DLA PIPER

EVERYTHING MATTERS

Financing and Regulating PPP

Risks and Issues in Structuring a PPP Framework

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Introduction: PPP sectors

Public Private Partnership

- **Industry**
  - oil and gas
- **Transportation**
  - roads/bridge/ travels
  - airports
  - seaports
  - rail lines
- **Utilities**
  - powerplants
  - desalination water/ treatment plants
  - wastewater treatment plants
  - waste disposal/recycling and waste-to-energy
  - district cooling
- **Social Infrastructure**
  - hospitals and clinics
  - schools
  - prisons

Introduction – What is a Social Infrastructure project?

- Social Infrastructure includes projects in the following sectors:
  - Healthcare (hospitals)
  - Education (schools, universities)
  - Social Housing
  - Prisons
- Social Infrastructure projects are well suited to the PPP model as European examples demonstrate

What is PPP?

- Increasing tendency for governments to use public private partnerships (PPPs) to build roads, bridges, railways, hospitals, schools etc

- Private sector raises money then recoups the investment by operating the asset over a long period and either charging the user (concession-type PPP) or receiving payments from the government (PFI-type PPP)

- The key of a PPP project is that the Public sector can obtain a new infrastructure (i) without paying for it during construction, (ii) transferring to the Private sector the construction risks and, in turn, (iii) granting the Private sector with the right to operate the asset and generate the necessary cash flow to repay the investment

Concession type and PFI type PPP

Concession

- Private sector can charge end users for the use of the asset (e.g. a toll road, a commercial port, a toll bridge, an underground)
- These projects involve a demand risk (revenues depend on the use of the asset by end users) → Revenue generating projects

PFI

- The asset itself cannot generate income directly from charging the end-users but the government pays a consideration for the availability of the asset which is used for providing activities of public interest (hospitals, schools, prisons, etc)
- These projects do not involve demand risk as the payment from the government is not, or at least is in a minimum part, linked with the use of the asset by end-users → Non-revenue generating projects

Social Infrastructure projects are availability based projects

Risks and Issues in Structuring a PPP Framework

In structuring a PPP legal framework, few issues must be taken into consideration, in order to:

- attract investors (being contractors, investors in equity and lenders)
- guarantee good value for money for the Public Sector

Risks and Issues in Structuring a PPP Framework

Attracting Investors

In order to attract investors and make possible to create a PPP market few risks and issues need to be taken into account:

- Risks
  - currency (local currency vs USD/Euro)
  - inflation
  - interest rates

  The combination of these three factors has a significant impact on the bankability of a project and is reflected in the duration of the operation phase. Under current circumstances banks are not in a position to lend for more than 15-20 yrs max.

  - demand risk (‘cold projects’ vs “hot projects’)
    - cold projects: based on availability type payment mechanism, are repaid by payments made by the public sector subject to availability and performance regimes (hospitals, schools, etc.)
    - hot projects: based on revenues generated by end customers (toll roads, ports, light rail, etc.)

Risks and Issues in Structuring a PPP Framework

Attracting Investors (2)

- Issues
  - political stability
    - key issue for implementing PPP projects
  - step-in rights for the lenders
    - ability of the lenders to protect the project by taking control replacing the non performing Project Company
  - ability to transfer equity following and during construction
    - important for setting conditions for a secondary market
  - established legal framework for enforcement of securities
    - banks interested in an actual and enforceable security package

Risks and Issues in Structuring a PPP Framework

Attracting Investors (3)

- Issues
  - allow foreign investors and mix with local market players
    - prequalification criteria to ensure international participation
  - compensation on termination
    - in PPP projects, it follows different rules than traditional contracts: aimed at securing recoverability by the banks of financial penalties and charges
  - availability payments: who is ultimately the public authority guaranteeing the payment?
    - local municipalities, regional authorities, ministries, government…

Legal Issues in Structuring a PPP Framework

Value for Money for the Public Sector:

- transparent and selective awarding procedure
  - creates competition on prices
- knowledge of PPP: establishment of well trained and assisted PPP Units
  - PPP requires specific competences which generally are not held by public sector especially in local authorities
- Involvement of external counsels at an early stage/soft test on construction and lending markets before undertaking the tender
  - increases the bankability of the project

