Executive Summary - Primer on Project Development Funds

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The PPPRC section on Product Development Funds (PDFs) will be periodically updated to continuously identify lessons learned and success factors that influence the design and operationalization of PDFs. Let us know what you think by taking a Quick Survey.

Executive Summary

Project development funds (PDFs) are dedicated vehicles that governments establish to systematically support the preparation of public-private partnerships (PPPs). The lack of adequate and consolidated resources to appropriately evaluate and prepare potential PPP projects is a key constraint faced by many PPP programs, and inhibits the ability of PPP projects to raise private investment. PDFs are generally established to address this challenge, by providing dedicated and centralized funding for PPP project preparation that is not subject to the constraints of typical government budgeting processes. Moreover, they often go beyond the provision of funding to address a range of challenges that can undermine the provision of high-quality and efficient PPP project preparation. By driving a cultural shift to encourage a greater consideration of PPPs, PDFs also serve as tools that can support overall government policy for, and signal political commitment to, the use of PPPs.

PDFs have contributed to the successful implementation of PPP projects, which can serve to support the increased private investment that will be critical if the United Nations Sustainable Development Goals (SDGs) are to be achieved. PDFs have directed significant funding to the preparation of PPP projects and contributed strongly to PPP projects reaching financial close and implementation. They have also supported the building of critical PPP capacity within governments and driven private sector confidence in PPP programs. These impacts help to increase private investment in infrastructure, a critical source of finance to support the achievement of the US$2 trillion to US$3 trillion of investment per year estimated to be necessary to achieve the SDGs. Although PDFs are not a panacea—they must be supported by a conducive PPP enabling environment and are often accompanied by other reforms—they can support the transmission of infrastructure development good practices. However, PDFs require deliberate design and management to be successful, and a wide range of issues—from legal status and governance to sustainability—need to be considered prior to their implementation.

This primer on project development funds (hereafter, “Primer”) seeks to capture and distill lessons for public sector and other PPP practitioners related to how and why PDFs are established, and how best to enable them to contribute to the success of PPP programs. Through its review of PDF and other relevant experience, this Primer seeks to identify lessons learned and success factors that influence the design and operationalization of PDFs. It aims to paint a clear picture of how and why PDFs can support the development of PPP programs to assist policy makers in understanding whether a PDF can help to address their particular PPP program challenges. Where practitioners are developing a PDF, this Primer provides detailed information on PDF design features to assist them in establishing a PDF that will deliver on its objectives.

PDF Design Findings

There is no one “right” PDF design, only a PDF design that best supports project preparation in a particular jurisdiction. PDFs take a wide range of forms, whether an independent legal entity with complex revolving features intended to support a large number of projects, a much simpler separate line item in the budget, or anything in between. Ultimately, they are tools and must be designed to work within an existing environment for existing users. Their effectiveness therefore depends on how well they address the project preparation challenges facing PPPs in a specific country. Despite the fact that PDF design is necessarily contextual, there are clear lessons that may be useful to practitioners to develop effective PDFs. Key questions that should be addressed when considering, designing or implementing a PDF are captured in the figure below, along with a reference to where they are covered in the Primer. This is followed by a summary of key findings by topic.

Figure 1: PDF Design Checklist

Topic	**Read more in Primer section**
PDF Motivations and Experience	
What is the rationale for the establishment of a PDF and what are its key objectives?	2.1
Are there preconditions to the establishment of a PDF?	2.2
PDF Design: Structure	
What legal instruments are appropriate for the establishment of a PDF?	3.1
How can a PDF’s legal structure support its effectiveness?	3.1
Where should a PDF be situated within government?	3.2
What governance structure is appropriate for a PDF?	3.2
How (and by whom) should a PDF’s day to day operations be administered?	3.3
PDF Design: Funding	
What sources of funding should a PDF expect to access?	4.1
What level of funding is necessary to support PDF operation?	4.2
Should PDFs incorporate revolving features that may improve financial sustainability, and if so, how?	4.3

