact compete in this process<sup>48</sup> [interviews, Special Purpose Vehicle (SPV) state government representative, 2017-18].

State governments bear a range of social, economic, financial and political risks. The liabilities of delivering the heightened promise of employment opportunities is translated to state government levels, since the power and accountability for 'economic and social planning' is vested with both the central and state governments as per the Concurrent List of the Seventh Schedule of the Constitution of India. More tangibly, norms for PPP project cycles do not mandate post-project measurement of employment or growth as outputs. Contrary to political claims that infrastructure is a key catalyst to growth, critical literature has amply demonstrated that growth occurs based on a set of contextual forces – political environment, institutional arrangements and capacity, skills, infrastructure and geography. Often these forces are contingent upon institutional performance involving multiple actors [Storper, 2010: 19; Jenkins et al., 2014]. Through a study of 28 states in India, Misra argues that for general category states<sup>49</sup> the social infrastructure has greater influence on output than economic infrastructure (including transport) [Misra, 2015]. Given this anomalous relation between

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<sup>48</sup> Department of Industrial Development, Department of Transport, Public Works Department, Department of Infrastructure Development and Department of Finance, to name the key organisations involved.

<sup>49</sup> States capable of mobilising own resources for their developmental needs, versus those faced with special social, economic geographic constraints.

infrastructure and output, success or failure of infrastructure projects in providing local benefits would appear to directly affect electoral risks for politicians at national and state levels. However, this is seldom the case. As I have discussed in Chapter 04, infrastructure projects remain deliberately contained within elite politics, distant from the general public. Local and regional political agents are made aware of national government initiatives, mainly through the state government's land acquisition process, which forms one of the first key steps to initiating a project on PPP mode.

Fundamental to PPPs are the private sector's access to land and property rights for the contracted period. The responsibility and risk of acquiring unencumbered land are state government responsibilities, as the regulation of use of land under private ownership, in India, lies with the state government<sup>50</sup>. For approvals, the Public Works Department (PWD) at the state government level in the case of highways and concerned enterprises affiliated with industrial-infrastructure development departments for airports generally bear the burden of ensuring clearance of social and environmental impact assessments. Finally, the state government's safeguards to the concessionaire through the State Support Agreement (SSA) form a key prerequisite to initiate a PPP-based project [interviews, SPV representatives, 2017-8].

While the normative premise of the guidelines seems to place the state government in a subordinate role to the national government<sup>51</sup>, a Joint Venture (JV) arrangement between the national and state governments in a PPP places a substantial responsibility and risk on the state government [interviews, senior officers, state government, 2017-8]. In this context, state government's disposition towards the centre translates into conflicts, resistance or negotiation [Sinha, 2003: 467], depending on the state's administrative, economic capacity and political relations with the concerned ministry. Officials at the national government often criticised the state governments, citing inefficiencies and opacity as key hurdles to successful implementation of PPPs [Haldea, 2012: 46, 47]. State government officials counter this perspective. The centre, they argue, often opportunistically uses their long-drawn out, risky efforts to mobilise land and finances in order to leverage political and administrative mileage [interviews, state government officials, 2017, 2020]. Studies undertaken by international finance institutions underlined the lack of a cohesive regulatory framework to unify national and state-level governance [Economic Times, 2012<sup>52</sup>]. This analysis supports my own, of the tensions between state and national governments, which are an integral characteristic of rescaling processes.

#### Limited Responsibilities for the Private Party in the Guidelines

While the guidelines underscore the importance of 'leveraging private capital', they refrain from imposing any public purpose obligations on the private sector. Instead, they point towards PPP contracts, more specifically the Concession Agreement, as pivotal to defining the terms, rights and obligations of all parties. The guidelines thus ascribe seminal importance to micro level contracts as prime legal instruments which bind the private party to deliver their responsibilities which have implications at the macro level. Going beyond intra-State tensions, ambivalent legal relationships that supersede specific political or administrative jurisdictions complicate rescaling processes of the State.

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<sup>50</sup> In a federal governance structure, Town Planning Acts at the state level prescribe conditions for the use, acquisition and pooling of land.

<sup>51</sup> The AAI places the national government as the primary owner on PPP projects, while marginally recognising state government's contributions. For example, the website of the AAI states, 'Government of India has been encouraging participation of state Governments in development of airport infrastructures. The New Bangalore Airport, New Hyderabad Airport and Cochin International Airport (CIAL) are examples of participation of state govt. through JV. In the Domestic airport, state governments normally hand over the required land for development of airport free of cost and free from all encumbrances as a token of state government participation. The examples are Vizag, Khajuraho, Amritsar, Pathankot, Dehradun, Lucknow, Varanasi airports where respective state governments have given land free of cost.' <https://www.aai.aero/en/content/what-role-state-govt-upgradation-airports>; Retrieved 15 June 2020.

<sup>52</sup> May 31, 2012

In summary, the PPP guidelines were an incomplete remedy for reducing risks that projects faced in the preliminary phase. Importantly, the set of guidelines lacked foundations in establishing institutional arrangements which laid out roles of all institutions involved and relationships between them. An entrepreneurial State disposed towards developing strategic orientations would have purposefully built alliances between the central and state governments and between government and private sector to serve wider societal benefits. However, the guidelines concentrated power at the national level and involved state government in minor ways. Norms introduced in the guidelines merely tendered procedural clarifications to the private sector and remained silent on private sector accountabilities. To the dismay of some innovation theorists [Mazzucato, 2018], an approach to 'fixing' flaws in the process disregarded making a cohesive vision that percolates all levels of governance, from senior bureaucrats to operational staff. I argue that the limited and incomplete approach of the central government reinforced the nascent pro-business strategy, although through a bureaucratic approach rather than an entrepreneurial one. The procedural approach the framers of the document adopted refrained from pro-actively steering complementary forms of economic organisation within the political economy of the PPP mechanism. The behaviour of this pro-business-bureaucratic State reinforced the dynamic of rescaling.

Having observed how State agencies used the guidelines to allocate power at the project level, I now turn to analyzing the organization of the private sector, vis-a-vis the project cycle and the PPP market.

