The legal framework for public-private partnerships (PPPs) and concessions in transition countries: evolution and trends

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Over the past few years significant improvements have taken place in numerous EBRD’s countries of operations in the policy and legislative framework of public-private partnerships (PPPs) and concessions. The enhancements in the region include a trend towards more pragmatism in law reform with the enactment of PPP legislation in addition to concession legislation; the introduction of a Private Finance Initiative model inherited from the United Kingdom (UK); the creation of PPP units such as those in western Europe; and some new initiatives concerning institutional PPPs.

The 2012 assessment of the legal framework for PPPs and concessions (“the Assessment”) is part of the EBRD’s exercise to evaluate the legal and institutional framework of member countries compared with best international practice developed since 2004. It also serves as an important tool to measure investors’ risk in each country and to identify reform needs and possible technical assistance. The Assessment showed that the average compliance status with best international practice for all relevant countries falls between "high compliance" and "medium compliance", with the larger category (17 countries) now being "highly compliant". It is also worth noting that among the 17 highly compliant countries, most have recently adopted a new concession or PPP law.

The question, therefore, is whether such legislative evolution will be translated into practice by the development of PPP projects that are so needed by many countries.

The 2012 EBRD Assessment

The enabling of fair and transparent PPP legislation is vital to the development of a market economy and as such the concession sector has long been recognised by the EBRD as a core area of its Legal Transition Programme and has now been extended to a larger scope regrouping all forms of PPP including but no longer limited to concession legislation.

Many of the EBRD’s countries of operations have had major deficiencies in their concession and PPP legal and institutional frameworks and this often acts as a barrier to investment and further economic development. Thus it was important to set the framework for overcoming the limitations of the public budget for infrastructure building by making use of the private sector’s resources, including financing and know-how.

The 2012 Assessment of the legal framework for PPPs and concessions is part of the EBRD Legal Transition Team’s (LTT’s) efforts to improve the legal environment in its countries of operations. The LTT’s ultimate objectives are to encourage and provide guidance to policy and law-makers while developing the concessions and PPP-related legal reform in the region. The 2012 Assessment analyses the PPP legislation in each of the EBRD’s countries of operations and benchmarks it to international best practice, including the UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects, European Union concession acquis communautaire and other related materials.

The Assessment combines the two approaches of law assessment that the LTT has undertaken since 2004, studying: (i) the compliance of concession/PPP laws (referring to the laws on the books) and (ii) their effectiveness (analysing the way the laws actually work in practice). The Assessment is contemplated as an upgrade to the last 2008
Concession Law Assessment and 2006 Legal Indicators Survey (LIS 2006) extended to all sorts of PPPs including Private Finance Initiative (PFI) types of contract and as such it applies a similar, and thus compatible, methodology in order to measure each country's progress in improving their concession/PPP legislation compared with international best practice.

The results of the 2012 Assessment are summarised in Charts 1 and 2 with respect to total country compliance and effectiveness, compared with best international practice (100 per cent).

Chart 1
Quality of PPP legislation in transition counties

The total figure which is represented in each graph for each country is the sum of the results of numerous questions concerning various core areas. The results shall therefore be studied in more detail as some issues may appear to be deal-breakers, preventing the development of any PPP project even if the total result may appear satisfactory.

Note: The chart shows the score for the extensiveness of national PPP laws. The scores have been calculated on the basis of a legislation questionnaire benchmarked against internationally accepted best standards and practices, including the UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects, European Union concession acquis communautaire and other related materials. Total scores are presented as a percentage, with 100 per cent representing the optimal maximum score for these benchmark indicators. Extensiveness is measured on the following scale: very high (above 90); high (70 to 90); medium (50-70); low (30 to 50). For more details see: www.ebrd.com/concessions

**Strongest and weakest assessment categories**

The Assessment revealed that security and support issues are the most problematic areas in the region. For the purposes of the assessment the security and support issues concentrate on the availability of reliable security instruments to contractually secure the assets and cash flow of the private party in favour of lenders, including “step-in” rights and the possibility of government financial support, or guarantee of, the contracting authority’s proper fulfilment of its obligations. Seventeen countries were shown to be below the medium range status, which demonstrated that serious improvement to this core area is required with respect to the security instruments available and the possibility of government support, which is necessary for the private financing of public infrastructure or service projects. Very few countries have a law which provides for “step-in” rights for lenders or for direct agreements between the lenders and the granting authority, which are considered “good standard” bankability provisions in project financing, without which it will be difficult, if not impossible, to arrange for the financing of a project.

