Laying the Foundation Stone: Lithuania’s new Concessions Laws and its lessons for PPPs in Central and Eastern Europe and the CIS

By Christopher Clement-Davies, partner, Vinson & Elkins¹
Giedrius Stasevicius, partner, Lideika, Petrauskas, Valiunas & Partners²
Alexei Zverev, Counsel, European Bank for Reconstruction & Development (‘EBRD’)³

Introduction

Public-private partnership projects (“PPPs”) can sometimes be made to work in isolation in countries attempting this form of infrastructure development for the first time. It may be possible for contractual and structural solutions to be found to deficiencies in the wider legal framework, and, with imagination and patience, problem areas to be thought through and overcome. In addition, successful lobbying in the corridors of government may also obtain one-off benefits or exemptions for individual projects, which may not be available at a more general level. Yet an ad hoc approach of this kind is usually far from ideal. PPPs tend to work best when they form part of a fully thought-out policy, a comprehensive, rigorously planned and carefully implemented programme – a “PPP system”, in other words. One vital component of such a system is likely to be the country’s concessions or infrastructure law (referred to in this article as the “concessions law”), the underlying legislative framework on which many of the project’s legal features may eventually have to depend. Some jurisdictions (such as certain common-law jurisdictions amongst “developed” economies) may not have a need for any such law. Others will, however, and, if they do, its contents and efficacy will obviously play a critical part in the government’s ability to implement PPPs. If it is seriously deficient, or has not yet been introduced, it can greatly compound the difficulties of putting infrastructure projects together. Conversely, a clear and comprehensive legislative framework should significantly facilitate the project’s successful structuring, negotiation and completion. In recent years, many of the transition economies of Central and Eastern Europe and the CIS have both attempted to implement PPP projects and have overhauled their concessions laws (or introduced them for the first time) as part of the transition process. On October 1 this year, the Republic of Lithuania’s new concessions law came into force. This article discusses some of the issues addressed, and lessons learned, by the two law firms engaged to advise on its terms.

Assignment Award

The assignment was commissioned by the EBRD, following an approach by the Ministry of Economy of the Republic of Lithuania (MoE) to the EBRD to carry out a review of its existing concessions law. Lithuania is currently taking a keen interest in PPPs as a vehicle for infrastructure development. A number of projects of this kind had been launched in Lithuania in previous years, although without using the Concessions model under the previous law. These were not unsuccessful in general terms. There was a lack of consistency

---

¹ Vinson & Elkins is a leading international law firm, based in the United States of America, with over 775 practising lawyers and offices in London, Moscow, Beijing, Singapore and Dubai as well as Houston, Dallas, Austin, New York and Washington.
² Lideika, Petrauskas, Valiunas & Partners is a leading Lithuanian law firm with 29 lawyers, 6 assistant lawyers, 2 tax advisers and 1 adviser on competition matters. It has offices in the Lithuanian cities of Vilnius and Klaipeda.
³ The European Bank for Reconstruction and Development is an international institution whose members comprise 60 countries, the European Community and The European Investment Bank. The EBRD operates in the countries of central and eastern Europe and the Commonwealth of Independent States committed to multiparty democracy, pluralism and market economies.
to their structures, however, and to the procedures applied to their implementation. The existing Concessions Law was thought to contain perhaps one or two undesirable features, but nothing worse than that. There was a perception that any significant obstacles in the way of a wider programme of PPPs were to be found at a policy, organisational or practical level. The MoE wanted to assess the efficacy of the Concessions Law nevertheless. The EBRD accordingly organised a competitive tender for an assignment to review it and make recommendations for its amendment. The tender was won at the end of 2001 by a combined team made up of the international law firm Vinson & Elkins with the leading Lithuanian (and Baltic States) firm Lideika, Petrauska, Valiuunas & Partners. The assignment was carried out during 2002. It consisted essentially of analysing the deficiencies in the existing legislation, and assisting the MoE to draft a new law to replace it (as well as helping to explain and modify its provisions during its passage through parliament). The new draft legislation quickly passed into law.

