

Public-Private Partnership in the Road Sector: a study on the agreement between the essence of the contract object and the legal form of contracts in Brazil

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ABSTRACT: The Brazilian National Treasury, through Decree No. 614/06, established the Standards for the consolidation of public accounts applicable to PPP contracts, recommending the adoption of the essence over form criterion, focusing on the essence of the economic relationship between contracting parties. However, an analysis of the essence of the contractual purpose was considered necessary because, in the final analysis, it is the phenomenon that needs to be accounted for. The methodology consists of a descriptive, exploratory, bibliographic and documentary research. Primary and secondary data were collected with a view to their structure in four theme units, so as to analyze the context in which PPP contracts emerged in Brazil. Through this research, it could be identified that there is no agreement between the essence of the contractual purpose and the legal form of the PPP contracts in the creation of highway structures in Brazil. Both the terms of Law No. 11.079/04 and those of Decree No. 614/06 delimit the analysis of the contract's essence, inducing to the supremacy of formal aspects over essence in the analysis of the phenomenon that has to be accounted for.

Key words: Public-private partnership; contract; infrastructure; public accounting; highway.

Received in 30/06/2008; revised in 10/12/2008; accept in 18/03/2009.

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Editor's note: *This paper was accepted by Antonio Lopo Martinez.*

1. INTRODUÇÃO

The concentration of hundreds of millions of people in urban areas exerts great pressure on the national and local governments at the time of meeting the needs of their citizens. According to a research by UN-HABITAT, *United Nations Human Settlements Programme* (2006), 2007 will represent a crucial moment in history, as half of the world population will live in cities: The number of persons who dwell in urban centers around the world would climb from 49% to 62% of the world's population, in the course of the next 25 years. The research still projects that the average annual growth rate of the urban world population, in this interval, will be 1.78%, almost double the rate of growth of the total world population.

These projections generate questions with respect to the capacity of governments accompanying the changes and ensuring the economic development of their peoples, without incurring in socially unacceptable asymmetries.

In Latin America, according to the World Bank (2005, p. 9), public financing of infrastructure has declined significantly, especially due to fiscal adjustment and, this reduction has not been compensated by an increase in private financing. As a result, deficiencies of infrastructure, in terms of existence as well as quality have generated obstacles to growth and the struggle against poverty.

On the other hand, the infrastructure deficiencies, particularly of roads, ports and the network of logistic terminals impair productivity in Latin American: logistic costs in the region represent between 20% and 30% of the value of products against a rate of 9% in OECD countries, Organization for Economic Co-operation and Development (*Ibid.*, p. 10).

In this discussion, Davezies and Prud'homme (1996, p. 57) qualify as "generally impossible" the fact of attracting private operators in investments in public infrastructure for profitability and risk reasons. They affirm that "strict profitability in general is low, and these reduced rates are almost always caused by unforeseen events".

Thus, Public-Private Partnerships (PPPs) have emerged in the world as an alternative to encourage private participation in public investments. In Brazil, the discussion of their implementation has generated questions with respect to transparency of these contracts, the guarantees offered by the government and the accounting treatment of public expenditure. Among them:

The contractual commitments assumed by the State in the PPPs may, in the light of budget principles, depend on the structure adopted for the project and be classified as current or not expenses, continued or not, capital expenditure or credit operations [...] (MEYER and ENEI, 2004, p. 1).

Therefore, the structure of the PPP contract would not only be important to reach transparency of processes and a clear delimitation of the rights and obligations of the parties, but also to characterize the essence of the phenomenon to be accounted for: the contractual purpose.

The accounting rule issued for PPP contracts commends the adoption of the criterion of "essence over form", as a focus of the essence of the economic relationship by the contracting parties. However, one notices the relevance of characterizing the essence of the contractual purpose and assessing, on this basis, the legal and accounting structure already established for PPP contracts.

Thus, considering the importance of highway infrastructure to the economy of countries, the goal of this research is: to identify if there is agreement between the essence of

the contractual purpose and the legal form of Public-Private partnership agreements in the creation of highway infrastructures in Brazil.

2. THEORETICAL REFERENTIAL

Traditionally, the provision of public services has been recognized as a natural monopoly of the public administration, but the latter has gone through a series of reforms, aimed at “[...] introducing, in public organizations a culture of flexibility and entrepreneurial management, which permits them to act quickly and efficiently, in a world of fast transformations” (GUIMARÃES, 2000, p.1).

Spink (1997) conducted a descriptive study of the administrative reforms in Latin America in the past seventy years.

The author did not limit his research to a description of what was done to reform the public administration, but brought to the discussion the content in which measures were implemented. This permitted to better understand the nature of reforms, by being seen as answers to the specific needs of its time.