### ***5.1.3 Variegated Markets: Inter-Firm Relations***

In a State space of incomplete guidelines, by 2008, firms offering a range of competencies pertaining to infrastructure finance and engineering had started to consolidate their presence [2008, authors' reflections from her urban practice]. The PPP Guidelines of the DEA (2013) were not meant to guide interactions between firms in the creation of a market. Within this flexible regulatory environment, private firms organized themselves through different types of consortia, to in order to capture multiple opportunities that PPP markets offered.

#### *Market Variety*

For the government, creating markets meant regulating relationships between a variety of firms from multiple industries such as infrastructure, finance, retail and construction, and regulating experimental engagements among them as well as with a heterogeneous State [corroborating Srinivas, 2012: 171]. In order to analyse this relationship, I have categorised firms under six main types, based on their core competencies.

*Firm type A, financial services:* International, domestic firms with high annual turnovers (greater than one billion USD), offering services at the strategic level, including procurement management consultancy, market assessment, project feasibility studies, project financial structuring, auditing of projects, firms, due diligence of financial/technical design of projects and advisory services for debt-restructuring.

*Firm type B, design:* International and national companies engaged in technical expertise, involving master planning of new townships, allied trunk infrastructure, detailed technical engineering design, web-enabled data-led software design systems for tracking project progress and independent engineers (IE) for quality control, including setting standards for smart, sustainable engineering.

*Firm type C, design, programme management, investment, operations:* International and national firms (one billion USD turnover) offering competencies starting at the managerial level, project management, master planning of new townships, allied trunk infrastructure, detailed technical engineering design, IE for quality control, investment, execution, project operations and maintenance of selected PPP projects.



*Firm type D, construction:* Project execution for construction contracting firms which sub-contract with material suppliers. Public sector units (such as Engineering Procurement India, Ltd) also compete with private firms in this space.

*Firm type E, programme managers, execution, non-banking lending:* Firms offering end-to-end services from procurement to operations (with turnover of one billion USD). Competencies include technical advisory services, procurement management, programme/project management, market assessment, project feasibility studies, project financial structuring, due diligence on financial and technical design of projects, asset management, training and skill development.

*Firm type F: Legal services and arbitration:* Law firms offering services in dispute resolution at all stages of the project cycle provide services to companies for dispute resolution, including arbitration, litigation and interpretation of regulatory and contractual terms.

The project cycle supports variety through several types of collaborations between these firms and markets. First, at the upstream end, international (some domestic) firms who offer advisory services also prepare feasibility studies involving 'financial and project structuring'. Firms preparing this study strategically develop scope for continued involvement of private companies in the project cycle. Such a self-serving cycle, wherein the regulated firms create norms for the regulator to perform its own functions, diminishes the salience of public accountability, as argued by Raco [Raco, 2014: 179]. Second, a small range of large sized firms compete fiercely through public contracting in order to capture these markets within the project cycle the State offers. They explore partnerships to leverage exclusive technical skills and financial strength, while eliminating other players in the market. Firms attempt to eliminate competition through several channels: one, by partnering with others; two, by suggesting formal amendments to procurement documents to persuade exclusive entry to projects. Exclusivity is leveraged on technical, managerial, contractual or financial parameters [court proceedings of legal disputes, Annex II, Case 02; interview with senior manager private firm type A, 2017]. My interviews reinforce scholarly observations that international (as well as large domestic firms) formed larger cohorts to lobby for highly specialised criteria for procurement and technical standards in order to eliminate smaller firms [Braithwaite, 2008, cited in Raco, 2014: 177. 178. 179].

Third, large domestic firms, often backed silently by national and / or state-level political interests, resisted the rise of other firms through mergers, acquisitions and bonded partnerships, intending to dominate the market [interview, employee, firm type A, 2017]. Fourth, some projects in the PPP market necessitated scales of investment and technological expertise for which existing firms lacked capacity. Government policy attracted international firms, but with prerequisites that facilitated building of local capacities and knowledge transfer. Foreign Direct Investment (FDI) policy initially mandated that international firms partner with local ones to this end. For example, the airports sector required several such international-domestic firm partnerships in order to emulate global best practices. For projects with total project costs above one billion INR (10-12 million USD), international firms generally lead the consortia by developing concepts, while domestic firms executed them in the field in order to mainstream and scale up international practices.

Fifth, a handful of large firms, promoted jointly by public and private organisations (offering end-to-end services), also created niche opportunities for themselves as programme management consultants to secure their place throughout the project cycle. A constant condition was incumbency of firms unfamiliar with challenges of PPPs. Several medium-sized pre-existing contractors who never fully grasped the risks the PPP model posed faced bankruptcy over time, marking exclusionary creative destruction of firms. A small segment of large old domestic firms with a strategic bent, i.e., construction firms, which had large turnovers accompanied by experience, morphed themselves organisationally,

reinforcing historically embedded development of infrastructure investment markets that the rescaled State engendered.

Ubiquity of Private Firms in the Project Cycle

Generally, no one firm offers all competencies. In a market where financial risks are high, bundling all services magnifies risks [interviews, Managing Director, private firm, 2018]. To minimise risks of large investments, firms experimented on pooling risks through partnerships or sub-consultancy arrangements. Table 5.2 below shows their spread. Through an intricate and often drawn-out process of internal networking, private companies occupy the entire range of tasks in the project cycle they had developed on behalf of the State [interviews, 2017]. The project cycle incorporated new forms of ‘contractual packaging’ [as Bentley and Rafferty, 1992, (cited in Raco, 2014: 181) have argued about mega-projects], which were ‘broken-up’ along their trajectory and aligned to suit firm competencies.

Firm types	A: Financial Services	B: Design	C: Programme management, design, selective investment, operations	D: Construction	E: Programme management, construction, non-banking lending	F: Legal services, arbitration
Project cycle						
Enabling policy environment	X	X	X	X	X	
Feasibility studies and financial project structuring	X				X	X
Bid process management	X		X		X	X
Design		X	X			X
Quality Control	X	X	X		X	X
Construction				X	X	X
Operations and Maintenance			X	X	X	X

**Table 5.2:** Private firm competencies along PPP project cycle

Source: author’s research

Coalitions also navigate procurement rules of the government. Government public procurement processes establish clear conditions for ‘conflict of interest’ in order to forbid firms from working in consecutive stages of the project procurement process [Tender Guidelines, Central Vigilance Commission]. Firms thus seek sub-consultancy arrangements in order to participate in the project, while manoeuvring flexibly designed norms. Even merely participating in the public procurement process allows firms to access information and stay in the decision-making game [interviews with bid managers in firms and government departments, 2016].

