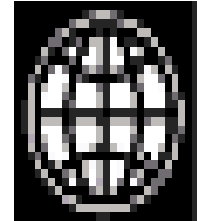


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Institut Français d'Experts  
Juridiques Internationaux



*Economic and legal conditions of success of public private  
infrastructure projects in developing countries  
(workshop)*

*The relationship between the socio-economic nature of the  
infrastructure services and the institutional and contractual  
framework*

**Marc Frilet**

Attorney - IFEJI General Secretary

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## **The world public infrastructure challenge: lessons learnt**

### **Lessons learned in the late eighties**

- Without massive improvement of public infrastructure services, the developing countries have no chance to substantially alleviate poverty and improve economic climate and governance
- Without such massive improvement a substantial part of the development aid and NGO efforts would be wasted.
- The massive improvement cannot be financed entirely by the tax budget: the international development aid will not be sufficient
- The remaining gap is huge and equals several points of GDP
- There is only one option left : to attract private capital, and private promoters to invest and deliver the services

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## **The world public infrastructure challenge: lessons learnt**

### **Lessons learned in the late nineties**

- The private capital and private promoters have their own conditions and standards they will only consider projects which are competitive in their judgment.
  
- Most of the public infrastructure projects developed in early eighties were very influenced by the traditional commercial and banking legal culture; they were often rigid, highly leveraged and based on the project finance model. They often fell short of addressing socio economic and long term issues such as:
  - Affordability of the service and willingness to pay by the end users
  - Adaptation of the service or price to future expectations and inevitable changes in the economic conditions. Ex: Dahbol power project India
  
- The consequential dramatic decrease of private participation in public infrastructure services after the peak of 1997
  
- Main lesson; outright privatization is not a solution in the core sectors (transport, water, power)

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## **The world public infrastructure challenge: lessons learnt**

### **Lessons learned in the current decade**

#### **1- Developing countries**

- The alternative to outright privatization which usually referred to as Public Private Partnership (PPP) has been difficult to organize and to implement in developing countries
- Very few PPP ventures have yet passed the test of time, ( often beyond 10 years)
- Many landmark projects much advertised have difficulty to reach closure; ex: NEPAD in Africa
- However some of them are showing promising signs of success even in the core areas of water and transport.
- If no additional efforts are made to meet the challenges the current global crisis will increase the number of projects in distress.

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## **The world public infrastructure challenge: lessons learnt**