Particularly in Brazil, a reform was started in 1995 to substitute the bureaucratic public administration by the management one, based on principles of new public management.

By dealing with the reforms which aim at reaching efficiency in the provision of services, both in Brazil and abroad, they make explicit: (1) the need to delimit the area of performance of AP, getting into the discussion the terms of reduction, decentralization, transfer of activities, external contracting, among others; and (2) the influence of the private sector in the reforms implemented. The Master Plan of Management Reform in Brazil is an example of this last point.

Brazil has crossed a *continuum* of reforms, which aimed at meeting public needs and interests efficiently. In line with this, the notion of public service also changed.

Modesto (2005, p. 460) clarifies this by affirming that the legal nature of an activity is not subordinated to the quality of the subject who performs it.

In turn, the Constitution (BRAZIL, 1988), in Article 175, established: It is up to the public power, in accordance with the law, directly or under the concession or permission regime, always through bidding, to provide public services.

It is thus understood that the Brazilian rule agrees with the notion that in the final analysis, “[...] public service is materialized always in the provisions made in favor of users” (VOLPE, 2005, p. 4), even though offered by a private or third sector entity, and with different degrees of intervention or autonomy.

Apart from the theoretical discussion, the demand for public services is growing and the answer of governments in general terms proves insufficient to meet this demand, in particular when services require infrastructure.

The solution for the infrastructure problems is a necessary condition for all to have access to basic services such as electricity, communications, urban transportation and sanitation (BRASIL, 2006a).

The IMF, International Monetary Fund (2005), in a research conducted in eight countries, including Brazil, concluded that the options of politics and the margins to increase public expenditure of capital in infrastructure by flexibilization of the fiscal balance are limited, especially in countries with high level of public debt and vulnerability anti macroeconomic shocks.

The research also revealed that countries are using the PPPs to promote greater investment in the sector through participation by the private sector in the supply of

infrastructure assets and services, and that these have offered efficiency gains in these activities. However, the literature also presents criticisms, to the effect that:

“[...] innumerable experiences [...] show the successes and errors in projects of this type, but their implementation is always slow. [...] in England, it was three years between the idea and the first partnership project, and even so there are risks of retrocession; in Portugal [...] the PPPs went wrong, they exploded the public budget and had to be suspended” (LEITÃO, 2004, p. 1).

To count on a theoretical referential, which enables better understanding of the particularities of PPPs contracts in Brazil, the concepts found in the literature were analyzed. They outline some of the characteristics of this type of partnership with respect to:

- The contractual purpose, as one considers that the government busy services and not a physical asset, as in a conventional contract (BENTZ *et al.*, 2004, p.3);
- The regulation is “creatively” differentiated aiming at a higher added value in the provision of services (KPMG, 2002), an aspect linked to the allocation of risks;
- The responsibility of the public entity for compensation (RUBIO, 2003, p. 3-4);
- The control exercised on the private partner through performance indicators in the provision of the service, not of physical-financial control of the work (BRITO and SILVEIRA, 2005, p. 8-9).

Cretella Neto (2005, p. 1) ratifies that in a PPP contract, the public administration performs control and inspection actions, highlighting however these actions as resulting from a legal relationship¹ established in the execution of a contract, which is the instrument which beyond bestowing legality on the relationship by the parties, defines the terms that will govern it.

According to Moreira Neto (1997, p. 75-76):

“[...] the word partnership, from Latin *partarius*, participant, has been used traditionally in law to designate a *sui generis* type of company where the composition of capital stock nor the institution of a new person occur, but, only, a business relationship, where one of the parties assumes certain obligations with view to participation in profits made.”

However, in the national scope, the Law of PPPs (BRAZIL, 2004a, Art. 2) in its chapter IV, regulates the SPE, Specific Purpose Company, which shall be constituted before the execution of the contract to implement and manage the purpose of the partnership (*Ibid.*, Article 9).

Thus, the term partnership, in light of the Law of PPPs in Brazil, has come to break with the “traditional use” of the term by encompassing in its concept the creation of a new legal entity.

To reinforce the notion of PPP, one considered timely its comparison to other forms of partnership practiced by the public administration with the private sector. Table 1 was prepared based on the classification made by Di Pietro (2005):

One observes that the PPP forms the same category with the common concession, authorization and permission. Due to the concession being an institution that covers PPPs contracts and needs to be differentiated, this institution shall be presented in its doctrinaire terms, since, as Wald teaches (1996, p. 56), they permit, “knowledge of the implicit premises that are particular to them”.