PDF Design: Project Selection

What users, projects and activities should be eligible for PDF support?	5.1
How advanced should projects be in order to access PDF support?	5.2
What other eligibility criteria may be considered to allocate PDF funding?	5.3
What project implementation arrangements can support the effective use of PDF funds?	5.4

PDF Operational Considerations

What considerations should be taken into account when staffing a PDF?	6.1
How can PDFs drive demand for their services?	6.2
What role should a PDF play in advisor procurement and management?	6.3
How do PDFs report on and monitor performance?	6.4

Designing an Effective PDF: Structure

PDFs function within and alongside the broader PPP enabling environment, which often underpins a PDF's structure. Although there are exceptions, PDFs are most often established as part of a country's PPP framework, and are enabled within PPP legislation. They are typically governed by an independent committee or board, whose composition resembles broader PPP governance structures thereby supporting alignment between the PDF and PPP policy. PDFs are generally located within an existing institution—generally the central agency responsible for the PPP program, which also commonly houses the PPP unit and is often responsible for PDF administration. This model provides a number of benefits, including allowing the PDF to leverage scarce capacity and existing relationships, create a "one-stop shop" for PPP program tools and support, and build traction and engagement between PPP units (armed with project preparation funding) and implementing agencies.

PDF legal structures vary considerably, but they are typically focused on enabling the functionality necessary to fund PPP advisory services. Effectively managing the high costs, long timeframes, and expertise requirements associated with PPP advisory services often requires functionality that may not be enabled under existing financial management or public procurement rules. PDFs are, in many cases, special purpose bank accounts, operated by governments to disburse funds for project preparation. The legal structure of a PDF is therefore often designed around ensuring the PDF bank account can function as required. This often,

but not always, requires the creation of a separate legal entity, depending on the specific needs of the PDF and the financial management policies of the country in which it operates.

Designing an Effective PDF: Funding

Although PDFs are more than just a funding source, a PDF's funding model is central to its ability to deliver on its objectives. PDFs are generally designed to address funding challenges; however, they must still raise funds in order to function, often from constrained sources. PDFs that have lofty ambitions, but insufficient funding, will fail to deliver. Determining how to fund a PDF requires making decisions on where the funding will be sourced, how much will be required both initially and over time, and whether the PDF will seek to operate on a self-sustaining basis.

Government contributions are by far the most common form of funding for PDFs, highlighting that PDFs do not often relieve governments of carrying the burden of PPP project preparation costs. The majority of PDFs are funded either entirely, or in large part, through government contributions. Development partners have provided extensive support for PPP project preparation, but the use of development partner funds to capitalize a PDF is relatively uncommon. Development partners have also financed programmatic project preparation through specific lending operations, which enables support for a country's PPP program, but does not directly capitalize a PDF. Private investment in PDFs is likely to remain limited in many PPP markets.

PDFs do not require large initial capitalization, and funding requirements are largely driven by the size of the PPP pipeline. The number of projects a PDF aims to support is a key driver of PDF funding requirements, because the majority of PDF costs are a function of project preparation costs. Although a large PPP program could require substantial capital, expected funding requirements do not need to be available at the time the PDF is established, and many countries have established successful PDFs with US$20 million or less. A smaller initial PDF size may be particularly appropriate for supporting less developed PPP programs to allow time to build capacity and experience. In all cases, political commitment is necessary to ensure sufficient funding allocations over the life of the PDF.

The use of revolving features can stretch scarce project preparation funds, but financial sustainability is elusive. The sustainability of a PDF, in particular the need for ongoing funding contributions, can be influenced by the use of revolving features, which enable the PDF to recover the costs of project preparation. Revolving features typically include success fees, which the private partner is obligated to pay upon successful closure of the project, and in some cases reimbursement requirements for unsuccessful projects. Although these revolving features can reduce the need for external funding to support the PDF's costs, they are unlikely to fully alleviate the need for government funding. In addition to supporting cost recovery, revolving features are expected to support increased focus on project success and ownership by implementing agencies. However, they can also undermine a PDF's attractiveness as a source of funds and can bias project selection against early-stage or more challenging projects. As a result, the use of such features should be carefully considered.