### **Lessons learned in the current decade**

#### **2- Rest of the world**

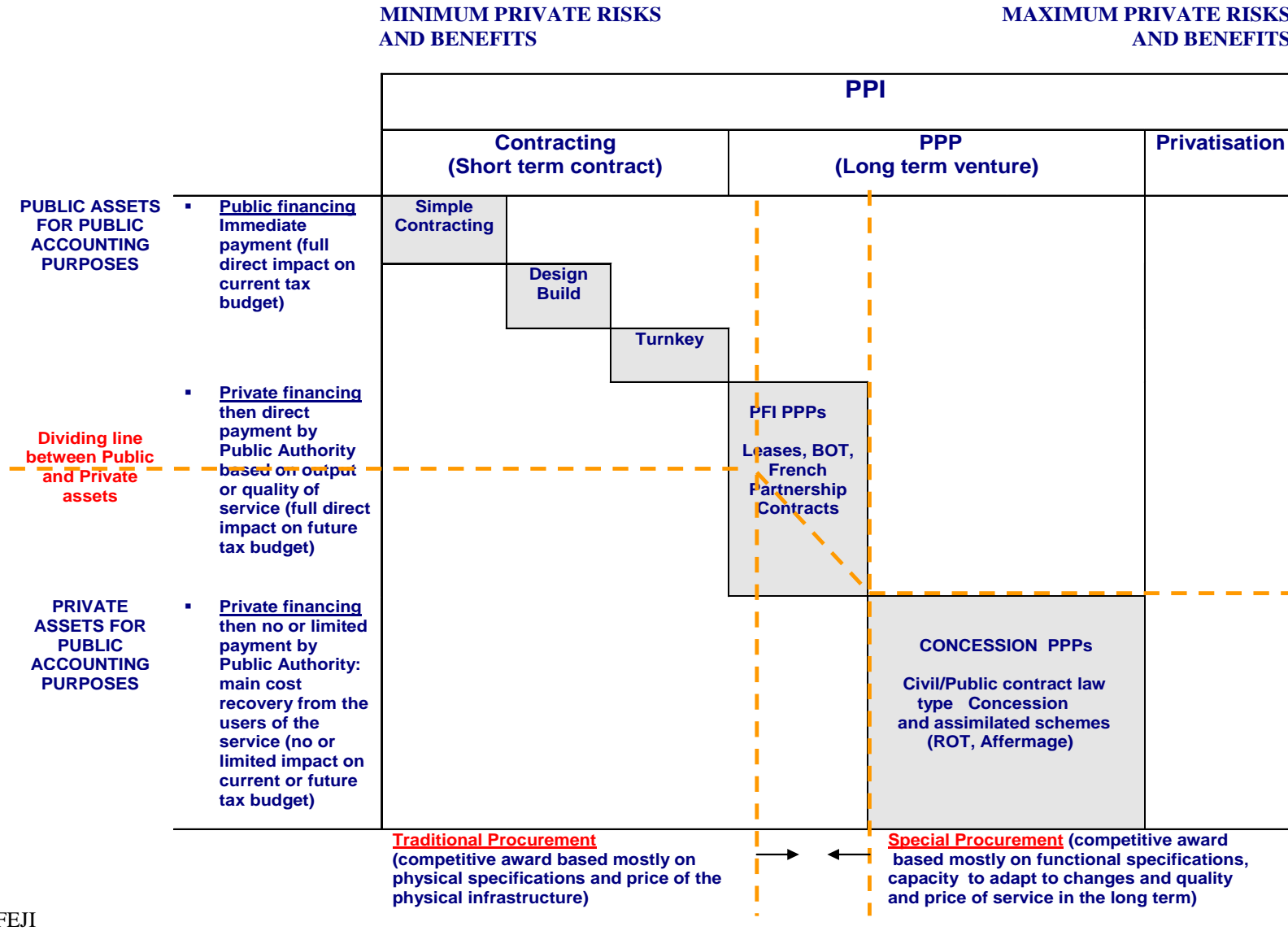
- Numerous PPP's in the rest of the world have been successful
- There is mounting evidence that the success is not reserved to developed economies
- It is imperative to build on the lessons learned for the condition of success for resilient PPP ventures for public services in the core sectors.
- It is essential to assess their relevance for developing countries.
- The main lessons for PPP in core sectors :
  - Not all the PPP formats have a chance to succeed and to meet the challenge in developing countries.
  - Resilient PPP and their legal framework must fully integrate underlying socio-economic parameters

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## **PPP in core public service sectors: which format and why?**

- There is a lot of confusion in the PPP definition: PPP is often used as a marketing tool not in line with the reality of the world and of the underlying situation that it represent.
- Consequently when a particular project has to be developed in a particular sector and in particular country It is often considered that the deal is unique, that there are few precedents, that there is no contractual legal framework or best practices to refer to.
- This triggers difficult appraisals and evaluation of the issues then lengthy negotiations with teams of both side afraid of unknown future evolution and testing new concepts and clauses etc.
- This perception is in sharp contrast with the reality; for each family of PPP there is a vast area of practical experience based on thousands of projects around the world.
- A PPP flow chart is one of the best tool to clarify the situation

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## **The distinctive features between the two families of PPP's**

➤ **The PFI PPP's**: nearly two decades of experience and lessons learned mostly in the common law world with a mother country: UK

-A lot of useful lessons in project preparation, value for money public sector comparator, performance criteria etc.

-Model well adapted to fully commercial PPP's when revenues for the service are directly paid by the public authority during the whole venture.