Delegation of Services	Private collaboration in the performance of medium-activities of the Administration	Associated management of Public or Public Utility Services
- Common Concession - PPP - Authorization - Permission	- Outsourcing	- Conventions -Management Contracts

Table 1 – Modes of partnership in function of the type of administrative activities

SOURCE: DI PIETRO, 2005, p. 54 – 59

As far as the doctrine is concerned, concession is an act through which the public power grants, to a natural person or company, the right to exploit in its name and on its own account, by certain compulsory charges, certain economic activities of economic interest and public utility for a period of time.

Concessions in Brazil are regulated by Law No. 8.987/95 (BRAZIL, 1995a) and by Law No. 9.074/95 (BRAZIL, 1995b), which deal with two types of concessions (in addition to the permissions). One of them is the public service concession, i.e.: “[...] the delegation of its provision made by the licensing power, by bid, in the competition mode, to the legal entity or consortium of companies, which demonstrate capacity for their performance, on account and risk and for a definite period” (BRAZIL, 1995a, Article 2, item II).

The second, the public service concession preceded by the execution of a public work is:

“[...] the construction, total or partial, conservation, reform, expansion or improvement of any works of public interest, delegated by the licensing power, by bid, in the competition mode, to the legal entity or consortium of companies, which demonstrate capacity for its performance, on its account and risk, so that the investment of the concessionaire is remunerated and amortized by the exploration of the service or of the work for a definite period” (BRAZIL, 1995a, Article 2, item III).

In the legal literature, one criticizes the second type of concession, to the effect that it is not different from concession of public services. Masagão (1933, *passim*) claims that the concession contract of a public work is always accessory to a public service concession contract, as the public administration aims at providing services.

Thus, the execution of the work is entrusted to a person who recovers its investments, through the remuneration received in the management of the public service, to which it intended the performance of the work.

On the other hand, Di Pietro (2005) recognizes the existence of this contract as an autonomous mode to the concession of public service, however, he emphasizes that to characterize it as such, the concessionaire’s remuneration must not be made by the licensing power, which would qualify it as turnkey contract².

The author also cites the various modes of concession regulated by the national regulations, highlighting that “there is conjugation of different modes in which one constitutes the main purpose and the other(s) the accessory” (*Ibid.*, p. 84):

- Concession of public service, in its common form, regulated by Law No.8.987/95;
- Concession of public work, regulated by the same Law No. 8.987/95 and now also by Law No. 11.079/04, in its sponsored form;
- Sponsored concession, one of the modes of public-private partnership contemplated in Law No. 11.079/04;

- Administrative concession, another mode of public-private partnership also instituted by Law No. 11.079/04;
- Concession of use of public assets, with or without exploitation of the good, regulated by sparse legislation.

Thus, one evidences the relationship existing between the concepts “concession” and “PPP”, important to understand the analysis that will be performed in this work.

On the other hand, in the discussion on PPPs contracts, it is common to find the presence of an accounting aspect, the possibility of the government accounting of the expenses in PPPs off the Balance Sheet, i.e., private expenses in infrastructure goods without impact on the governmental capital expenses, and, which, however, involves the investments necessary to the provision of public services to attend society.

The benefit is focused on control of the public debt levels, enabling the government to present a healthy financial situation in view of the international financial system and to obtain the resources necessary to meet other demands of society.

STN, the National Treasury Secretariat, through Ordinance No. 614/06 (BRAZIL, 2006c), established the general rules in connection with the consolidation of public accounts applicable to PPP contracts, establishing in its Article 4:

The assumption by the public partnership of a significant part of at least one among the risks of demand, availability or construction will be considered a sufficient condition to characterize that the essence of its economic relationship implies recording assets accounted in the SPE in the balance sheet of the public entity in compensation to the assumption of an equal value resulting from risks assumed.

Thus, nationally, there is a relationship between the transfer or sharing of risks and the form of accounting. However, one notices a need of scientific work, which discuss the relationship among these two variables, as will be shown below.

Handley-Schachler and Gao (2003) deal with success and failure cases of the private initiative in England, and state that the implications of the PPPs, in connection with public sector financial risk, the transfer of risks and the effects of the private initiatives on the public sector debt, can be quite different in emergent economies, especially in those experiencing rapid and unpredictable growth, which may affect the standards of demand costs, as well as risks linked to it.

On the other hand, Edwards and Shaoul (2002) deal with the problems of the concept of risk transfer on which rests the rationality of the PPPs, this is due to dispersion of risks and costs not being made evident in this process.