Designing an Effective PDF: Project Selection

The scope of a PDF, which guides overall project selection, is often inextricably linked with the overall PPP framework within a country. The range of projects and users that a PDF will support is often linked to the definition of a PPP and relevant institutions in a country's PPP framework. Most PDFs provide support across a wide range of infrastructure and social sectors, with a focus on public sector-driven PPP project preparation (although some PDFs support unsolicited proposals). A narrow mandate to support specific sectors or project types is not common, and may limit the PDF's flexibility.

The point at which a PDF engages in the project development process is a critical design decision. PDFs typically fund all aspects of PPP project preparation and transaction advisory required across the typical PPP

project cycle to structure and tender a viable project. However, PDFs must determine how “ready” or developed a project should be to access PDF support. Determining an appropriate point when projects can access the PDF within the PPP project cycle has important implications for the overall project preparation landscape within a country, as well as the funding requirements and sustainability of a PDF. Supporting projects in earlier stages of development can help to ensure sufficient demand for PDF support and avoid gaps in project development support, but may also lead to a higher number of projects supported by the PDF which are not ultimately implemented as PPPs.

PDF eligibility criteria tend to reflect project assessment criteria found within the PPP project approvals process. PDFs cannot support all PPP projects in a country, and applications for PDF support are generally reviewed on a rolling basis, with funding provided on a first-come, first-served basis. Eligibility criteria guide PDF funding decisions and tend to closely reflect the project assessment criteria used more broadly within the PPP project cycle. However, given the importance of implementing agencies in driving PPP project development, additional weight is often placed on evaluating their commitment to PPP project implementation to help allocate PDF funding to projects with a higher likelihood of success.

Key Issues in PDF Operationalization

Specialized skill sets are often required for the effective performance of PDF functions but can be hard to find. The role of a PDF strongly influences staffing requirements, with some PDFs serving only to allocate funding, and others engaging heavily in interacting with implementing agencies, and procuring and managing PPP advisors. This means that appropriate staffing levels and costs vary considerably across PDFs. Despite varied staffing levels, most PDFs will require technical experts who are well-versed in PPP policy and PPP frameworks, transaction requirements and contract structures, as well as procurement. The requisite skill sets are, however, often difficult to find in many countries. To address these challenges PDFs often leverage external resources, either through development partners or, less commonly, local development finance institutions (DFIs), to supplement internal capacity.

Ensuring demand for PDF support requires a focus on the needs of implementing agencies. A key challenge for many PDFs is receiving sufficient, suitable applications from implementing agencies. Overcoming this challenge requires addressing issues such as a lack of interest in PPPs, concerns about a loss of control over project development, and a lack of capacity to identify and assess PPP projects. PDFs should adopt a demand-led approach by thinking of implementing agencies as clients. A PDF’s services should be tailored to implementing agency needs, which should be continually assessed over the life of the PDF, both to attract new users and to stay relevant for those with increased PPP experience and capacity.

Procurement and management of PPP advisors are core functions for many PDFs. PDFs are seen to play a critical role in maintaining consistent and appropriate quality standards that support both PPP projects and the development of the local PPP advisory market. This often translates into supporting procurement and advisor management, including through the empanelment of advisors, to expedite the procurement process and help to ensure the quality of advisory support.

Key Lessons for Practitioners

The following lessons can help to guide practitioners as they consider the design and implementation of PDFs.

Figure 2: Summary of Key Lessons for Practitioners

1. Ensure that the PPP enabling environment is sufficiently well developed to support appropriate preparation and implementation of PPP projects.

The PPP framework is often a critical building block for PDF design, and it, and the broader PPP enabling environment, must be sufficiently developed if PPP projects are to be successfully implemented. Without a conducive environment, PDFs are unlikely to be able to grow the PPP program.