**Lithuania’s Interest in PPPs**

What exactly was it that was attracting the Lithuanian Government to PPPs at this point in time? At one level, no-one should be surprised by its interest. Most readers will be familiar with the dramatic increase in the use and application of PPP techniques in many countries around the world over the past ten years. The British Government arguably led the way with its pioneering Private Finance Initiative. PPP systems have also since been (or are being) introduced in Holland, Belgium, Spain, Portugal, Greece, Finland, Japan, South Africa, Ireland, Italy, Germany and France (as well as in a number of Central and Eastern European countries – see below). They are currently being given serious consideration in Turkey, Mexico, Russia, the Indian sub-continent, other parts of Africa and elsewhere. They have already been in use for many years in South-East Asia, Latin America and – at least in some respects – the Middle East. Numerous factors have played their part in the evolution of this pattern. These range from a changing political landscape, a loss of faith in state control and the impact of budgetary constraints, to the perceived successes of privatisation, the extent and urgency of the need for new infrastructure, the search for better value for money and higher standards in public services, and, perhaps above all, the rapid evolution of the techniques and skills involved in implementing PPPs. A detailed discussion of why this is so, and of the “pros” and “cons” of PPPs (which are by no means universally endorsed), is beyond the scope of this article. The growth of PPPs internationally, however, would certainly have contributed to the Lithuanian Government’s thinking.

At another level, however, an unhesitating rush to embrace PPPs was not in any sense inevitable in Lithuania. The track record of PPPs in the region was very much a qualified one. Various attempts to apply PPP techniques to infrastructure development had already been made in Central and Eastern Europe and the CIS. These included road projects in Hungary, Poland, Romania and the Czech Republic, water projects in Slovenia, Bulgaria and Romania, telecoms projects in Hungary and Poland, and at least the beginnings of a number of port, airport and rail projects. These attempts, however, had met with varying degrees of success. The M5 in Hungary, and the water and waste-water concessions in Slovenia and Bulgaria, for example, were successfully closed and implemented. The M1/M15 in Hungary, on the other hand, did not generate sufficient revenue to remain solvent, whilst the D47 in the Czech Republic was cancelled following a flawed procurement process. The process of putting these projects together had also been long and arduous in several cases. Yet, there is a fairly widespread view that the set-backs and disappointments had been more reflective of the difficulties of adapting this complex and challenging methodology to transitioning
economies and legal systems, than of any fundamental or insuperable obstacles. They are, in a sense, treated as helpful pointers on a journey leading to more refined techniques and better thought-out and structured projects which, it is widely accepted, may take years of evolution before success can be more readily assumed. This seems to have been the thinking in Lithuania.

A number of other factors played their part in this decision. Lithuania was keen to promote innovative ways of meeting the country’s accelerating demand for new and better infrastructure, and to attract private finance to its development. Municipalities were also clamouring to introduce new facilities in the health, educational, transport and water sectors (amongst others), and the Government wanted to ensure that the legal and regulatory framework applicable to them was transparent and consistent. Having learned the lessons of an ambitious privatisation programme in the 1990s, government bodies were also interested in exploring ways of leasing and developing public assets without necessarily selling them outright. Moreover, the country is in the first wave of EU accession countries. It aspires to join the EU in 2004, by which time its infrastructure and infrastructure-related laws, as well as its budgetary practices, will largely conform to EU prescribed standards (the *acquis communautaire*). EU structural funds will become available for its infrastructure projects following accession.

**Limited Precedents**

Just as the experience of implementing PPP projects in Central and Eastern Europe and the CIS has been mixed, the legal framework behind those projects is very varied. A number of countries in the region have introduced concessions laws since the early 1990s with a view to the promotion of PPPs. These laws differ widely in quality, however. The EBRD has developed (and is still refining) a number of mechanisms for reviewing and evaluating them. One such tool, known as the EBRD’s Annual Legal Indicator Survey (LIS), allows the Bank to give existing concessions laws a range of classifications, from “comprehensive” to “inadequate” to “detrimental”. LIS is a perception-based tool launched in 1995 to measure and analyse the legal systems of the EBRD’s countries of operation⁴. It takes a “snapshot” of the state of legal reforms as perceived by local lawyers. None of the 27 countries of operation has been rated as having a “comprehensive” concessions regime.