In the final analysis, the authors mention that, in view of the failure of the project in the transfer or risks and in obtaining *value for money*³, upon comparing with estimates by the public sector, the possibility of reinforcing and/or dissolving the partnership is, in practical terms, circumscribed to legal and operational aspects.

Thus, the public sector can end up being locked into the partnership for good or for evil. This contribution has dealt with the subjects and problems that limit the benefits derived from the PPPs assessing them from the transfer of risks and not from an accounting perspective.

Broadbent and Laughlin (2002), in turn, placed the importance for AP of transmitting legitimacy in each activity or decision making, and emphasized the accounting profession as one of the bodies that supply it through its statements. In view of this, the very authors recognize that the process of legitimizing is delicate due to interests that support the importance of the PPPs being very strong and influential.

It is evident that the impact of the PPPs may be assessed by recording and measuring its effect on public finance, and must be faithfully reflected by the accounting. In this research, one shall propose an alternative assessment of the essence of the PPP contract, based on the contractual purpose, aimed at faithfully characterizing the phenomenon to account for.

3. METHODOLOGY

In the choice of the theme, one considered important raising an accounting discussion not circumscribed to legal aspects of the phenomenon to analyze the essence of PPP contracts in Brazil, where as the regulatory accounting milestone applicable to these contracts commends the criterion of “essence over form”.

By characterizing said essence one shall exert impact on the form of accounting this partnership system and, therefore, in evidencing the financial and economic situation of the institutions, basis for assessing the management by the public administration.

One also considered that, even though the possibility of registration of infrastructures outside the Public Balance Sheet has been diffused, in general, the accounting theme has not had a highlighted presence in the discussion of the PPPs, despite the provisions of STN having been issued almost one year and eight months after the sanction of the Law that regulates them.

In the accounting rule, one adopted prioritization of the essence of PPPs contracts as a criterion for registration, as a focus in the economic relationship among the parties.

However, this work aimed at determining if there is agreement between the essence of the contractual purpose and the legal form of PPPs contracts in the creation of highway infrastructures in Brazil. Thus, one intended to submit to discussion an additional criterion to assess the economic essence of these contracts.

Based on what was said previously, this is an exploratory research, defined by Martins (2002, p. 38) as an “[...] approach adopted for the search of greater information on a certain subject”.

According to Gil (1996, p. 45): “A fair share of the exploratory studies can be defined as bibliographical research” and this study is thus characterized, as one worked in it with secondary data obtained from material published in books, theses, dissertations, scientific articles and other materials accessible to the public, with the purpose of structuring, analyzing and interpreting them (MARTINS, *op. cit.*, p. 35).

It is, in turn, a documentary research, as it used non conventional literature, defined in the terms of Mattar (2005, p. 153), as:

[...] the non conventional and semi-published documents that are produced in the scope of the government, academia, commerce and industry, in whose origin the commercial aspect is not taken into account, therefore, they are not normally found in the commercial distribution circuits and in libraries.

Moreover, documents such as laws, government manuals and statistical reports were analyzed.

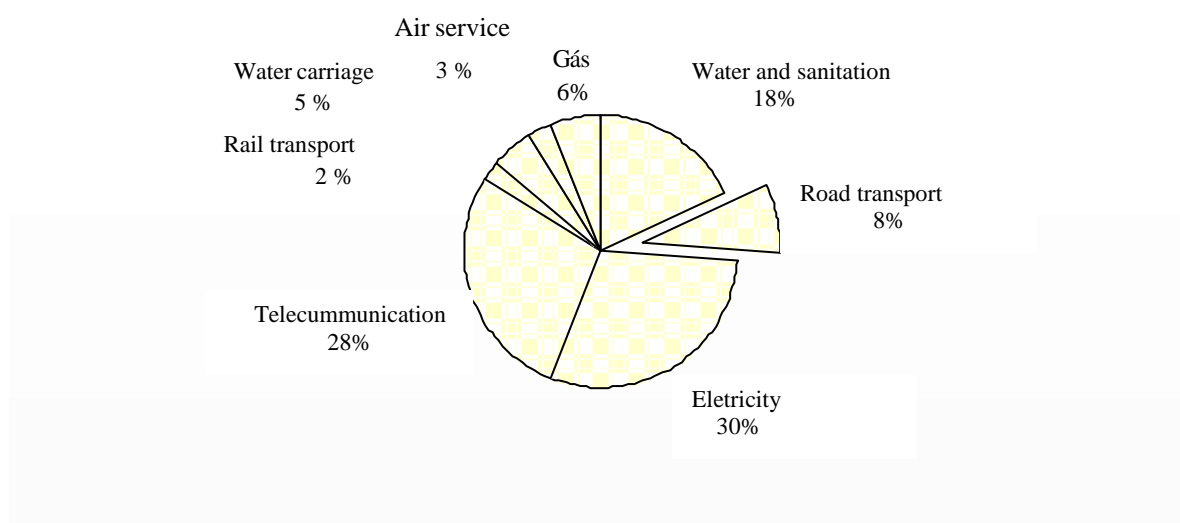
Finally, it is also a descriptive research (MARTINS, *op.cit.*, p.36), as it described the context in which the PPPs appeared in Brazil as well as an attributed legal source.