In the preliminary phase of PPP adoption, firms sought partnerships with great optimism. However, with an increase in risks, firms started to tread more carefully, paying attention to firm and project histories, client relationships and political leverage of potential partners, among other factors. In the years 2011 and beyond, firms internalised market-led skills and aligned themselves with performance standards and risks they co-created with the State.

### The Private Consortium forming Concessionaire

This section discusses the economic reasoning that guides private companies to form coalitions. Generally, in order to mitigate risks, due to the high value of projects, the grantor (government agency) determines firm qualification criteria of the concessionaire (private firm), requiring them to demonstrate proven capacity for completion of substantial financial, managerial and operational tasks on similar projects at the national or international level. In a bundled contractual arrangement, the concessionaire is primarily accountable to deliver the scope of work, including design, construction, operations, project management, finance and legal management. However, most firms lack holistic competencies and struggle to assemble proven capacity through multiple strategies. Scholars have examined three key forces--innovation, opportunism and diversification to optimise costs--that firms generally prioritised as criteria for capturing markets through collaboration [see Casper, in Hall, Soskice, 2001: 398-99, for analysis of industrial-corporate strategies Germany, the United States].

*Diversification to optimise costs:* Firm capacity to take on risks varies considerably [interviews, 2016-18]. To deliver diverse obligations, the lead firm applying for the role of concessionaire typically needs to engage with specialised experts and consultancy firms to internalise the preparation of financial feasibility studies, urban and regional master plans, architectural and engineering design, independent audits or reviews. To optimise transaction costs, large firms generally form consortia or sub-contracting arrangements with medium-sized firms [ibid].

*Opportunism:* Collaborations promising political networks and least-cost bids were preferred. International and domestic firms often employed ex-bureaucrats in order to ease navigation of complex bureaucratic processes and expand networks internal to the government [interviews, private firm type B, 2018]. Large firms backed by a nexus with politicians often showed proven capacity through partnerships with fictitious companies they themselves registered, in order to retain financial flows within political-business circles [interviews, 2016; Sachdev, The Quint, 2018<sup>53</sup>].

*Innovation:* For the market as for the State, hybrid organisational innovations to enable a workable collaboration was key. Firms restructured their organisations to mimic rescaled organisational structures within the government. Sectoral heads of corporate companies (urban development, water, airports, highways), although highly technically qualified, seemed inadequate for facing complexities that PPP projects now demanded. Regional business heads replaced the sectoral heads in order to lead business development and manage complex contracts. Their business acumen was perceived as a match for high strategic calibre officers from the Indian Administrative Service or political shrewdness. Firms established internal specialised risk committees to scrutinise partnerships before bidding [interviews, private firm representatives, 2016-8].

With the emergence of private players, the *road and highways* construction market has become substantially variegated in size [IBEF, 2018], and the market in turn targets projects of varying scales. A fragmented private highways operators market lacks a cohesive organisational structure at sectoral level. The private airport sector is represented by the Association of Private Airport Operators (APAO<sup>54</sup>). The APAO interacts with policy makers and politicians in order to lobby for the needs of the industry. To leverage suitable markets, they co-organise events and conferences to influence policy in their own favour [drawing on Saxenian, 2001, on the IT industry in India].

Although regulatory, pro-business capitalism affected the priorities of the State in establishing robust institutional arrangements, the markets that evolved in the national highways and airport sectors (from about 2008 onwards) demonstrated several economic traits (as in other industries), including

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<sup>53</sup> 21 December 2018

<sup>54</sup> APAO is an apex Industry Association of the major private airports in India, established in 2009; <http://www.apaoindia.com/>; Retrieved 26 August 2020..

differentiation, oligopolies, concentration, dominance of multi-nationals in establishing overall contours of the PPP project cycle and some innovation [Pant and Srivastava, 2015; Hall and Soskice, 2001; Srinivas, 2012].

#### *Fragmentation Among Lending Agencies*

Processing long-term loans spanning 20-30-year contract periods is challenging for public or commercial lending agencies in India [interviews, PPP finance experts, 2019]. Model processes established by GoI recommended that the bulk of the financing should be borne by lending agencies, in particular public sector banks (PSB) [Haldea, 2015: 03]. Given the large outlay of finances required, PSBs formed consortia to finance projects estimated at a total cost of ten billion INR (about 150 million USD) and above<sup>55</sup>. Risks of investment were thus spread thin across multiple lending agencies. Three key issues confronted lending agencies. One, PSBs lacked capacities to conduct due diligence of project risks and viability which would safeguard loan repayments from concessionaires. Funds provided by PSBs were in reality diverted by private concessionaires towards other ventures of the parent company while accountants from the SPV consistently showed losses on their accounts [interviews, Indian engineers now working on international projects, 2018]. They were also utilised for financing gold-plated costs (giving the customer more than expected). Two, managers of PSBs are often subject to interference from politicians who instruct them to offer requisite loans to projects, with little consideration for due diligence [interviews, bank staff, 2019]. Bank managers thus tread a politically sensitive terrain of struggle, often risking their personal credibility and security, while developing loan structures and pricing strategies that are mutually viable for them and the concessionaire. Three, concessionaires of many projects national highway projects, seek to raise loans from commercial banks on a 'non-recourse' basis [Haldea, 2015: 10]. In other words, lending agencies have no guarantee of assets or collateral in the case of defaulted loan repayments. Moreover, infrastructure assets are 'sunk investments' with zero value for alternative buyers [Flyvbjerg et al., 2003]. As a result, commercial banks insist on State guarantees for loan defaults as safeguards against their own risks [interviews, bank staff, 2019], thus transferring risks to the State [interviews with finance experts, 2019]. Lending institutions thereby contribute to the disproportionate risk-bearing by the State.

For the government, retaining private investment also meant establishing financial instruments to aid projects facing financial duress. To this end, backing this network of risk organisations are partnership arrangements between banking institutions and 'funds' established by the central government. In 2006, in response to financial strain faced by a majority of PPP projects, the central government established 'funds' such as the India Infrastructure Finance Company Limited (IIFCL). A variety of funds involving partnerships between PSBs, international finance institutions and private firms were formed over time in order to address project risks, making the State and public banks integral to financial risks that private firms experienced.