On the other hand, settlement of disputes and applicable law does not appear to be a serious problem as all countries, with one exception, appear to be above the medium range status, but it must be taken into account that some of the questions in this core area, such as the possibility of foreign arbitration, appear to be deal-breaker issues, without which no concession or PPP could be financed in these countries.

The absence of ratifications of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958) and/or of the Washington ICSID Convention on the Settlement of Investment Disputes (ICSID) (1965) is not a good signal to the international business community and financing institutions (and this absence still applies to Belarus, Poland and Tajikistan).

Chart 3 shows how the countries have scored in relation to security and support issues and settlement of disputes and applicable law.
Chart 3
Quality of legislation in relation to (1) security and support issues and (2) settlement of disputes and applicable law

Note: The chart shows the score for the extensiveness of national PPP laws in the two areas above. The scores have been calculated on the basis of a legislation questionnaire, as benchmarked against internationally accepted best standards and practices, including the UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects and other related materials. Total scores are presented as a percentage, with 100 per cent representing the maximum. For more details see: www.ebrd.com/concessions

Significant legislative activity

Within three or four years, if we take 2008 as the starting point since the last assessment, no less than 17 EBRD countries, representing roughly half of the EBRD countries of operations, have enacted a new concession or PPP law. 3

During the same period numerous other countries have further adopted some significant amendments to their existing legislation, making them more compliant with international best practices. Chart 4 illustrates how the level of compliance of existing legislation with international best practices has evolved since the last Assessment in 2007-08.

Such a trend is even more remarkable in that it was noted in the 2007-08 Assessment that since the previous concession law assessment in the EBRD's countries of operations (made in 2004 and 2005), also roughly half of the 28 concerned countries at that time experienced significant changes with respect to their concession legal framework, either through the enactment of a new concession or PPP law or as a result of changes in their public procurement law affecting works or service concessions.

This represents a very significant development in such a short period of time affecting most EBRD countries of operations. The recently proposed geographical extension of the EBRD region to include southern and eastern Mediterranean countries such as Egypt, Jordan, Morocco and Tunisia has shown the same dynamism towards the enactment of new PPP legislation. As in all such countries the drafting of a PPP law is in progress if not yet achieved.
Trend towards regulating PPPs in addition to concessions

Many countries are now aware that they need a PPP law in addition to a concession law. Most of the new laws refer to all types of PPPs including, but not limited to, concessions. Even in the very few cases where the new law is limited to traditional concessions and the Build Operate Transfer (BOT) form of PPP, the drafting of a larger PPP law is under consideration (such as in Turkey, Morocco, Russia, Jordan and Tunisia). Countries without concession laws (for example, Belarus) are also asking for assistance in this respect. This trend clearly shows that most countries today in the area of EBRD operations recognise the necessity of improving and enlarging their concession and PPP framework and adopting the proper instruments necessary to develop PPPs.

For the past decade legislative trends in the EBRD region of operations have slightly changed focus from regulating BOT-type concessions to wider range spectrum PPP arrangements including “lighter” arrangements (those not necessarily involving a construction element or end-user payment) and management contracts of less duration. Procedure-wise, PPP requires a more flexible and effective mechanism than that of procurement and concessions.

Generally, until 2004-05 most countries used to regulate concessions in their national laws, with PPPs remaining a matter of legal policy and structuring under the existing rules of the law on obligations, or similar, as opposed to a single Act regulation. Accordingly, there have been virtually no definitions of PPP available on either a national or international level. This has recently changed and we have witnessed a new trend whereby countries are developing a separate PPP Act, or an Act including concessions as a type of PPP, among others.