Legal Issues in Structuring a PPP Framework

Value for Money for the Public Sector:

- creation of a framework law vs beginning in developing experience in a specific sector
  - depending on the urgent needs of each country, it might be advisable that a pilot sector be chosen, subject to an actual programme of subsequent deals which should be ready to come into the market
- right balance in the transfer of risks to the private sector
  - current market conditions impose a well balanced share of risks
- effective monitoring and application of the penalties regime (availability payment and payments based on performance)
  - ensures that the Project Company is constantly bearing the risks undertaken under the project agreement

Case Study: Turkey and PPP in Healthcare Sector

- The Ministry of Health of the Republic of Turkey (MoH) has developed and is implementing a plan to expand and improve its medical sector by creating a new and efficient public health infrastructure
- To achieve this vision, the Turkish government calculated that a significant number of projects are required totalling an investment of more than USD 5 billion which the MoH plans to implement within a 5 year period
- The main challenge for the MoH, will be to procure such projects in the most efficient, cost effective and rapid manner, without overburdening the public finances and straining the limited public resources
- The MoH has decided that a carefully designed Public Private Partnership program would be the best way to effectively carry out the project of creating a modern and efficient health infrastructure in Turkey
- The Kayseri Health Campus project is the first PPP program adopted for the healthcare sector in Turkey

Case Study: Kayseri Health Campus

2005:	Supplementary Article 7 to law No. 3359 of 1987, as introduced by Law No. 5396 of 2005 sets out the principles of PPP contracts
2006:	Issuance of the Regulation (2006), implementing Art. 7
2007:	Set up by the MoH of the Department of Public Private Partnership (2007), development of base documentation for the Project and a Preliminary Feasibility Report.
2009 (March):	Appointment of SLF as Legal Strategic Advisor (March 2009), a joint venture between:

- DLA Piper;
- ACT ECON a competition and regulation consultancy firm (based in Istanbul and Ankara); and
- Koyuncuoglu Law Firm (Turkish law firm based in Istanbul and Ankara).

Case Study: Kayseri Health Campus

2009 (August):	Review and preparation of all tender documentation and publication by the MoH of the Request for Qualification (7 August 2009) with term for submission of the requests on 15 September 2009
2009 (October):	The term for submission of the requests for qualification has been postponed to 22nd October
2009 (31 October):	Announcement of qualified bidders is expected
2010 (28 February):	Expected deadline for the submission of the bids
2010 (April):	Expected announcement of the winning consortium

Case Study: Kayseri Health Campus

Location:	Kayseri Province: 2,800,000 people
Beds:	No. 1,548 of which:
	▪ 1,048 general hospital
	▪ 200 physiotherapy and rehabilitation
	▪ 200 psychiatric hospital
	▪ 100 high security forensic psychiatric hospital
Capacity:	Expected access to healthcare services by 10,000 people per day

Case Study: Kayseri Health Campus

Type of contract:	PPP agreement based on international PPP standards (NHS, Continental Europe, etc)
Duration:	3 years construction – 25 years operation
Cost of Investment:	Estimated in approximately TL 428m (USD278m)
Tender Documentation:	As per the Regulations, a Preliminary Design developed by the Administration will be made available to the bidders in addition to the Project Agreement, relevant schedules and other technical documentation

Case Study: Kayseri Health Campus

Contract Parties:	**Ministry of Health – Project Company**
Subcontractors:	**Design and Build Contractor and Service Providers**
Services:	**Non-Clinical Services as per the Regulation, including:**
	▪ **Building and plants services and maintenance**
	▪ **Ground Maintenance**
	▪ **Security**
	▪ **Pest control service**
	▪ **Cleaning Services**
	▪ **Help Desk**
	▪ **Kitchen/Catering Services**
	▪ **Laundry/Linen Services**
	▪ **Sterilization Services**
	▪ **Waste Management and Disposal Service**
	▪ **Communication and IT (MIS and HIS)**
	▪ **Medical and non-medical equipment, including educational/training equipment**