Having explored intra-State, inter-firm relationships at the project cycle level, the section below expands on State-firm interactions in the phases of the project cycle.

## **5.2 State-Firm Interactions within the Project Cycle**

In a partnership arrangement, the roles of State and private sector agencies mutually affect the other's performance. As custodians of policy formulation and implementation, government organisations frame laws, rules and procedures to regulate multiple markets within the PPP. However, the actual governance of capital investments in both airports and highway sectors, including for consultancy services, engineering design, construction, construction material supply, labour contractors, facility operators and users, are market-led (feasibility, financial project structuring, clustering, linkages and

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<sup>55</sup> For example, IDBI Bank Limited: Consortium for Infrastructure Project Financing, 25 June 2012; <https://www.marketscreener.com/IDBI-BANK-LIMITED-9743068/news/IDBI-Bank-Limited-Consortium-for-Infrastructure-Project-Financing-14384753/>; Retrieved September 04, 2020.

pricing). As innovation theorists have argued (in the case of growth of Information technology, in India), the challenge for the State was to enlarge the range of participants in policymaking and scope [Guhathakurta and Parthasarathy, in Shaw, 2007; Saxenian, 2001]. In fact, pro-business alliances between the government and businesses had restricted essential policy debates. Therefore, investigating interactions between State agencies and firms as part of a wider evolving market environment is necessary [drawing on Srinivas, on the pharmaceuticals industry in India, 2013: 46].

Market variety poses the challenge of interactions between heterogeneous sets of actors, which bring together differentiated institutions [Srinivas, 2012]. For instance, values and norms governing the banking system may be misaligned with those of the infrastructure construction industry, making collaboration between them complicated. The rules orienting actions of State agencies at the national level may diverge from state government prerogatives. Procedures catering to redistributive goals of the government may be poorly aligned with both the private investors involved at various scales and the lending agencies. While the State-firm collaboration seems paradoxical, viewing the process through the position of innovative institutions helps clarify the prevalence of varying institutional values.

Researchers examining the entrepreneurial State through the lens of uneven development [Harvey, 2006] focus attention on contradictions in values among interacting institutions. In contrast, the innovative institutions approach is a 'sympathetic' one, where theorists view the State's planning apparatus from a multi-faceted lens, where the State is endowed with multiple values and obligations [Srinivas, 2012: 04]. They argue that regulations/norms governing interactions between divergent institutions may or may not be complementary to one another [Jackson, W.A, 2007: 235-253]. Significant here is the work of economic and human geographers, who steer away from clear distinctions between the State and markets in order to mark the emergence of the hybrid domain, an intermediate space of collaborations between society, corporate societal responsibility, the State and policy, and that incorporates both public and private interests [Aoyama and Parthasarathy, 2016]. However, in order to evaluate risks in PPPs, this study extends the lens of regulatory capitalism on hybrid firms. Rather than view the State and the market as institutions in mutual opposition (as traditional economists do), this study endorses the counterargument that the innovative institutions approach suggests that development inherently embodies 'institutional variety', including States, firms, technical standards, insurance and citizenship [Srinivas, 2012: 05]. This theoretical framing of institutional variety informs the analysis of cooperative and conflictual public-private institutional relations below.

All stages of the PPP project cycle for airport and highway projects involve interactions between a variety of public-private stakeholders. Five stages are significant for our discussion:

1. Navigating demand and supply
2. Feasibility studies
3. Procurement of concessionaire's services
4. Establishing a SPV
5. Contract execution

Stakeholder relations at each stage are discussed below.

### ***5.2.1 Navigating Uncertain Demand and Supply: Promotion***

As seen in Chapter 04, creating demand for private sector investment in PPP projects required policy reforms and institutional restructuring. In the case of the airports sector, Chapter 04 shows how privatisation unfolded in phases, owing to lack of private sector interest, until negotiations led to contractual alignment. Over time, governments at the national, state and local levels collaborated seamlessly to test private sector demand before launching costly tendering processes. Over time, public

institutions adopted market-led measures as precautions. One such measure demonstrating its entrepreneurial shift is discussed here.

To prove commercial attractiveness of the project in the preliminary stage, the grantor started to undertake the challenging task of promoting the project. Upon receiving Parliamentary approvals for project viability, the grantor develops communication strategies to disseminate the components of the project through roadshows, typically, a strategy that the private sector adopts for marketing products. Master plans for the infrastructure facility and its real estate potential are presented to international and domestic private investors as an attractive product. Locational advantages of the project are valorised. Measures taken by the grantor to render the project free of risks and encumbrances is highlighted. Total project cost estimates and revenue projections are set out. With a pro-business approach, grantors cross their conventional boundaries and use media publicity to promulgate information on the merits of projects [author's attendance of a public roadshow for a railway station modernisation project, 2019]. Despite promotional measures, which test the boundaries of the State, a few clauses in the financial model of proposed projects may still seem unviable for private investors. A well-meaning 'risk-taking' grantor may even have to shelve the project or defer its launch, to the loss of its public provisioning goals.

### ***5.2.2 Feasibility Studies, Financial Project Structuring: Outsourcing***

Central government guidelines require all identified projects to be tested for financial viability. At this stage, rather than conducting an internal investigation, central and state government agencies generally outsource feasibility studies to private firms who bring the necessary technical expertise on financial analysis of projects [interviews with financial analysts; study of Feasibility Studies, 2016-2019]. For the grantor, private firms develop the financial structure of the project. This includes defining scope, location and land requirements through political involvement. Technical teams estimate total project costs, capital needs, cash flow and potential sources of revenue, pricing strategy and revenue share arrangements, generally aligning them with existing political ambitions. The world over, feasibility studies are critiqued for being overly ambitious and inadequate in anticipating financial, political and legal risks [Flyvbjerg, Bruzelius and Rothengatter, 2003]. My interviews align with this analysis. The intermediary space of State-market alliances at this stage is characterised by wilfully inadequate attention of contingencies projects may encounter. This is particularly so for the highways sector. Airport modernization experienced this dynamic to a lesser extent as the five airports stipulated for restructuring were mainly selected based on adequate demand. Regardless, (worldwide) there are no penalties ascribed to either the public agency commissioning the study or the private agency, for constructing unrealistic projections, despite its implications for project delays resulting in cost escalations [ibid].

