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Hot Topics in Implementing PPPs

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Hot Topics in Implementing PPPs -- Outline

- Overview of the situation in Russia
- Long-term support or contractual payments from the governmental authority
- Change of Law resulting in additional costs or decreased revenues.
- Impact of political decisions and deadlines
- Compliance with environmental, social and corporate governance (ESG) standards
- Laws regulating infrastructure – selected comments

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Overview of the Situation in Russia

- “Principal models of PPP so far are Build-Transfer-Own and Life Cycle Contract based on Federal Law on Concessionary Agreements, Build-Own-Lease to public entity-Transfer, lease from public entity models that are compliant with the Civil Code of the Russian Federation have been implemented on the regional level. 70 of the 83 subjects of the Russian Federation issued their own laws on participation in PPP projects”. (source: *VEB*)
- The amount of infrastructure financing envisaged to be procured by 2020 in Russia is estimated at USD 600 billion.
- In Russia a large number of PPP projects (around 1000) are realized in transport, utilities, social infrastructure and territorial development.
- “Financing of the ongoing PPP projects is provided mostly by a very limited pool of banks - Vnesheconombank, Russian commercial banks with state participation, such as VTB, Gazprombank, Sberbank, international financial organizations (primarily EBRD, Eurasian Development Bank, IFC)” (source: *VEB*)
- Russian private pension funds, investment funds, international investors have limited involvement.

Long-term support or contractual payments from the governmental authority

- Where public support or payments are required under the concession agreement, does the public finance law or special authorising legislation permit a long-term public party commitment to make payments to the end of the concession period?
- Is there a currency conversion risk involved?
- How would the long-term public party commitment be treated for purposes of public accounts?

Change of Law resulting in additional costs or decreased revenues (1)

- Project company / private investor will require an indemnity (a right to reimbursement) on account of additional costs or decreased revenues due to a Change in Law
- How broad should the scope of Change of Law be?
  - Does it cover laws, regulations, interpretations, internal administrative procedures?
- The term “PPP” is still not defined in the legislation.
  - On March 13, 2013 the Government of the Russian Federation initiated a draft federal law “On the bases of private-public partnership in the Russian Federation”, which still at the edge of being considered by the Russian Parliament
  - The second draft of the abovementioned law introduced in Autumn 2013 specified 11 forms that Public Private Partnerships can take in Russia, i.e. the list can be considered as restrictive.

Change of Law resulting in additional costs or decreased revenues (2)

- “The Concession Law regulates BTO projects exclusively. Regional laws regulate different PPP forms to a varying degree, including in many cases BOT, BOOT and BOO. There is unfortunately a risk of inconsistency between regional PPP laws and the federal Concession Law and Public Procurement Law. In case of a dispute, if a court finds that the regional law contradicts with the federal one, the latter should inevitably prevail.” (source: *EBRD*)

- The risk of future change does not apply to current laws or foreseen changes – so would an indemnity cover these proposals?
- Risk of public party v. powers of awarding authority
  - The current State Budget laws prohibit the public partner to take on and execute financial obligations under an agreement
- Different damages, dependent on whether the operator takes demand risk
  - To what extent should an indemnity cover lost revenues?
- Must the change be discriminatory for damages to be available?

Change of Law resulting in additional costs or decreased revenues (3)

- What standard of materiality (deductible amount) should apply before an indemnity becomes available to the project company?
- Availability of alternative remedies to monetary damages
  - Example: can compensation be paid through an extension of the concession?
- Other material legal issues
  - Example: no procedure for provision of land plots for the PPP projects exists. A separate auction for lease of relevant land plots is required in addition to the PPP tender.

Impact of political decisions and deadlines

- Political deadlines include
  - International sporting events
  - Elections
- Resolving major issues and maintaining timetables
  - Legal titles and permitting
  - Regulatory risk / legislative changes
  - Bankability
  - Conditional bids / negotiating the concession agreement with the preferred bidder

Compliance with environmental, social and corporate governance (ESG) standards (1)

- Evolving ESG standards
  - World Bank Group
    - IFC Policy and Performance Standards on Environmental and Social Sustainability (updated 2012)
    - Environmental, Health and Safety Guidelines (revision underway)
  - EBRD
    - Environmental and Social Policy (January 2014 – revised draft released for consultation)
  - EIB
    - Environmental and Social Handbook (updated December 2013)
  - Principles of Responsible Investment (PRI)
  - Santiago Principles (adopted by Sovereign Wealth Funds)
  - Equator Principles III – transition period ended 1 January 2014

Compliance with environmental, social and corporate governance (ESG) standards (2)

➢ Equator Principles III

Since 2003, the terms “sustainable development” and “social and environmental liability” have become instrumental in capital raising projects as a result of the adoption of the Equator Principles. These principles, currently adopted by 79 banks, provide a financial industry benchmark for determining, assessing and managing social and environmental risks in project financings.

Borrowers are not able to finance their operations on global capital markets unless they comply with the guidelines of a given bank’s social and environmental policies derived from the Equator Principles.

In June last year, the Equator Principles were revised significantly. Since January 1, 2014, the revised version of the Equator Principles (EPIII) have applied to:

- project finance advisory services where the scope of financing is at least US$10 million;
- corporate loans where the scope of financing is at least US$100 million; and

Compliance with environmental, social and corporate governance (ESG) standards (3)

- bridge loans with a tenor of less than two years that will be refinanced through project financings or corporate loans.

Additionally, the EPIII require (as a condition precedent in loan agreements) that borrowers:

- perform an environmental impact assessment of projects which may trigger adverse environmental and social risks (e.g. human rights or employment levels);
- evaluate options to reduce greenhouse gas emissions if a project is expected to produce annual greenhouse gas emissions of more than 100,000 tons of CO2 (carbon oxide);
- ensure effective engagement with local communities affected by a project and with governments or NGOs where necessary; and
- publish a report on environmental impact assessment findings and annual emissions (over 100,000 tons of CO2) (to be made available online).

Laws Regulating Infrastructure – Selected Comments

- Russia
  - PPP project implementation experience in the road infrastructure sector in Russia has been the subject of widespread discussion by legislators and business community members alike.
  - Federal Law No. 115-FZ "On Concession Agreements" implemented certain amendments which were largely related to the promotion of PPP project implementation in motor transport and road infrastructure.
  - The current version of the Law on Concession Agreements significantly expands the scope of PPP project implementation to encompass most motor transport and road infrastructure facilities, including individual motor roads, tolling instruments, and road service facilities.
- European Union
  - Focusing on transport, the Directorate-General for Mobility and Transport (DG MOVE) of the European Commission oversees policies respecting air, road, rail and water transport with the goal of creating a single competitive European transport are, as spelled out in a Commission White Paper issued in 2011. To this end, the European Commission has issued numerous Directives regarding transport infrastructure that are implemented at the national level.

Thank you

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