The choice of the economic sector was based on the importance of highway infrastructure for the development of policies of struggle against poverty and by the potential negative effect exercised in entrepreneurial logistic costs, as mentioned in the introduction.

The literature reveals the difficulty of the sector in attracting private investments, if compared to other sectors, for reasons of profitability and risk⁴ (Table 1). However, a research made by *Aecom Consult, Inc.* (2005, p. 4), for the U.S. Department of Transportation, sustains that the PPPs emerged as an alternative path to overcome difficulties by revealing that, in international terms:

[...] around of third of the infrastructure of public use planned since 1985 or finished by October 2004 has been for road projects, bridges and tunnels. In an international basis, the road has been the greatest category of infrastructure to use private finance through public-private partnership agreements.

Thus, the benefit achieved by this sector through the formalization of this system of partnerships has been evidenced.



Graph 1 – Private infrastructure projects per sector

SOURCE: WORLD BANK *In: FISHER; BABBAR, 1996, p. 1*

A final criterion for the choice of sector was that the first PPP contract structure by the Brazilian federal government was for restoration, maintenance, operation and capacity of highways BR-324 and BR-116 in the States of Minas Gerais and Bahia (BRAZIL, 2006b).

On the other hand, the definition of the federal sphere as a field of study of this research is sustained: (1) by the greater availability of information at this governmental level, which enabled this study; and (2) by the intention that the findings contribute to a discussion of the recent accounting rule issued by the government.

One worked on the database obtained in primary sources (COOPER and SCHINDLER, 2003, p. 223). Thus, the sources comprised: interviews, laws, regulations and government data, as well as encyclopedias, books, manuals, magazine articles, newspapers and sites.

In the analysis and interpretation of data, the technique used by Spink (1997) was followed, assessing the context in which was issued the regulation of PPPs contracts in Brazil and the terms that were present in the discussion previous to it.

Krippendorff (1990, p. 81-82) affirms that, in the analysis of content, it is necessary to determine units to relate the field of observations and that of messages. In this work, four thematic units were defined:

- Unit I: Refers to the antecedents of the partnerships between the public and private sectors, as reported in governmental documentary sources, books and works presented in congresses. This has permitted to know what was sought in each form of partnership;
- Unit II: Brings the economic context at the time of conception and implementation of contracts, including the tax status and the condition of highways in Brazil;
- Unit III: One aimed at identifying the objectives behind the discussion on the PPPs, as well as discussing the arguments that define the essence of PPP contracts today;
- Unit IV: They analyzed the general accounting pronouncements in relation to categorization of public expenses to identify the criterion maintained by STN until the existence of the PPPs with respect to the essence of the creation of infrastructures.

4. ANALYSIS AND DISCUSSION

a. Unit I – Antecedents of Partnerships

A reform of the Brazilian AP is characterized by two minimum realities which rulers face at all levels of government: (1) financial crisis in terms of lack of funds to invest in essential areas such as health, education, social security, housing, transportation and safety; and (2) search of new institutions that permit to achieve greater efficiency in the provision of these services. According to Di Pietro (2005, p. 68-80), the evolution of administrative decentralization reforms has gone through the following phases:

- Concession to private companies: delegation of the execution of public services on its account and risk, under the inspection and control of the public administration, including collected from the user;
- Appearance of mixed economy and public companies: the former to fulfill the new obligation of the public administration – participate in exploitation losses, the latter to provide certain services without having to face the difference of foci existing in a mixed economy company – the fixation of accessible prices for the population *versus* profit, aiming at obtaining higher prices;
- Concession of public services to state-owned companies: the institution goes back to following the international trend, but this time with delegation to state-owned companies. The justification of the concession is lost – to provide a service without investing a vast amount of public funds;
- Again the concession to the private company, without abandoning the possibility of making concessions to state-owned companies. In this phase, privatization strictly speaking emerges.

One observes that the public administration has sought different forms to involve the private sector in public investments, including, with the passing of time, it has had to change certain premises which were favorable to it to retain this involvement.

