

Abstract

There is a global trend for local governments to engage in public-private partnerships (PPPs) to provide infrastructures and public services. Light rails, water systems, waste management, schools, sport centres, social housing, are just a few examples of sectors where the private sector is becoming more actively involved with local authorities. Most of these engagements are done through mixed companies and contractual concessions. Both suffer from a major shortcoming – renegotiations. Contracts are often renegotiated within few years after signature, and some evidence show that the results might not protect the public interest. This paper tries to understand how and why renegotiations of local concessions happen by looking at the specific characteristics of contracts (endogenous determinants). To illustrate the discussion, a case study from a light rail system is analysed, exemplifying the effect of a contractual renegotiation. The authors argue that contractual renegotiation can be useful in decreasing contract incompleteness, but a poor design of these clauses can allow for opportunistic behaviour by concessionaires.

Keywords: Concessions; renegotiations; public infrastructures; local government; light rail services.

Policy Implications

Renegotiations per se are not a problem. The process of adjusting the contract to new conditions unveiled over time can increase the welfare of both agents (private and public), as long as opportunistic behaviors are prevented. The problem arises when, under renegotiations, the advantages of the competitive bidding disappear. Defining rules for the renegotiation is in fact the most effective way to reduce, or to deal with the incomplete nature of contracts. Accounting for the high transaction costs of foreseeing all possible contingency can be a solution to define, *a priori*, the rules to manage renegotiations that are extremely likely to happen.