### ***5.2.3 Public Procurement of Services of Private Concessionaire: Buying Investment***

Chapter 03 lays out the legal ambiguity in the regulation of public procurement. Public procurement constitutes 30% of the total GDP. Despite the significance of transactions through procurement, a maze of flexible guidelines, regulations and rules govern the process [The Hindu, 2019<sup>56</sup>]. In 2012, the then-National government, led by the United Progressive Alliance, introduced the Public Procurement Bill in the Lok Sabha (the lower house) in order to ensure 'transparency, accountability and probity in the procurement process'. This has remained unpassed till date. Furthermore, Article 282 of the Constitution of India makes provisions for financial autonomy in public spending at national and state government levels. However, this is unaccompanied by legal provisions for public procurement, grievance redressal or dispute resolution. Regardless of the sector, airports or highways, this sustained ambivalence produces several grey areas of interaction between the elected representatives, administrative officials and private parties.

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<sup>56</sup> June 17, 2019

Within the flexibly defined norms, the obligatory two-stage process Request for Qualification (RFQ) and Request for Proposals (RFP) involves defining firm qualification criteria, stages of procurement, identifying experts for evaluation of bids and the selection process itself. Earlier this chapter discussed how MoF-DEA's guidelines for public procurement attempted to reduce the absence of its central and state-level legislation. Despite being well-intentioned, this approach made the procurement process susceptible to numerous, often opportunistic interpretations [Haldea, 2010]. Interviews reveal how opportunism and collusion is pervasive among the administrative State, private parties and political agents.

Semi-autonomous public authorities such as NHAI/AAI navigate a complex set of power relations involving central ministries and private corporations while facilitating the selection of the preferred bidder. The converse is also true, as heterogeneous firms aggressively jostle with one another as well as with administrators and politicians at national, state and local levels, depending on leverage, to in order to capture markets. The management of public procurement for PPP projects treads a sensitive ground characterised by intense informal negotiations that occur behind the curtain of official meetings, among public authorities and private firms [interviews, 2015-6], often with grey areas and disputes escalated to litigation [ibid].

#### ***5.2.4 Affirming Partnership through Special Purpose Vehicle: Ring-fencing***

Mismatched State-market institutional interests in a PPP project are affirmed through the Special Purpose Vehicle (SPV). Constituted under Section 25 of the Companies Act India, 2013, its governance is structured on shareholding arrangements between public and private transacting parties. The law recognises such SPVs as ring-fenced, secure entities. They are by law, free of restrictions applicable to government companies [Haldea, 2017]. Within a ring-fenced arrangement, legislation backing the functioning of SPVs enables greater flexibility for the public sector to augment private sector participation in its shareholding arrangements (in comparison to shareholding arrangements prescribed for Public Sector Units) [ibid].

In this context, two perspectives are significant. On the one hand, some critics within the government argue that in a PPP-SPV, the government's representation is merely customary [Haldea, Times Of India, 2018<sup>57</sup>]. The Secretary of a central government department is generally assigned the position of chairperson, whereas the Managing Director, with executive powers, is generally from the private sector [websites, SPVs]<sup>58</sup>. The other view from state government officials however refutes this argument. My fieldwork shows that distribution of power and risks here is not as straightforward. Power allocation and sharing is often contingent upon political relationships between the central and state governments, the systemic strength of institutions managing the project and their bargaining capacities [interviews, 2017-18]. Fundamentally, the SPV as a shareholder model where veto power rests with a limited few, as opposed to a stakeholder model with wider base, poses larger concerns.

There are inherent contradictions. The public shareholder in a SPV arrangement may also play the role of the grantor. This implies conflict of interest, as the public agency is the regulator, the facilitator and partner to the private party. A bounded arrangement is aimed at building a financially secure risk-free environment. However, internal decision making and veto powers in an SPV are strongly influenced by political relations. Governance within the PPP-SPV thus often translates into weakly coordinated actions of actors. Laden with differing values, their transactions at multiple spatial scales often translate into unclearly defined decision-making spaces with opacity in accountability. The SPV embodies blurred boundaries of institutional roles in hybrid institutions, here at the cost of transparent and just transactions.

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<sup>57</sup> 12 October 2018

<sup>58</sup> See Bengaluru International Airport Ltd, Shamshabad International Airport Ltd.

### **5.2.5 Contracts: Negotiation, Guarantee and Protection**

Contracts are not a static statute, but rather, as any regulation, signify an evolutionary process [Srinivas, 2012: 49]. They are integral to organisation of relations between State and non-State actors [Raco and Savini, 2019: 259]. Moreover, as Raco and Savini observe, 'A contract is never like another contract' [ibid: 53]. Contracts are plural in their form, driving different forms of consensus. PPP contracts represent different forms of alliances and distribution of risks between the State and PPP markets at a particular point in time. The *Concession Agreement* signed between the grantor and the concessionaire represents exchange and negotiation between the heterogeneous set of State actors and a multitude of firms of various scales and types. *The State Support Agreement (SSA)* reinforces the role of the State as a guarantor to its private partner, paradoxically, in order to sustain an environment of fair competition. The *Operations and Maintenance Agreement (OMA)* between the grantor and the operator entrusts the State with multiple roles – as a monitoring agency, it inspects performance of the concessionaire, and as a provider to citizens, it maintains control over pricing and safeguards users.

In the case of airports under AERA's regulatory regime, interviews reveal that, generally speaking, contractual terms are pre-negotiated and fixed for the entire period of the contract. Highway contracts entail greater degrees of adaptations and customisation, resulting in relatively more frequent renegotiations [multiple interviews (6), senior project managers (8), 2015]. As urbanists and planners have examined in the case of concession agreements in The Netherlands, flexibility typifies contracts where stakeholders manoeuvre conditions while delivering accountability in negotiated ways [van den Hurk and Tasan-Kok, 2020]. Hybrid governance thus enhances agility while questioning accountability in interactions between transacting parties in a PPP. PPP contracts as negotiated spaces are discussed later in this chapter.

### **5.2.6 Scrutiny and Quality Monitoring: Auditing by Independent Regulatory Authorities**

Partnering agencies are subject to financial scrutiny and quality monitoring through external agents. Three types of institutions are discussed here: The Comptroller Auditor General (CAG) in charge of investigation, the Airports Economic Regulatory Authority (AERA) in charge of setting performance standards and the Independent Engineer (IE) in charge of monitoring quality. While the former two are independent regulatory authorities created through constitutional provisions, the latter is generally a private firm or a State-Owned Enterprise (SOE), appointed jointly by the grantor and the concessionaire.