Examples of “adequate” systems of concessions law include FYR Macedonia, Bulgaria, Hungary and Moldova, whilst those of Russia, Georgia and the Czech Republic fall into the “inadequate” category under the 2002 LIS results (see the attached map)⁵. Interestingly, Lithuania’s concessions laws were rated as “barely adequate”. Another evaluation tool developed by the EBRD is the Concessions Law Assessment Checklist. This checklist takes the form of a comprehensive questionnaire, which is currently being completed in relation to each country with the help of outside consultants. The questionnaire is divided into chapters: policy framework, legal framework, selection of concessionaire, concession agreement, enforcement, etc. Whilst it takes into account the laws already present on the statute books of the country in question, the results of the assessment are designed to assist potential investors who already possess a solid background of knowledge of the laws of that country to make their PPP-related investment decisions. The questionnaire and the results of the assessment

---

⁴ The EBRD’s countries of operations are: Albania, Armenia, Azerbaijan, Belarus, Bosnia & Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, FYR Macedonia, Georgia, Hungary, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Poland, Romania, Russian Federation, Serbia and Montenegro, Slovak Republic, Slovenia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

⁵ The EBRD last up-dated its Concessions Law LIS in 2002.
are expected to be placed on the EBRD website as soon as the verification process is completed later this year.

There is, in fact, a widespread belief that some of these concessions laws are capable of further improvement. They can be unclear, unduly limited in scope, sometimes over-prescriptive and at other times subject to problematic omissions. Several of them were also implemented at speed, before fully thought-out PPP systems had been devised in the countries in question. This may give rise to further institutional and practical difficulties as and when PPPs come to be implemented on a wider scale (as many commentators expect them to be). One should not sound too critical a note, however. When most of these laws were passed, there was a dearth of helpful precedents. The work of bodies such as UNCITRAL (see below) had not yet got underway, and one should remember that the “science” of PPP implementation has made dramatic strides over the past decade, with approaches to institutional, organisational, tendering and financial issues only very recently moving towards greater standardisation, as consensus builds up on international best practice. The same is true of concessions laws and concession agreements.

The Review Process

As we have said, the initial expectation was that the existing Concessions Law in Lithuania would not need to be extensively amended. A detailed review of the Law quickly suggested that this was not the case, however. There were fundamental deficiencies in its structure, scope, content and language, together with a lack of flexibility throughout, which could only be corrected by a thorough-going re-draft. Memoranda were prepared explaining the areas of deficiency and discussed with the MoE.

Precedents from a number of jurisdictions were looked at and adapted to help frame appropriate new provisions (including the draft OECD “Basic Elements” as well as various existing laws already in force). Valuable guidance was also provided by the work of the UNCITRAL (United Nationals Trade Law Commission) Committee on Privately-Financed Infrastructure Projects, which had already published a legislative guide on this subject (in 2000) and was to finalise its model provisions later in 2003. (The UN had also published its UNIDO BOT Guidelines in 1996.) Predictably, however, there were no ideal or readily adaptable precedents to hand. As is so often the case with concession agreements as well as legislation, the combination of local legal traditions with the particular business and political environment in which the new Law was evolving, meant that provisions had to be carefully constructed and refined to suit Lithuania’s particular needs and to ensure consistency with its other existing laws. The assignment also had to take account of the wider legal context. Procurement and construction laws, investment protection, company and insolvency legislation, contract law and other provisions of the revised civil code had to be considered, as well as the relevant EU requirements and recommendations. The new draft law went through several iterations before the MoE could submit it first to the Cabinet and then to the Lithuanian Parliament.