Case Study: Kayseri Health Campus

Non-Medical Functional Area:	- **As per the Regulation activities which the Project Company can carry out within Non-Medical Functional Areas may include the following:** -**car park** -**hotel** -**bank branch** -**restaurant** -**conference and culture centre** -**internet and communication centre** -**pharmacy** -**day nursery** -**fitness and diet centre** -**taxi and transportation services**

Case Study: Al Ghubrah IWPP

- The Sultanate of Oman has transparent and tested PPP procurement strategies in the power and water sector
- DLA Piper is currently advising the Oman Power and Water Procurement Company (OPWP) in preparing a tender for the construction, operation and maintenance of a Brownfield independent water and power plant under a BOO arrangement
- The IWPP is being tendered in line with the OPWP's "7 Year Statement (2009 – 2015)" to meet the demands of <u>water</u> and <u>electricity</u> in Oman
- The IWPP will be constructed near the existing state-owned facility at Al Ghubrah and is expected to have an approximate capacity of <u>500 MW</u> and <u>30 million gallons/day</u> of desalinated water
- The aim is to maintain a transparent tendering process by not deviating substantially from the project document structure and risk allocation adopted in prior projects in Oman
- Regulation by the Authority for Electricity Regulation expected to attract potential bidders as well as banks

Case Study: Al Ghubrah IWPP

June 2008:	Feasibility Study for additional power and water desalination capabilities at the Al Ghubrah site
December 2008:	OPWP release their 7 Year Statement for meeting Oman's Power and Water requirements from 2009 through 2015
April 2009:	Advisory services contract was awarded to the consortium of Ernst & Young as financial advisors, DLA Piper as legal advisors and British Power International as technical advisors
Q1 2010:	RFP expected to go to market
Q2 2010:	Contract is expected to be awarded
2012/ 2013:	Expected Project completion (Open cycle, then combined cycle)

Key Principals for Procurement Process

Transparent and objective system	A transparent, objective and efficient process expected to create interest in the Project and increase participation of potential bidders
Minimize the process duration	Duration minimized in order to facilitate the process and ensure bidders are able to provide power in a timely manner to meet Oman's increasing demands
Tried and tested process	Use accepted, tried and tested procurement processes implemented in Oman in the past to facilitate efficient and comprehensive compliance
Maximum participation	Increased participation expected to enhance success of the bid process
Adopt relevant bid process model	Consider prior processes that present similar conditions and requirements for the Al Ghubrah IWPP

Regulation and Structure

Sector Law	The law for the regulation and privatisation of the electricity and related water sector (Sector Law of 2004) clarified the role of Government entities and opened the market to private investment and foreign ownership
Ministry Responsible for Power and Water	The Public Authority for Electricity and Water (PAEW)
Off take Entity	The Government run OPWP is the off-taker
Regulator	The Authority for Electricity Regulation (AER) was established by the Sector Law and is the independent regulator
Tried and Tested Procurement Process	Consistent policy making
	Known and agreed risk allocation
	Comfort to bidders (Oman government is not new in these type of projects)
	Clear and established contract documents
	Security (no Government guarantee required for bankability: thanks to above factors)
	Banks know and support the procurement process
	Enforcement rights

Case Study: Birmingham Highways

- DLA Piper was retained by Birmingham City Council (**BCC**) to advise on the development of its 2.6 billion pound highways maintenance and streetlighting PPP project
- EU procured project: UK as EU Member State has implemented detailed legislation governing public procurement under the Public Contracts Regulations 2006 (SI 2006 No 5) which in turn implement Directive 2004/18/EC and Directive 2004/17/EC (**2004 EU Procurement Directives**)
- UK has developed numerous standardised suites of PPP documentation to use across 17 different sectors together with guidance from UK HM Treasury for local authorities
- Procurement advice available from quasi central government advisory bodies such as Partnerships UK, the 4Ps and the Private Finance Unit:

Case Study: Birmingham Highways

Key Issues

New sector for PPP	The highways maintenance sector is emerging in England and this was only the second project of this type approved by HM Treasury. It was therefore awarded pathfinder status and DLA Piper and BCC were permitted to develop bespoke project documentation to meet the specific needs of the Project
Project Specific Risk Profile	Developing a project specific risk profile that required extensive alternations to standardised approaches in different sectors for example, insurance. Traditionally local authorities require all assets built under the PPP project to be insured against physical damage to its full reinstatement value. Physical damage insurance is not, however, available for 3,000 kilometers of road surface in any worldwide insurance market
Payment Mechanism	Availability Type payment mechanism (no demand risk): payment based on availability and maintenance outputs

Case Study: Birmingham Highways

Performance Monitoring	Very complex performance availability criteria in an urban environment, including delegation of statutory functions of the Highway Authority to a private sector provider, and the management of the highway within existing public legislation
Interactions	Liability of the private sector for claims from users of roads, interactions with other road users/developers
Current Status	This project is currently ongoing, the preferred bidder was announced this summer and the Project is expected to reach financial close in early 2010. On the basis of the experience gained in this project DLA Piper has secured instructions to act for all the other local authorities in England who have been permitted to procure highways maintenance contracts by HM Treasury – the Isle of Wight Council, Hounslow Borough Council and Sheffield City Council.

Case Study: Mafraq-Ghweifat Highway Project (Abu Dhabi)

- Firm commitment to promoting the role of the private sector in Government's and DOT's Strategic Plans for 2009-2013
- Abu Dhabi Plan 2030 and the Surface Transport Master Plan
  - AED 300+ billion expenditure on projects by 2030:
    - 590 km regional rail
    - 1,311 km freight rail
    - 130 km segregated Metro
    - 340 km tram network
    - 39 new and upgraded highway projects
    - Other water, freight, pedestrian projects
- DOT's preference for outcome-based approach
  - Availability/performance-based PPP projects
  - Performance-based maintenance contracts

Case Study: Mafraq-Ghweifat Highway Project (Abu Dhabi)

Description	327km highway between Abu Dhabi and KSA
Concessionaire Duties	Design, refurbish, expansion, operation, maintenance and finance
Estimated Cost	In excess to USD 3 billion
Concession Grantor	Abu Dhabi Department of Transport for Abu Dhabi Government
Term	In excess of 20-25 years
Construction Period	In excess of 3-4 years
Payment	Availability based monthly unitary payments ("Unitary Charge")

Case Study: Mafraq-Ghweifat Highway Project (Abu Dhabi)

- Main Project Highway components
  - Upgrade 145km to dual 3-lane carriageway
  - Upgrade 165km to dual 4-lane carriageway
  - Upgrade 20km to dual 4-lane carriageway with collector/distributor roads
  - Existing road dual 2-lane
- Total length approx. 327km
- Other components:
  - 23 interchanges
  - Culverts
  - Underpasses (pedestrian, camel and military)
  - 52 rest areas

Case Study: Mafraq-Ghweifat Highway Project (Abu Dhabi)

- DLA Piper is assisting one of the shortlisted consortia in:
  - Drafting and negotiating key project documentation, including Project Agreement and Finance Documents;
  - Due diligence report
  - Corporate structuring advice
  - Land documentation
- The consortium comprises of:
  - Macquarie Capital Group Limited
  - Abu Dhabi Commercial Bank PJSC
  - Al Jaber Transport and General Contracting LLC
  - N.V. Besix SA
  - Mouchel Middle East Limited
  - Transfield Services (International)

Case Study: Mafraq-Ghweifat Highway Project (Abu Dhabi)

Milestone	Date
Start of the Interactive Process	7 May 2009
Date by which Bidders must submit proposed amendments to project documents	2 August 2009
Last date by which Bidders may request Interactive Workshop	2 August 2009
Final date for Interactive Workshops	16 August 2009
Date before which Grantor may issue/re-issue any project documents	31 August 2009
Proposal submission (Closing Date)	December 2009
Selection of Preferred Bidder	Expected Q1 2010
Execution of Project Documents and financial close	Expected Q2 2010

Thank you

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