Overall, the CAG, an independent regulator established at the national government level is empowered to investigate all transactions occurring between public and private parties at all stages of the contracting process. The role of CAG evokes three types of sentiments among government officials and staff. One, that the CAG as an independent entity defines transparency required of organisations it monitors [Haldea, 2017]. However, while it scrutinizes transactions of all other public organisations, its own actions are opaque, enhancing degrees of institutional imperviousness. Two, rather than function strategically to curb the mismanagement of public money, it functions merely as a routine auditor [ibid]. Three, the CAG scrutinizes deviations from contracts entirely on technical assessments. Thus, with regard to this third assessment, the CAG not only fails to recognise (process-centric or technical) innovations, but also penalises earnest decision-making [interview, Executive Director, state government agency, 2017]. As a result, scrutiny dissuades bureaucrats from taking risks to support innovation. Given the flexibility and ambiguity in rule-making in a reformed State, some SPVs (metro rail corporations) may even remain exempt from CAG's monitoring, giving them greater autonomy than others [Haldea, 2017]. Researchers have argued how institutional evolution here reflects changes in the political realm. The CAG's functions have transitioned from expenditure audits to value-for-money audits of large investments in infrastructure, all at the cost of exclusion of social audits [Das, 2005: 129].

*Performance standards in Airport PPP projects* are defined by the Airports Authority of India (AAI) and Airports Economic Regulatory Authority (AERA), in partnership with private consortia. I interviewed



senior private sector managers of airport SPVs, who strongly stressed the benefits of an organisation such as the AERA, which is shielded from day-to-day interventions from third-party political agents, for effective contract execution. As an independent regulatory authority, AERA provides significant stability to governance of PPP led airports [senior officials, SPV, 2019-20]. It offers predictability to transacting parties through its role by pre-determining performance standards, pricing strategy, revenue share arrangements, monitoring investments, costs, revenue and project operations. The AERA, state government officials explained, in fact enables stronger bargaining powers and efficiency for the State. Both parties view its distance from everyday politics as an advantage. However, as critics of regulatory institutions have argued, whereas the separation from day-to-day political interference safeguards the authority from political opportunism, its opaque regulatory framing, particularly on financial matters, reduces visibility on its internal decisions that impact the user of the airport, tax payer and the public.

An *Independent Engineer* (IE) monitors performance in both sectors. Under the aegis of the grantor at the national level (generally, NHA, AAI) and corresponding departments at the state government level, contracts make provisions for independent project quality monitoring [see sample concession agreement, Annex I]. The grantor is thus required to appoint an 'independent' inspector to monitor the progress of the project. An Independent Engineer (IE) is empowered to approve quality as well as financial implications of any changes in contractual scope introduced by the grantor. Curiously, the remuneration and expenses of the IE are shared by both parties, bringing into question the actual level of independence entrusted to the IE [Interview, IE staff, 2015]. The appointment of a private party as IE creates opportunities for it to assume the authoritative role of a public authority entrusted with monitoring process, quality and performance. At the same time, it provides avenues for the grantor to hedge responsibility. As a private firm, the IE also gains benefits of early access to information on proposed government policy interventions and projects, all of which imposes obstacles to fair competition.

The administrative State's dilemma is rife with diverging roles, including a navigator of demand, a regulator of project terms, a promotor of political vision, a buyer of (concessionaire's) services, an agency that strikes a hard bargain with private markets while also serving as their guarantor, an auditor of quality and a partner to the market. Following the trajectory of the overall project cycle, at the initial stage of demand creation, efforts of an overdrawn and innovative State to attract the private sector through events/roadshows has no guaranteed outcomes. At the start of PPPs, the feasibility study translates into a speculative game of demand estimate and financial returns, which the political and administrative agents and their private consultants wilfully engage in in order to prove financial viability of projects. Consolidation of State-firm relations in a SPV is geared to efficiency, yet it is primarily characterised by uncoordinated decisions between partners with divergent goals, fenced in by opaque governance processes. Contracts are flexible in order to accommodate public-private logic, yet renegotiations are transparent only up to a certain extent. The nature of regulatory institutions charged with investigation exacerbates opacity in the airports sector while impeding transparency in access to markets for the private sector. Cumulatively, new organisational structures geared to achieve efficiency in outputs bring to question wider access and outcomes. Contractual arrangements further structure these hybrid relationships and are discussed below specifically.

### **5.3 Negotiated Contracts**

Research on the regulatory State also focuses on new public contracting [Yeatman 1995, cited in Raco, 2014: 179], where contracts tend to replace broader legal frameworks [Raco, 2010]. Critics have argued that contracts entail expensive employment of experts, lawyers and consultants [Raco, 2014: 179], akin to elite spaces that rescaling processes engendered through macro level policies. Theorists have critiqued public contracts as rigid, supporting risk averseness of public agents [Moszoro and Spiller and Stolorz, 2014], or contractual governance in mega-projects as tools of opaque decisions [Raco, 2014; Hilyard, 2016]. As a counterpoint, others have contended that related traditional arguments on loss of

public accountability need to be deconstructed [Tasan-Kok, van den Hurk, Özogul and Bittencourt, 2019]. Through extensive studies of municipal contracts in urban regeneration in The Netherlands, they argue that accountability in contractual governance exists in multiple forms through a flexibly negotiated governance between public and private actors. This section draws on this body of critique in order to view PPP contracts in India for highways and airports through a negotiated lens.

The unsettled nature of the relationships between State agencies and private firms in a PPP is discussed through an analysis of three contracts - the Concession Agreement, the State Support Agreement and the Operations and Maintenance Agreement in order to understand the multiple roles transacting parties assume (as analysed above in Contracts: Negotiation).

### **5.3.1 State-Led Concession Agreement**

The concession agreement is at the core of all contracts in a PPP. Foremost, the State seeks to balance the contributions of the public and private sectors to ensure public service obligations are economically completed. A key strategy the contract incorporates to achieve this is allocation of risks between contracting parties. On principle, the State mandates the private party to bear majority of the investment and risks. This includes establishing several strategies, including ensuring all equity commitments from the concessionaire, performance criteria, technical standards, conditions of completion and payment conditions between transacting parties. Normatively, this must include a clear pricing strategy and revenue share arrangements, among other parameters. However, in reality these vary by sector and project in the Indian context.