-Model difficult to adapt to long term demand risks and to revenues generated by users fees

➤ **The Concession PPP's**: 150 years of experience and lessons learned mostly in the civil law world with a mother country: France

-A lot of useful lessons in legal and contractual framework

-Model well adapted to non fully commercial PPP's in the core sector when revenues for the service are coming from the end users



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**Is it realistic to promote further the Concession PPPs in developing countries given the poor track record and the financial crisis?**

- A first and simple political answer: Yes since there is no sensible alternative. New concepts, new procedures, new incentives, must be designed and or promoted.
- A second answer often heard in the field today: good idea in principle, but adaptation to less sophisticated economies is questionable. The capacity building exercise will be enormous.
- A third and somewhat unexpected answer from the few legal and financial expert teams involved in day to day work in developing countries and having shared their experience with a systemic approach: Yes because' very few concession PPP's in a developing world have so far been based on a legal, contractual and institutional framework, which are the conditions for resilient concession PPP's:
- Contrary to widespread belief and thanks to the global crisis, there is a new window of opportunity.

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### **The main conditions of success of resilient concession PPPs and their adaptation to the developing countries situation**

#### Two universal conditions

➤ **The Concession PPP must result in :**

- A service adapted to the reasonable expectations and to the contributive capacity of the end users often for decades,
- A concessionaire having sufficient guaranties that it will have the capacity to make a reasonable profit during the life cycle of the venture, if it performs well even in case of additional investments and of adaptation of the service to the public needs

#### How to fulfill those conditions?

- 1) An in-depth analysis and common understanding of the socio economic conditions which will impact on the operation and on its economic viability for the life of the venture
- 2) A consensus on core legal and contractual principles governing the concession
- 3) A consensus on the partnership procedures defusing most of the risks and sharing the upside above a certain threshold

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**I - Socio economic analysis to be translated into appropriate legal and contractual conditions**

A masterpiece reference document summarising some of the best practices: «*Attracting investors to African public private partnerships: a project preparation guide*», World Bank ICA PPIAF 2009

- 1) Preliminary question: Is concession PPP (or affermage PPP) the best option? The answer is in essence positive when
  - all or most of the PPP income will derive from users fee
  - the public sector is unlikely to be competitive in financing, construction and operation
  - the public sector is ready to support and to promote actively the Project

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**I - Socio economic analysis to be translated into appropriate legal and contractual conditions**

**2) When PPP is the best option what are the prerequisite before advertising the project for competition? Outline of the critical path**

**A) Very detailed and robust analysis at least in the following areas:**

- Capex**
- Opex**
- income from users fees**
- socio economics externalities**

**B) Design of a preliminary business case taking into account reasonable hypothesis in term of allocating or sharing risks and opportunities and showing key financial parameters. Calculating the internal rate of return.**

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**2) When PPP is the best option what are the prerequisite before advertising the project for competition? Outline of the critical path**

**C) Matching the results with the reasonable expectations of the potential bidders**

**D) Testing the business case with conservative sensitivity ratios.**

**E) In most cases; Redesigning the deliverables of the Project in order to have best chances to adapt to the market. Preferred option for sharing or allocation of risk and benefits will have to be revisited and the condition of financing of the gap with a fully commercially viable project will have to be well tested.**

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**3) Have the railways or port projects in Africa followed such a critical path?**

**A) Existing railway PPP : reference document : *Review of selected railway concessions in Sub-Sahara Africa: World Bank 2006***

**There are several railways in PPP operation in Africa under the concession or affermage model. For each of them there has been difficult start and expectation not met. Some issues :**

- Unrealistic forecast of the demand : too high expectation from users**
- Difficult (and unfair?) competition with the truck services**
- State not strictly fulfilling financial and regulatory commitment**

**Many of those issues could have been mitigated before finalizing the deal**

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Nevertheless those PPP projects are real improvement in operational terms, even if the future remains somewhat uncertain.

It is fair to say that it was difficult at the time to comply with the critical path due to the history of those public railways: those deals stand somewhere between privatization and PPP.

**B) PPP railway project in preparation. Example: Conakry Kankan (Guinea)**

- 600 kms of reconstruction of an old not operating railway
- Priority for 40 kms of urban railway
- Prima facie little chances for concession PPP
- However the critical path has been followed and the feasibility of resilient PPP emerges.

