

INTERNATIONAL MEETING INFRASTRUCTURE AND PPPs

BUSINESS OPPORTUNITIES IN INFRASTRUCTURE AND PPPs:
MEETING WITH THE WORLD REFERENCES ON THE THEME

APRIL 27TH - 28TH, 2015 - BRASILIA

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Guarantees - Operational means to bring remedies to the present situation

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Guarantees for privately financed infrastructure projects: A universal driver for economic development

Without guarantees at contract signature, many essential public services projects would have not been possible in PPP as early as 19th century : some examples:

- Railways in US and Canada
- Railways in India
- Canals in US
- Canals and railways in France
- Development of Paris infrastructures and Hausmann buildings, etc.

However, very early many of these guarantees have been criticized.

Some countries like UK refused sovereign guarantees for railways.

Others like India criticized heavily the guarantee to be given to international lenders.

Over the years a lot of international experience gained but insufficient exchanges on lessons learnt.

In the last 50 years, the guarantees for protection of infrastructure investment became a hot issue leading to numerous State laws and Treaties of various nature: Bilateral and Multilateral Treaties

Guarantees in our modern world: complex situation preventing completion of many projects

Present situation is far from being satisfactory in spite of genuine efforts of the international community (IFIs, States, international organizations, etc.) to resolve the issues.

Bâle III and others financial restrictions either expressed or more or less implied through contingent liability situations have exacerbated the problem.

Several landmark projects in distress have further limited the possibility to develop guarantees and to issue sovereign or other guarantees : two examples out of many:

- Power sector : Dahbol IPP Project in India
- Toll highway: roadlink Seoul to Incheon airport

Quotes from Timothy Irwin, World Bank expert in a reference publication: “Government Guarantees- Allocating and Valuing Risk in Privately Financed Infrastructure Projects” :

“It is very difficult for government to make good decisions about guarantees”

“Psychological research show that people struggle to make accurate judgment about risks and then fail to make the best use of even their judgment”

How to obtain satisfactory guarantees for PPP projects? (1)

1. DECREASE THE RISK PROFILE DURING PROJECTS PREPARATION PHASE

Project preparation needs to be substantially improved for most projects: insufficient resources generally allocated to project preparation

▪ **Example: Demand risk for a toll highway**

Time is gone where a government would simply accept to bear demand risk below certain parameters.

Lessons learnt indicate that without very comprehensive studies, few chances to conclude a sustainable project:

- Best practices on the content of the studies : some key analysis:
 - Global affordability
 - Global traffic forecast
 - General willingness to pay
 - Detailed sensibility analysis relating to possible economic changes
 - New technology
 - Competing transport infrastructure in the future

- Best practices on the organization of the study:
 - Be assured that the studies will be carried out by a team of international and local experts working in an integrated manner under strict supervision for assessing the interest and benefits for the people and free of conflict of interest
 - Be assured that the final studies are robust and endorsed by all stakeholders

How to obtain satisfactory guarantees for PPP projects? (2)

2. MAXIMIZING THE CONTRACTUAL GUARANTEES BY REFERENCE TO LESSONS LEARNT INTERNATIONALLY

2.1 Examples: concession PPP for ports, airports, railways...

- If subsidy is needed to bridge the economic and financial gap: focus on an investment subsidy payable during the construction phase: Easy to secure before contract signature
- During contract negotiation :
 - Propose and agree detailed framework of clauses on the avoidance, reduction or sharing of risks based on lessons learnt internationally: examples:
 - Permitting risks
 - Tax risks
 - Environmental risks
 - Land use and expropriation risks
 - Propose and agree other key clauses for situations which are likely to arise over the PPP life cycle: examples
 - Tariff determination and tariff changes
 - Adaptation of public service for general interest reasons
 - Economic and financial equilibrium
 - Changes in laws
 - Dispute avoidance and alternative dispute resolution mechanisms
 - Efficient arbitration

How to obtain satisfactory guarantees for PPP projects? (3)

2. MAXIMIZING THE CONTRACTUAL GUARANTEES BY REFERENCE TO LESSONS LEARNT INTERNATIONALLY (2)

2.2 Examples: public payment PFI PPP: Hospital, school, prison

- In those schemes, the recovery from the investment and operation comes entirely from public funds
- The main obligation of the private party aside from financing is:
 - to complete a global contract for design and construction of the building or facility with performance requirements; and
 - to operate and maintain the building or facility during the PPP lifecycle
- The main risks often for decades after satisfactory construction: risk of default of payment by public sector

Lessons learnt internationally: financial liability to pay for PFI PPP qualifies as public debt: consequences:

- Payment default amounts to default in reimbursement of public debt
- In most countries, special remedies available for securing payment of such public debt
- When PPP contract is concluded with sub sovereign or public company: Example: public utilities.
 - the public debt qualification may need to be specially recognized or endorsed.
 - Example of endorsement: PPP contract cosigned by Ministry of Finance.

How to obtain satisfactory guarantees for PPP projects? (4)

3. EXPLORE IN DETAILS THE RANGE OF EXTERNAL GUARANTEES POSSIBLE OR REALLY NEEDED AND CHANCES TO GET THEM

- **Investment protection laws and Treaties**

In some situation the possible risks are reasonably covered by investment protection laws or by bilateral or multilateral investment Treaties.

- **Step to be taken:** carry out an appropriate due diligence with experienced professionals able to advise on precedent and actual implementation

- **External guarantees**

If the above is not sufficient: Carry out an appropriate due diligence on the range of external guarantees prima facie available

Examples:

- National or international guarantee funds
- Special external investment protection guarantee: example: MIGA or World Bank breach of contract guarantee
- When an external guarantee appears available it is necessary to explore in details the real conditions of issuance

How to obtain satisfactory guarantees for PPP projects ? (5)

3. EXPLORE IN DETAILS THE RANGE OF EXTERNAL GUARANTEES POSSIBLE OR REALLY NEEDED AND CHANCES TO GET THEM (2)

➤ Step to be taken:

- Go beyond information generally provided and analyze essentially
 - ✓ Standard risk matrix used by the guarantor institution
 - ✓ How this risk matrix has been used in similar situation?
 - ✓ What is the detailed procedural chain?: timing and precedent
- For government guarantee:
 - ✓ Understand the scope and evaluation of the contingent liability taken by a government

This is in fact a critical issue for a political decision to deliver a government guarantee.

Take into account international best practices relating to the decision to assume the contingent liability and how to determine value, monitor, and limit such liability: a leading publication from the World Bank Timothy Irwin and Tanya Mokdad: “Managing Contingent Liabilities in Public-Private Partnership”.

Based on those information, evaluate in advance if the project has chances to meet those conditions.

If reasonably possible adapt the project before applying for guarantee

A way forward for improving private sector guarantees for pipelines of successful PPP

Coordinated international actions appear necessary for decreasing uncertainties and risks :

- Improve procedures and standards for project preparation and for financing the preparation
- Promote innovative set of template clauses to be included in the PPP agreement in line with international best practices
- Promote improvement of the investment protection climate in line with international best practices: State laws, bilateral investment Treaties, multilateral investment Treaties: learn from successful examples such as the European Energy Charter or framework agreements for landmark investment projects
- Promote transparent information for the scope and condition of delivery of external guarantees: engage with the various institutions to exchange on risk matrix, evaluation criteria and approval process, etc.
- Consider new external guarantees instruments

CICA, IFEJI and UNECE are ready to contribute within the framework of the UNECE international Center of Excellence.

Coordination with Brazil and Latin America situation may be easily developed through a Latin American HUB which could be set up in Brazil with the support of CBIC

Thank You !

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