#### Equity Commitments: Firm or State?

A key aspect is equity commitments from the concessionaire at the start of the project and at key stages. The CA requires that before the commencement of the project, the concessionaire must make capital payments in a concession fee. While the project structure and contract prescribe the debt to equity arrangements, these are often renegotiated through the course of project implementation. By norms, the authority should offer no warranties. The feasibility studies determine user demand, based on which return on investments for the concessionaire is defined. The issue is that estimates made by transport and financial experts are often over-ambitious or idealistic. Total project cost, capacity of the asset to generate revenue, user charges levied by the concessionaire, property valuation/depreciation, operation and maintenance costs of the asset are all estimates made for the best-case scenario at the time of feasibility studies [Flyvbjerg et al, 2003]. In reality, user demand is contingent upon several social, economic and political factors [interview, senior manager, airport and national highways SPVs, 2017].

Given this uncertainty, in practice the gap between the estimated user demand and actual demand determines the State's support in Viability Gap Funding to the concessionaire, subject to market-based inconsistencies on accomplishment of traffic volumes for national highways. These are mediated through dedicated funds (such as the dedicated State-owned Fund India Infrastructure Finance Corporation Limited (IIFCL)) or loans the grantor and state government counterparts take to offset the funding gap, transferring a substantial financial burden onto the State. Equity commitments from the public and private parties are thus contractually open to renegotiation. My interviews revealed that the public agent supports its private partner to maintain relations and accomplish its targets, as critics of rigid contracts have argued [van den Hurk and Tasan-Kok, 2020].

#### Auditor-Auditee Relationship

The Independent Engineer, a competitor to the concessionaire, plays an important role in according completion certificates. The incongruity in the role of the IE, a private consultant evaluating the delivery of another private consultant was discussed earlier. Contracts thus embed intricate relations of contradiction between auditors and auditees. Also, audit statements on quality of design, construction

and operation are not a straightforward execution of contractual conditions. These are generally contingent upon bargaining capacities of the concessionaire [WB, PPP, Road Concession Agreement], which are further subject to renegotiation, depending on sectoral technical prerogatives and national-regional and local political claims to rents. For both sectors, interviews reveal that construction drawings for design, with detailed material specifications are not necessarily included in the agreement, inducing ambiguity on total project costs estimated in the feasibility study. During execution, sub-contracting agreements between the concessionaire and sub-contractors may thus result in inextricable locking in of obligations and risks with the concessionaire, impeding quality and costs [see also Raco, 2014].

#### Third-Party Claims to Property Rights

Terms of fair transaction, such as grants of property rights, are clarified in the contract, including the extent of third-party claims to property assets. Conditions for third-party access to claims generally depend on comprehensive legislation at the national level. Absent a central or state-level PPP law, third-party intervention often translates into opportunistic expropriation, for both national highways and airports. This implies that the establishment of internal checks and balances is often subject to discretion of the autonomous authorities, as Levy and Spiller have argued on public contracting [Levy and Spiller, 1994] and is generally guided by sensitivities of political-business alliances.

Chapter 06 discusses these anomalous circumstances through specific cases of dispute.

#### **5.3.2 Firm-led State Support Agreement**

The State Support Agreement (SSA)<sup>59</sup> is a strategic firm-led contract between the concessionaire and sub-national government agencies, i.e., the state government(s) (and in some cases, the local government). The extent of demand from the State is a reflection of the firm's ex-ante bargaining capacity. As theorists have observed, multi-national firms exert greater leverage. First, the SSA imposes on the state government, the responsibility of providing unencumbered land for development of infrastructure and allied functions. Second, it protects targeted revenue returns for the Special Purpose Vehicle by preventing establishment of any other competing facility in its spatial vicinity<sup>60</sup>. Third, it makes provisions for the State's equity contributions. The SSA is viewed differently by government officials. Aligned with innovation theorists on traits of a risk-taking State, some officials from states with greater capacity to manage funds for their development needs believe that it is the responsibility of the government to extend support to the private sector, provided returns are estimated prudently. At the same time, the same officials also opine that the central government often instrumentalizes the state government through the SSA to ascertain land and funding, the two key prerequisites to PPPs.

#### **5.3.3 Mutual Accountabilities in Operations and Maintenance Contract**

In an O&M contract between the granting agency and the operator, the latter is required to operate the facility, collect user fees, maintain and upgrade the facility. In a PPP project, under the Build Operate Transfer model, the O&M contract is typically bundled with the Concession Agreement and spans long periods of the PPP project tenure (10-20 years). Bundling the two contracts makes management easier for the public sector but compounds risks for the private investor [interview, 2018]. Several factors that increase a private investor's risks, of which user fees is an important parameter, are discussed here.

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<sup>59</sup> See SSA, Modernization and Restructuring of Delhi Airport

<sup>60</sup> To expand on this context, 'contracts', including special forms of contract (for development of infrastructure), fall under the Concurrent List [Concurrent List or List-III (Seventh Schedule)]. This provision empowers the national and state governments to formulate, enforce laws and regulations, both at the national and state levels. Given this context of semi-autonomy at the state level, state governments are free to conceive infrastructure projects, explore partnerships with other government agencies and the private sector for financing and developing infrastructure.

### *User Fees*

National Highway project segments undertaken on PPP mode often confront lower than estimated traffic volumes. To meet revenue gaps, renegotiations on user fees and revenue share are recurrent with highways [interviews, managers, SPV, 2016-17]. The Model Concession Agreement itself makes provisions for negotiations on extending the contract, in case of unrealized traffic volumes. These open up channels for manipulative behaviour by the concessionaire [ibid, 2018] to report incorrect data on traffic volumes or manufacture contingencies, such as insolvency. The result often is project delays, cost escalations and financial risks [ibid].

For airports, prior to establishment of AERA, user fees were determined through complex negotiations between the concessionaire, oil companies and airlines (Bengaluru, Hyderabad) [interviews, SPV managers, 2020]. Under the aegis of AERA, a precise mechanism for determination of user fee is specified. This aids the concessionaire to estimate revenues and plan loan repayment to lending agencies while ensuring project viability. While this arrangement appears to compromise the grantor's interests, a hybrid revenue-share model (the Hybrid Till model), which the AERA introduced, safeguards proportionate returns for the public party.