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**I - Socio economic analysis to be translated into appropriate legal and contractual conditions**

**C) Example of a port project (Madagascar, port d'Ehoala)**

- New deep port to be built in relation to mining products
- Initial studies show the potential of public multi user port and concession PPP considered
- Critical path for preparing the PPP fully organized ;several layers of studies, counter expertises, and financial scenario prepared, and wide consensus on the economic platform.
- Port fully built in time with an element of investment subsidized,
- Official opening July 2009
- Optimistic expectations in spite of difficult political and economic situation



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**II - Outline of legal and contractual principles essential for resilient concession PPP in the core sectors**

There is a growing consensus that public service PPP in the core sectors must integrate fundamental legal and contractual principles which have governed the vast majority of resilient concession PPP's in the world.

Those legal and contractual principles derive less from a particular legal system than from the very nature of the deal. Some examples:

- **Condition of delivery of essential public services:**
  - **Continuity of the service**
  - **Non discrimination between the users**
  - **Adaptability of the service**
  - **Transparency of the financial and operating condition**

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**II - Outline of legal and contractual principles essential for resilient concession PPP in the core sectors**

**A. Some major legal or contractual consequences deriving from the above principles: a particular equilibrium between rights and obligations alien to most commercial contracts. Examples:**

**A1- Particular rights of the conceding Authority:**

- . to terminate the venture not only for default but also for convenience if duly justified by the general interest.**
- . to impose changes in the agreement in order to adapt the service to the interest of the end users.**
- . to use the equipment and workforce of the concessionaire even when dispute arises for continuing the operation**

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**II - Outline of legal and contractual principles essential for resilient concession PPP in the core sectors**

**A2- Particular rights of the Concessionaire:**

- right to full indemnification when the Public Authority exercises the above sovereign rights : compensation, which can be rendered efficient through various techniques.

-right to adequate compensation when an unforeseen impediment (“sujétions imprévues”) occurs during construction, or rehabilitation.

right to reinstate the equilibrium of the contract conditions when a hardship (“imprévision”) situation arises, i.e. when the surrounding economic circumstances prevailing at the date of signature have substantially changed in an unforeseen manner (easy calculation if the concession financial matrix is a contractual reference)

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**II - Outline of legal and contractual principles essential for resilient concession PPP in the core sectors**

**B- How many concession PPP's are governed by the above legal and contractual framework in developing countries?**

**B1 - Example of existing PPP railways in Africa: some key legal principles are not included:**

-Most of the railway operation is governed by pure commercial and competition law (within some limits for the tariffs). Public service obligation are the exception, limited to non commercially viable passenger services.

-No reference to the hardship theory and to the overall financial equilibrium principles benefiting to the concessionaire.

**B2 - PPP railway project in preparation (Conakry Kankan): key principles considered in order to facilitate resilient PPP.**

**B3 - Existing Port project (Ehoala): key legal principles included**

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**III -Partnership procedures and regulatory system facilitating resilient PPP. How to prevent destabilisation of the venture?**

**Partnership and ADR**

1- Partnering procedure: very valuable process for dialogue and capacity building: regular well prepared meeting at various levels, including a charter to behave as partner.

2- Alternative dispute resolution (ADR procedures): can be very efficient if well structured in advance in a simple manner

**Outside regulation**

1- The underlying references and legal principles that the regulator must follow needs to be clearly expressed.

2- The constitution and operation of the regulator (experience, independence and integrity )are essential.

**International arbitration**

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## **CONCLUSION**

**The socio-economic nature of the infrastructure services in the core sector triggers several legal and contractual conditions widely recognized as best practices which are the basis of resilient PPP's**

**Those conditions and best practices only start to be really appraised and slowly integrated in the concession PPP's in developing countries. If well formulated and promoted those principles will without doubt renew the interest and appetite for concession PPP which are a urgent necessity in core infrastructure services.**

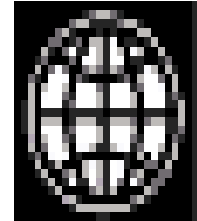
**A new wave of regulations procedure and contractual conditions is a pre requisite; their content is ripe to be included in laws and contracts**

**Some countries are ahead of others, example : recent concession law Tunisia, public contract law Senegal.**

**However a huge task remains, and the IFEJI PPP working group is ready to further contribute to this superior objective**

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Juridiques Internationaux



***THANK YOU***

**Frilet - Société d'Avocats**  
**94 Boulevard Flandrin**  
**75116 Paris**  
**avocats@frilet.com**  
**+33.1.56.26.00.40**