One notices that, despite the existence of the mentioned foci differences, one has gone back to the institution of concessions and, moreover, the privatizations were implemented, evidencing the failure of the capacity of the public administration to meet the population's needs.

b. Unit II – Economic Context

In Brazil, the budgetary resources necessary for recovery and expansion of the productive base are scarce, due to the effect that the conjugation of the following had in the financial situation of the public sector: (1) the high cost of the public debt⁵; (2) the LRF, Law of Fiscal Responsibility, conceived to restrain the disobedience by irresponsible rulers; (3) the need to generate a fiscal surplus; and (4) the legal expenses linked to education and health (CINTRA, 2004, *passim*).

Cretella (2005) emphasizes that the fact that governments have increased taxes successively, from the 1980s, has inhibited investments and increased tax evasion by taxpayers. The author affirms: “[...] in Brazil, the sources of generation of cash by the Treasury have been exhausted for a long time” (*op.cit.*, p. 4-5).

Road transport is an essential activity (BRAZIL, 2002), i.e., an activity that meets the unpostponable needs of the community (BRAZIL, 1988). Therefore, one could infer that: If road transport is essential (as the distribution of medication and foods), the infrastructure that enables this transportation (and distribution) is also considered as such.

According to ABDIB, Brazilian Association of Infrastructure and Base Industries *apud* Cintra (*op.cit.*), in Brazil “[...] half of the 57 thousand kilometers of the road network is in a terrible condition of conservation.” According to the same source, the need for resources for investment in infrastructure in Brazil is estimated at US\$ 20 billion per year.

c. Unit III – Strategies Undertaken

Based on the pronouncements made during the PPP International Seminar on the provision of infrastructure services (2003), by those who could be considered protagonists in the discussion on PPPs in Brazil, one could determine a point of convergence among all of them: the search for a creative formula, which attracts private capital to face two situations: (1) the need for investment in infrastructure assets; and (2) the limitation of this capacity and that of government debt.

To meet this need is significantly important due to its impact on economic growth. Thus, the new strategy to attract private financing of the basic infrastructure projects, such as highways, without affecting public finance was the sanction of the PPPs laws, as it opens the possibility to obtain financing of infrastructure which is reflected off the Public Balance Sheets, which would permit the government to increase investment in infrastructure without affecting its level of debt.

Basically, there are two arguments to reflect an infrastructure off the Public Balance Sheet: (1) the significant transfer of risks to the private partner; and (2) the conditioning of its retribution to the provision of services to the collectivity in the opportunity and quality agreed, which would configure the operation in a service acquisition, not of work.

Below a discussion with respect to these arguments will be held.

4.3.1 Transfer of Risks

Edwards and Shaoul (2002) have approached the complexity involved in the concept of transfer of risks on which rests the rationality of PPPs, due to the fact that the dispersion of risks and costs does not make this process immediately evident.

Although in the Brazilian accounting rule, one has recognized the complexity stated by the authors, in it was adopted the sharing of risks as the sole criterion to condition the registration of assets in or off the Public Balance Sheet, with regard to PPPs.

Fayard (1999, p. 8) put it as follows:

It is worthwhile to recall that although contracts [...] may offer benefits to all the parties, in many cases, the public authorities would seem to think that the concession is a means to obtain something for nothing. They must be realistic: the private sector can get involved in a project if the remuneration contemplated is proportional to the level of risk. This means that in the case of public-private partnership, the project must be financially viable, reducing part of the cost carried by the private sector or reducing the risk to which the latter is exposed.

In Brazil, the criterion has been similar by highlighting the importance of PPPs as “[...] a mechanism of efficiency to bring, through the construction of good contracts, incentives to both sectors [...]” (PPP INTERNATIONAL SEMINAR, 2003).

Article 5 of the law of the PPPs provides that its clauses shall comply with the provisions of Article 23 of Law No. 8.987/95, where applicable. This article, in item IV, points out as an essential clause of the contract, that relative to the price of the service and to the criteria and procedures for the readjustment and review of tariffs. In turn, Article 9, § 2, of this Law provides that contracts may provide mechanisms of review of tariffs, to maintain the economic-financial equilibrium.

From the teachings of Di Pietro (2005, p. 114) on economic-financial equilibrium, one can affirm that if the interest of the private person in maximizing its benefit exists, the interest of the State in meeting the needs of the community converges with it. Therefore, the contract must reflect this convergence of interests containing clauses that distribute rights and obligations among the parties in a balanced way.

Thus, the innovative distribution of risks established by the Law of the PPPs, constitutes a form of attracting private investment, necessary to finance the creation of infrastructure assets, such as highways.