- Prior to developing a PDF, assess the PPP enabling environment, and identify key barriers to effective project preparation and implementation. Ensure key challenges are either addressed prior to or in parallel with PDF development or are otherwise reflected within PDF design.
- Where internal resources for addressing challenges are not sufficient, seek development partner support to assess and help address PPP project preparation and implementation challenges.

2. Determine a PDF’s role within the PPP project preparation landscape early in the PDF design process.

A PDF is only one part of the project preparation puzzle, which relies on and co-exists with other sources of support. PDF design is therefore strongly impacted by the specific role it is expected to play, as defined by its scope, the nature and volume of projects it is intended to support, how those projects are expected to be developed up to the point of PDF intervention, and the nature of PDF engagement in projects it supports. In particular, where sufficient funding is not available for upstream project identification and prioritization, PDFs may be unable to achieve their objectives.

- Assess the resources available across the entire project preparation landscape, including funding for upstream project development to ensure that a PDF’s design is consistent with the likely PPP project pipeline.
- Engage early with implementing agencies to identify project preparation challenges and design the PDF to reflect them.

3. Ensure PDF funding strategies are realistic and consistent with a PDF's broader goals.

PDFs are predominately funded by governments and therefore do not typically relieve governments of the burden of supporting the costs of PPP project preparation. Initial PDF funding strategies should generally focus on government funding as a main source. Small initial capitalization amounts are not uncommon. However, strong, continued political commitment will be necessary to drive the recurring or multi-year government funding allocations necessary to ensure a PDF is financially secure, because few PDFs are financially sustainable. PDFs that are not sufficiently funded over time are unable to meet their objectives.

- PDF funding strategies should generally focus on determining the government funding allocation that can be made available, both initially and over time. Other sources should only be included in funding strategies where there is clarity that they will materialize. In particular, PDF design should acknowledge the challenges and/or implications of financial sustainability objectives.
- Revolving features should be implemented where they are likely to support, or at least not undermine, a PDF’s ability to achieve its objectives. Care should be taken to design revolving features that do not unduly impact project viability or implementing agency interest.

4. Determine PDF structure based on how to best enable the functionality a PDF requires to achieve its objectives.

PDFs are not usually institutions, nor do they have a personality of their own. Rather, they are more often seen as tools that should, therefore, be shaped to meet the needs of their users. Consequently, a PDF's structure is only important to the extent that it provides the flexibility and functionality necessary to support successful PPP projects. How that functionality is translated into a formal PDF structure will vary considerably from one country to another, depending on local context.

Smaller economies and less developed PPP programs, in particular, may benefit from lighter PDF structures, which are less challenging to implement and which entail lower upfront resource commitments. PDF structures can then evolve to accommodate more sophisticated features or other PDF contributors as necessary.

- A PDF's structure should be dependent on local context and based on how best to deliver the PDF functionality required to enable the efficient delivery of high-quality project preparation. Key factors that should be well understood include public financial management and procurement requirements.
- PDF structure should be designed based on an assessment of project preparation challenges, PPP program needs, and funding sources available in the near to medium term, and the structure's effectiveness should be re-evaluated as conditions change.

5. Ensure PDFs are user-focused and able to evolve over time to maintain relevance.

PDFs provide a support service. Their ability to be successful depends entirely on how well that service is leveraged by implementing agencies. Where successful, PDFs can facilitate PPP program growth and increased experience with PPPs. As a result, the project preparation challenges experienced by implementing agencies, as well as the implementing agencies themselves, will change. These changes will in turn require a PDF's services to evolve alongside its users, and the PPP enabling environment, if they are to stay relevant.

Given this expectation, PDF design should recognize that PDF scope, structure and/or funding strategy may need to change to meet PPP program and implementing agency needs.

- Ensure that PDF design enables strong implementing agency project ownership.
- Allow sufficient flexibility within PDF design to enable PDF operations and offerings to evolve to meet changing challenges and requirements.
- Regularly review the PDF service offering and user requirements to lay the groundwork for necessary adaptations.

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