Given the relative lack of constructive and readily-usable precedents, the importance of local law traditions to the framing of legislation and the wide disparity of approach taken by
governments to the creation of viable PPP programmes, it is not easy to generalise about what
should or should not be included in any one concessions law. It does seem to the authors,
however, that it would usually make sense to include certain fundamental provisions. For
that reason, some of the international bodies which have recently studied this subject have
now felt able to draw up “Basic Elements” templates and “Model Legislative Provisions”.
The UNCTARAL “Legislative Guide to Privately-Financed Infrastructure Projects”, first
published in 2001, runs to some 200 pages. The authors heartily endorse most, if not all, of
its recommendations, and in carrying out this assignment were able to make extensive use of
the Model Legislative Provisions which followed it 2 years later. (The published version has
just been released). It is noteworthy that many of these recommendations are in the form of
negatives - statements about what concessions laws should not attempt to achieve or
restrictions that they should not contain. A great deal of the difficulties that arise with these
laws in practice derive from attempts to impose unnecessary constraints or excessive detail
on infrastructure projects. And, whilst common-law and civil law traditions, respectively,
may tend towards somewhat different approaches in this context, it has clearly proved
possible to frame legislative recommendations which straddle these two legal philosophies
(and their various permutations). The “fundamentals” would typically need to cover the
following ground:

• scope and definitions
• power and authority
• selection of concessionaries
• tendering procedures
• exceptions to competitive tendering

• negotiation procedure
• content and validity of concession agreement
• security and “step-in” rights
• dispute resolution
• miscellaneous

The new Lithuanian Concessions Law follows this pattern. In the ensuing paragraphs we
briefly summarise some of its main terms, whilst commenting on the issues they gave rise to
and the deficiencies in the previous Law which they were designed to replace.

The New Law

Part I: The new Law sets out objectives and applicable definitions in Articles 1 and 2. The
previous law had contained some awkward idiosyncrasies in these areas, defining
“Concession”, for example, as a “right to use property”, without developing these expressions
in terms which clearly covered the full range of activities, assets and services which PPPs can
embrace, and limiting “Concessionaires” to Lithuanian corporations. This had given rise to
concerns about scope. In the new law, “Concession” is very broadly defined in relation to the
activities it can cover (taking in design, construction, development, refurbishment, repair,
management, operation and/or maintenance etc.), simply requiring that these activities
contain a “commercial component” and that the Concessionaire assumes at least a
“significant part” of the risks associated with them. Similarly, any Lithuanian or foreign
legal entity can now become a Concessionaire. The previous law had also effectively
required all Concessions to take the form of “BOT” structures. The new Law allows for the
full range of possible PPP structures.
**Part II**: Article 3 provides further amplification of the potential scope of Concessions (clarifying a number of doubts that had affected the previous law). The new law extends to virtually all applicable sectors, from energy (heating, electricity, oil and gas) to rail, water, waste-water and sewerage, roads, bridges, tunnels, parking facilities and other transport infrastructure, telecoms facilities, health and educational “infrastructure”, ports and harbours, public transport and tourism, leisure, sports and cultural facilities, and (by way of catch-all) any other sector which the Government (or relevant local authority) approves for this purpose by specific resolution. Property which remains in the ownership of the State can be included, as can both new and existing assets. Assets and activities which have been formally designated for privatisation in Lithuania cannot be the subject of a Concession, whilst those which have already been “Conceded” cannot, in turn, be privatised during the term of the Concession Agreement. (Concessions cannot be awarded to entities which are prohibited by the separate Law on Investments from investing in the sectors concerned.)

**Part III** deals with the procedure for awarding Concessions. The previous law (in common with many such laws still in existence in other jurisdictions) had been in some ways unclear, inflexible and excessively bureaucratic in this respect, with features that could have been difficult to interpret and operate in practice. The procedures under the new law are clearer, simpler and more streamlined. Essentially, Concessions can be granted by any Government body (or other institution authorised by it) or local authority responsible at law for the function, activity or sector that is to “Conceded”. The assumption is that the prescribed competitive tendering procedure will be used, unless one of the designated exceptions applies. Direct agreements between Conceding Authorities and lenders are expressly allowed for (removing the doubt that often affects this subject in the region). A mechanism for streamlining the process of issuing ancillary licences and permits to a Concessionaire as part of the award of a Concession was also considered, but not thought to be practicable. The Conceding Authority is, however, obliged to provide relevant information about these subsidiary consents.