While the majority of the EBRD countries of operations have Concessions Acts, not regulating other forms of PPPs, there are currently 11 countries that have specific PPP Laws/Acts sometimes also including Concessions.4

A few of the abovementioned countries have enacted both a PPP Act and a Concession Act and it is therefore important to see exactly the scope of each law, and what arrangements are covered by which law.
Introduction of the PFI model

Following this pragmatic trend many countries are now aware that they need to introduce the Private Finance Initiative model (PFI) of PPP contracts, in particular for relatively small projects in the non-merchant sector. They are looking for a proper framework, not only to allow the traditional large concessions and BOT projects (where financing is based on the proceeds expected from the actual operation of the project) but also to acquire new legal instruments allowing the financing of non-commercial projects, as achieved successfully in most western European countries.

Contrary to the traditional concession with delegation of the associated public services, the PFI model contract usually provides for the financing and construction of the facility together with some maintenance services to the facility during its future operation – but often without the delegation of the public service itself which remains in the hands of the public entity. Such PFI models work in the non-merchant sector, such as in schools, hospitals, prisons and other public buildings or public facilities or non-commercial services.

The remuneration for such a project is based on a rent and/or service fee to be paid by the public authority user of the facility over a long-term operation period starting from the date of delivery and is based on the availability and performance of the new or rehabilitated public facility or services rendered.

Such projects can be of a smaller size than the traditional BOT type of contract, for which project finance-based financing will hardly be available or even considered by financial institutions below US$ 100 million of investment. Such smaller projects under the PFI model would therefore be more affordable for the states or local communities but require full confidence in the creditworthiness of the public user’s signature or of any guarantee to be provided by the state or local government.

Creation of PPP units

It is interesting to note that many new laws provide for the establishment of a specialised institution for assistance in the realisation of PPPs, as well as for promotion, information and consultancy in the field of PPPs. This is the case for Albania, Bosnia and Herzegovina, Croatia, Egypt, Mongolia, Poland, Romania, Serbia and Slovenia as has been the case in most of the western European countries which have developed PPP in the last two decades following the successful British experience.

It is still the case that in the majority of the countries assessed there is still no specialised independent body properly staffed with experts that would be engaged in all aspects of PPP projects, their development and promotion and assist in the implementation of a PPP project. Often such a role is devoted to a ministerial department, or an institution in charge of promoting investment and responsible for PPPs; often with a mission limited to policy matters or to monitor the enforcement of the law and thus not having the capacity to properly ensure the rapid take-off of PPP investment in the country.

Introduction of IPPP legislation

It is also worth noting that some countries also chose to regulate Institutionalised Public-Private Partnerships (IPPPs) in their recent PPP laws. During the last three years the emergence of IPPP legislation has resulted from the problems raised by the European Commission on the application of Community law on Public Procurement and Concessions to Institutionalised Public-Private Partnerships (IPPPs).

IPPP is a cooperation between public and private parties involving the establishment of a mixed capital entity which performs public contracts or concessions. The private input to the IPPP consists, apart from the contribution of capital or other assets, in the active participation in the operation of the contracts awarded to the public-private entity and/or the management of the public-private entity. Simple capital injections made by private investors into publicly owned companies do not constitute IPPP.

The European Commission has published guidance on creating IPPPs in order to clarify the rules applicable to the involvement of public and private partners through joint legal entities in the awarding of a PPP project – both to enhance legal certainty and to ensure fair competition through the tender selection of the private partner.

Obviously the involvement of public parties on the side of the private party in a joint venture may be a promising form of PPP in some countries, in particular where the private sector development is very low and where most of the economy remains in the hands of state-owned companies. Such IPPP may generate foreign direct investment and allow some sharing of production or profit but the participation of such mixed public-private joint ventures in any public tender for a PPP project is a serious risk for the transparency and competition process.

This form of IPPP maybe suited to the awarding of a concession already attributed to the special purpose vehicle created by a public party who is looking for a private partner to participate in the equity and to provide its expertise. In such cases the granting of concessions, which is part of the bidding package, is indirectly concerned and the private partner is to be selected through competitive bidding for the sale of
the private part of the share of the joint venture following similar rules to that for the direct selection of concessionaires. Having said that very few PPP laws contain protective provision to that effect.