Increasing user fees is a political and administrative decision [Pratap, V.K., 2015]. Such a move may cause social unrest and impact voter behaviour. It also means deviating from a State-controlled, normative approach to a demand-based pricing strategy. To retain private sector interest as well as meet public targets, the O&M contract provides incentives for increasing efficiency or improved collection of user charges. However, national highways, performance incentives are numerous and rigid [interviews, expressway operator, 2016]. In the case of airports, conditions are often fixed at the time of contract confirmation. Negotiations are seldom possible [interview, senior officer, SPV, 2020].

### *Mutual Accountabilities*

While performance measures are set for the concessionaire, in practice these are contingent upon mutual accomplishment of obligations. This may be likened to contracts for urban regeneration projects in The Netherlands, which include 'accountability duties' that serve as benchmarks for measuring private sector performance. Accountabilities in a PPP are however a shift in paradigm from the commonly agreed norms of municipal governance that are not contingent on negotiation [Tasan-Kok, et al, 2019].

Often, incomplete concession agreement results in unmet obligations from the grantor or the concessionaire (making unencumbered land available, changes to design, delays, project cost escalations, etc.). Unmet obligations eventually impose a risk burden on the state government forming SSA with the concessionaire. It also hinders performance targets for the operator [interview with private party representative]. There may be other liabilities facing the O&M contractor, such as condition of assets, inadequate quality of equipment, environmental conditions, changes in regulatory requirements and political interventions [Tirole, 2009; Bajari and Tadelis, 2001]. Unforeseen contingencies such as late-term changes and design variations are a major source of disputes in contractual relationships (Bajari and Tadelis, 2001). The grantor may impose penalties on the O&M contractor. These may include fixed fees, a performance-based fee and damages for failure to achieve performance parameters. Generally, monetary penalties are levied as a percentage (2-3%) of 'Daily Gross Toll revenue' collected [WB, PPP, Road Concession Agreement]. However, these are equally contested by the operator. Often the operator may sub-contract the operations component, making enforcement of fiscal discipline a difficult task [WB, PPP Overview].

To reduce its own risks, the private operator, especially in a national highway project, periodically renegotiates several clauses of the contract including levy of user fees, change of shareholding or termination of contract, which often leads to disputes and may need resolution through arbitration or litigation.

Overall, contractual governance for PPPs in the airports and national highway sectors in India is a negotiated process where the State's role oscillates between a regulator, a facilitator and a partner, alluding to custodianship of public interest. Reliance on technical expertise and regulatory interpretation as a key parameter of decision-making translates into negotiated decisions at the project level. Chapter 06 delves into a deeper investigation on such relationships.

#### **5.4 Conclusion: Varieties of States, Firms and their Relationships**

Returning to the specific research question of how the multiple transacting parties in a PPP interact with regulatory processes to shape their economic organisation in a project cycle, my fieldwork reveals conflictual and cooperative relationships between the State and the firm, defined through ambivalent legal contexts and multiple markets. The key issue was regarding how institutional arrangements produce and distribute risks while monitoring accountability towards socially relevant outcomes.

The first exploration on relationships between State agencies through the PPP Cell's PPP guidelines shows a strongly centralised process, mostly vested with the central government, although through a flexibly designed guidelines. The Planning Commission's idealistic norms for fair procurement, project execution and model agreements developed in a silo led to weak acceptance and ownership by the concerned national-level ministries. State governments bear significant degrees of responsibilities, as well as social and financial risks which remain unaddressed in the guidelines. Intriguingly, the national level guidelines, to retain trust, allocate no specific accountabilities to the private investor. Largely a situation of dependency on the private sector, rather than partnership emerges through the analysis of guidelines. While the State expanded participation of private firms in policy debates, firms' were selectively invited to decisions through the central government's discretion, as opposed to systemic procedures that solicited partnerships for innovation. This continued pro-business approach led to the crafting of incomplete guidelines in institutional arrangements, which led to an absence of clarity in intra-State, inter-firm and State-firm relationships through a systemic set of procedures and protocols.

The second exploration on the relationship between firms shows aggressive competition and cooperation to create the project cycle and stay in the PPP market that firms themselves co-created with the State. While diversification and innovation were strategically important in guiding organisation of firms, opportunism and oligopolistic configurations supported mainly by risk hedging, and to a lesser extent by risk pooling, primarily define contractual arrangements.

The third investigation on the relationship between the State and private sector in a PPP project cycle reinforces the theory of the rise of the hybrid organisation. State-firm relationships show they are not intrinsically opposed to each other. Rather, their relationships are contingent on varying contextual forces emerging from national-state government relations and the bargaining capacity of actors. The nature of conflicts or collaborations vary along the phase in the project cycle and the clarity of contractual agreements. The design of the overall project cycle yields some visibility on expected outputs and almost no guarantees on outcomes. The overall project cycle is appropriated as a business, fiscal or political instrument by the private party and political and administrative agents to suit their own goals. Uncoordinated decisions occur within opaque governance systems. Flexibility in contracts permit negotiation on most decisions, including accountabilities. The State plays different roles throughout the project cycle: a negotiator, a guarantor to its private partner, a regulator and a custodian of the user.

To summarise, what emerges is a State deeply entrenched with the private firm in PPP markets. The State and the firm use one another in an instrumental manner rather than conceptualising relationships that foster wider access to socially oriented innovation. For the private sector, comprising highly diversified competencies, the heterogeneous State is their guaranteed, risk-free market. Firms form oligopolistic relations to sustain their spaces in the market and remain active in a process co-created by both institutions. In this circumstance, despite its dilemma, the State becomes integral to firm oligopolies, as both actors play along to perpetuate their roles in the PPP game. The State's (central and state) continued financial guarantees to maintain this relationship of trust or dependency with its private partner exacerbates its own risks and societal ones.

Chapter 06 deepens this discussion on relationships between the State and the firm through an analysis of the behaviour of transacting parties at each stage of the project cycle. It discusses uncertainty and incomplete contracts to gain depth on 'State-firm' relationships at the level of specific stages of the project cycle. Through a study of disputes the chapter examines micro-project level relationships between all stakeholders in granular detail.