**Articles 8 to 16** lay down the detailed procedures for competitive tendering. They leave the Conceding Authority with considerable flexibility as to the precise tendering terms, but create a clear framework which is designed to provide guidance (eg. criteria for selection), an important element of objectivity and certain minimum standards in practice. The use of a pre-selection stage and non-binding proposals from bidders is essentially at the Conceding Authority’s discretion. There are formal requirements for announcing tenders and restrictions on the modifications that can be made to them once they have been launched. Certain minimum requirements for both binding and non-binding proposals are laid down. The Conceding Authority’s obligations in relation to the provision of information to bidders are set out. The criteria which the Conceding Authority may include in its evaluation process are clarified, distinguishing between the technical and financial aspects of tenders. The Conceding Authority has a duty to apply such criteria fairly and without discrimination. Parameters for the process of negotiation with the preferred bidder(s) are also included, as are a dispute-resolution procedure for aggrieved bidders and third-parties.

**Articles 17 and 18** address the exceptions to these rules, namely the circumstances in which Concessions can be granted without using competitive tenders, and the requirements applicable nevertheless when they are. (This is an area of clear potential abuse in many concessions laws, and one which (perhaps for that reason) the previous Lithuanian law did not address.) These include particularly urgent infrastructure needs where tendering is not feasible, national security and defence, unavoidable “one-sourcing”, the exercise of step-in
rights in connection with an existing concession, certain types of unsolicited proposal and exceptional financing terms (as defined).

**Part IV** addresses the subject of the Concession Agreement, arguably one of the main difficulties one typically encounters with concessions laws. Frequently, terms are prescribed too narrowly, giving rise both to inflexibility in negotiating those provisions and uncertainty about which additional terms can be included. The language used in the relevant statutes can also be one-sided and sweeping, with implications that can easily deter investors. The previous Lithuanian Concessions Law suffered from a number of drawbacks of this kind (and even cross-referred to a “Model Concession Agreement”, which was approved by the Government and seems to have been envisaged as basically non-negotiable). The new law confirms that the terms of the Concession agreement are essentially at the discretion of the parties, and fully negotiable by them. It then summarises (primarily by way of guidance) 25 outline clauses which are expected to be included unless the parties decide otherwise, covering most of the provisions typically encountered in agreements of this kind. The Concessionaire’s power to create security over its property, rights and assets is expressly confirmed. The parties are free (subject to the Lithuanian Civil Code, and in contrast with the previous Concessions Law) to agree on the governing law applicable to the agreement, and also (although subject to any applicable restrictions and with a default to the Lithuanian Courts if the agreement is silent on the point) on the choice of dispute resolution procedure, including domestic or international arbitration. Certain minimum termination rights are also provided for, subject, again, to the terms of the Concession Agreement.

Finally, the new law provides for non-discriminatory and equal treatment of foreign and domestic Concessionaires respectively (and allows for the potential impact of international treaties).

**Conclusion**

The impact of the new Concessions Law in practice will soon be tested out. We hope (and believe) that it will prove to be a clear, robust, flexible and durable piece of legislation, which will play a significant part in the successful implementation of Lithuania’s PPP programme. It is, of course, a specifically Lithuanian legislative act, not a mirror-image imported from another jurisdiction. Yet we believe that it takes account of some of the latest thinking in this field and the lessons learned from other countries attempting to create PPP systems of their own. We also hope that it will, in turn, be made use of as a helpful precedent by other transition economy countries, as PPPs continue to take shape in Central and Eastern Europe and the CIS.

For further information on this article, the authors can be contacted as follows:

**Christopher Clement-Davies - Vinson & Elkins : +44 (0) 207 065 6014**
**Giedrius Stasevicius - Lideika, Petrauskas, Valiunas & Partners : + 370 52 681 888**
**Alexei Zverev – EBRD : +44 (0) 207 338 6370**