**Pragmatism**

It is to be further noted that a significant part of these new concession or PPP laws have been drafted in a more pragmatic way than before and are no longer oriented towards the necessary requirements imposed on EU-acceding countries, as was the case for many countries before as shown in the 2007-08 EBRD Assessment.

Many of the new PPP laws are now very much oriented towards the satisfaction of a specific need for PPP, following best practice and the UNCTRAL *Legislative Guide on Privately Financed Infrastructure Projects* and often with the assistance of international financial institutions. They no longer too dogmatically concentrate on the traditional concession models without any consideration for the financial requirements of potential lenders. Many of the new laws contain the enabling provisions necessary to enlarge the scope of available PPP forms, together with the proper security provisions necessary to make the deals “bankable” and furthermore, many of the new laws provide for the necessary support of specialised PPP institutions such as PPP units.

As an example it is interesting to quote the case of Mongolia which did not even appear in the last 2008 Assessment as no concession legal framework could be identified at that time and which now emerges with a very high compliance mark and high effectiveness. The Mongolian Concession Law of 2010 which is the first adopted by this country without any past experience on concession except in the mining sector, is one of the very few legislations of any EBRD countries of operations which explicitly provides for a full range of PPP deals as well as for all sorts of security instruments. It also provides for the possibility of government support and guarantee, together with a specific chapter on lenders’ rights allowing for the possibility of direct agreement as well as so-called “step-in rights – all in accordance with lenders’ expectations to ensure the bankability of project finance deals.

The future will show if such “copy and paste” PPP new regulations, although inspired by the best international standards, will be sufficient to allow the rapid take-off of PPP projects in countries with no prior concession expertise such as Mongolia and without the full revision of their existing legal framework and business environment.

It will also be necessary to follow the evolution of some countries with noticeable past experience in the field of PPP such as the Czech Republic, Jordan and Morocco which are presently facing some political and social challenges from the population.

**The reasons for such evolution**

Among the reasons for such evolution and trends, the EBRD has identified the following consequences resulting from the changing environment:

- increased demand for infrastructure in the context of scarce financial resources and tougher competition for funds and expertise requiring modern innovative structuring of private sector participation in public infrastructure projects
- dissemination of experience of the first PPP/PFI projects in the UK and Australia
- establishment of specialist PPP institutional infrastructure (that is, PPP units/centres in 1999-2001 to enable implementation in Belgium, Ireland, Italy, Portugal, the Netherlands, and so on)
- the publication for public debate of an EU PPP Green Paper in November 2005 and an Interpretative Communication ruling out the developments of directives and instruments governing PPP on a supranational level.

The above factors accumulated to impact upon and, to a large extent, triggered the development of necessary adequate responses including a series of new PPP laws and national policies.

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1 For this Assessment the EBRD selected the law firm Gide Loyrette Nouel as consultant. The consultant team was led by Bruno de Cazalet, Senior Counsel at Gide Loyrette Nouel.

2 In due course the Bank may implement its expansion and initiate investments in the SEMED region, subject to shareholders’ ratification.

3 The Act of Public Private Partnership in Croatia (2008); the Law regulating Partnership in Egypt (2010); the Regulation for implementing Privatization transaction (including PPP) in Jordan (2008); the amendment of Concession law in Kazakhstan creating a PPP Center (2008); the PPP law of the Kyrgyz Republic (2009); the Latvia law on PPP (2009); the Macedonian law on Concession and other type of PPP (2008); the Moldova Concession and PPP law (2008); the Mongolian law on Concession (2010); the law on Concession of Montenegro (2009); the Polish Act on PPP (2008) and the Polish law on Concession of Works and Services (2009); the Romanian PPP Act dealing with IPPP (2010); numerous regional Russian PPP laws; the Serbian Law on PPP (2011); the Tajikistan Concession law (2011); the Tunisian Concession law (2008) and the Ukraine law on State Private Partnership (2010).