Another line of reasoning is the following: In the analysis of the economic context, it was evidenced that road transportation is an essential activity whose performance requires the creation of infrastructure assets (highways); and, as it is a fact that the Constitution in Article 21, item XII, provides that it is up to the Union to exploit, directly or by means of authorization, concession or permission, road transportation services, one infers that the government, by being obliged to meet the need of the population, is the natural incumbent of the responsibility to create these assets, even if for this, it uses private financing and assumes different degrees of risk, depending on its capacity, to attract this finance.

To reinforce what has been mentioned above, here is how Modesto (2005, p. 450) puts it:

“In the public service, the final responsibility for the provision is of the State. If the private person, as delegated, abandons the provision of the service, the State must assume it, answering for its continuity. The private person, in capacity of delegate, answers directly for the damages that it produces, but the State is not irresponsible to users of the services. In public services, in the event of *delegation of provision*, the State is not an indifferent third party, in the final analysis, for the regularity of the service and for the appropriate performance by its delegates, as it maintains the incumbency of the activity.”

Therefore, one considers that the government shares risks with the private partner, in the construction of road, aiming at creating attractive conditions for the financing of the work and, thus, complying with the very obligation of enabling the road transport service.

4.3.2 Form of Payment

To locate the purpose of this study in terms of the Law of the PPPs (*op.cit.*, Article 2), the creation of roads through PPPs fits into the mode of concession of services preceded by public work (sponsored concession).

Di Pietro (*op.cit.*, p. 146) draws attention to the concept contained in Article 2, item III, of Law No. 8.987, concession of public service preceded by the performance of a public work, which “[...] admits that, after the end of their work, the concessionaire only exploit commercially the work itself, without providing necessarily a public service.” This is why the concept makes reference to the fact that the investment made by the concessionaire can be remunerated and amortized by the exploitation of the service or of the work for a definite period.

Camargo (2004) already mentioned: “The microeconomic efficiency gain of the PPPs results from the fact that the same private agent will build and use the assets subsequently to offer the service, which is the objective of the contract”.

Di Pietro cites the forms of remuneration acceptable, in a concession of the work: (1) by contribution of instituted improvement; (2) by delegation of the execution of a public service; or (3) by simple commercial exploitation of units permitted by the work.

According to the author, in dealing with the second form of payment, the contract will have two successive objectives: first, execution of the work, afterwards, provision of the service.

An argument to consider the PPP as a service provision, not acquisition of the work, is the conditioning of the payment by the government to the private partner according to the quantity and quality of the services put at the disposal of users (BRAZIL, 2003; 2004a) and not according to the progress of the work.

However, Di Pietro (*op.cit.*, p. 146) says the following:

Suppose the event in which the concessionaire builds a public parking lot and is authorized, subsequently, to commercially exploit this parking lot as remuneration for construction of the work. Or that he builds a bridge and after commercially exploits the traffic by the bridge. There is no provision of service, but simple commercial exploitation resulting from the use of the public asset by the administrated. This occurs also in highway concessions.

It is clear, by the events presented, that the provision of services by the concessionaire would not be possible without the asset of infrastructure that was given them to build.

Thus, the terms “principal activity” and “accessory activity” apply in the case of the concession of highways, as one has it that “the purpose is the construction, expansion or reform of a public work, accompanied by the commercial exploitation of the work for purposes of remuneration of the concessionaire, but the same contract involves, as a rule, the use of assets form the public estate” (DI PIETRO, *op.cit.*, p. 84-85).

On the other hand, Modesto (2005, p. 466) affirms that, in economic terms, the existence or not of delegation of public services by concession is not indifferent, as, while provided directly by the State, they are financed by taxes, i.e., they are public services maintained by all. However, provided by concessionaires, as a rule, they are maintained only by users of the service, according to the intensity of the use of each.

Applying the above to a PPP contract, one infers that both the government (with the resources collected through taxes) and users (directly in function of their needs through tolls) shall pay for the financing of the infrastructure, without which it would not be possible to

provide the transportation service. At the end of the contract, this infrastructure shall pass to formal ownership by the State, and, consequently, of society.

One infers, therefore, that in the construction of highways in Brazil, under any type of contract, the fact of the private partnership receiving payment by the government of users, according to the progress of the work or provision of services (ACCESSORY ACTIVITY) is a remuneration for the infrastructure that he has built (PRINCIPAL ACTIVITY), without which it would not be possible for him to perform any service.

d. Unit IV – Accounting Criterion Applicable to Public Expenditure Prior to the PPPs

There are pronouncements issued by STN (BRAZIL, 2004b; 2005), which show, generally, the criterion adopted in relation to the construction and maintenance of infrastructure assets, such as highways and schools.

In the specific pronouncement to the highways, STN instructs to classify the expenses linked to construction as capital expenditures and those produced by maintenance, as current. This in attention to Law No. 4.320/64 (BRAZIL, 1964).

According to Law 4.320, in the current expenses are classified those with maintenance of services created previously and the expenses for the operation of bodies; and, in capital expenditures, those made with the purpose of creating capital goods (group - investments) or event to acquire capital goods already in use (group – financial inversions).

In accordance with STN (BRAZIL, 2001), paving in highway works is constituted in the act of making a surface capable of supporting traffic in comfort and safety conditions, which may be used in the construction of a new highway or in the repair of an existing one.

Thus, when the paving service is directed to the construction of a new highway, the expense shall be recorded as capital because one is dealing with the creation of a new capital good. However, if this service corresponds to the maintenance of highways built previously, it shall be recorded as a current expense.

Thus, it is important to highlight that STN itself, based on a general provision, has issued pronouncements such as those cited previously, where it compares the construction of a new highway to the creation of a capital good. And, such as paving, to build a highway is the act of creating a surface capable of supporting the traffic in comfort and safety conditions to the user.

This is the objective pursued with the construction of a highway. On the other hand, maintenance of the same is, instead, a service that complements this work.

Based on the definition of the work for bid purposes, expressed in Article 6, item I of Law No. 8.666/93⁶, STN affirms that there is no relationship between definition for bidding purposes and accounting classification, which provides the record of the budget performance as the purpose of the expense – maintenance, acquisition or creation.

Given the above, one clarified the change of the criterion maintained by STN from the existence of PPPs, with respect to the accounting of highway infrastructures in particular.

5. FINAL CONSIDERATIONS

The analysis made of the antecedents of the legal relationships between the public and private sector in Brazil, evidences the incapacity of the former in attracting private investments in search of meeting population needs. This coupled to the economic context, of

scarcity of resources and incapacity of public debt, determined that a new institution of reciprocal rights and obligations were implemented in both sectors.

One has discussed that the sharing of risks is a sufficient criterion to determine that the infrastructure built may be recorded off the Public Balance Sheet, because one is considering the acquisition of a service and not of a work. Let it be considered that a contract provides obligations and rights for both parties; therefore, this sharing of risks is constituted in a criterion to give to the contract a form which enables this financing. In the construction of highways, the sharing of risks aims at creating attractive conditions for private investment.

It was also evidenced that STN has maintained the criterion of accounting for the construction of highways as a work and not as a service, until the appearance of the PPPs, where one comes to consider the sharing of risks as an additional variable to determine if an infrastructure must be registered off or in Public Balance Sheets.

It was concluded that the purpose of a PPP contract, in the road sector is the creation of infrastructure and that its essence is comprised of a principal activity – the construction financed by the private sector, and an accessory one – the provision of a service, as form of payment for the financing. However, the Law of the PPPs would characterize the project as a concession of a service preceded by a public work, as if the latter were accessory.

Thus, both the terms of the Law of the PPPs and those of Ordinance 614/06, limit the analysis of the essence of the contract by establishing provisions, which disregard the antecedents of the PPPs, the economic context in which they emerged, the strategies necessary for their implementation as well as the accounting criteria previously maintained for capital expenses. Thus, both rules lead to the supremacy of formal aspects over the essence of the transactions at the time of assessing the phenomenon to be accounted for.

Finally, based on the findings of this research, one considers that there is no agreement between the essence of the contractual purpose and the legal form of PPPs contracts in the creation of highway infrastructures in Brazil.

This work submits to discussion an alternative assessment of the essence of the PPP contract based on the contractual purpose of partnership and not in the economic relationship among the partners.

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¹ Bound contemplated by Law. Mandatorily ruled by a set of laws and legal provisions.

² Contract – Agreement or adjustment containing certain terms and prices conditions for the performance of a work by another party.

³ Value for money: the optimum combination of whole life cost and quality (or fitness for purpose) to meet the user's requirement (HM TREASURY, 2004, p.34). The Government is clear that value for money should not be equated with the lowest cost option^o. (Id. p. 49).

⁴ Fisher e Babbar (1996, p. 1) reinforce the description of this difficulty making a comparison among the conditions in which the highway sector develops and the electricity sector, for example.

⁵ The public debt has gone from 30% of GDP in the first half of the 1990s to more than 50% in 2001. The high cost of financing of the public debt generated strong fiscal pressure and the tax burden triggered. As a consequence, the budget disequilibria of the public sector became routine.

⁶ Every construction, reform, fabrication, recovery or expansion, performed by direct and indirect performance (BRAZIL, 1993)