

THE PUBLIC-PRIVATE  
PARTNERSHIP  
LAW REVIEW

FOURTH EDITION

Editors

Bruno Werneck and Mário Saadi

THE LAWREVIEWS

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PARTNERSHIP  
LAW REVIEW

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# CONTENTS

PREFACE.....	vii
<i>Bruno Werneck and Mário Saadi</i>	
Chapter 1	ARGENTINA..... 11
<i>María Inés Corrá and Ximena Daract Laspiur</i>	
Chapter 2	AUSTRALIA..... 19
<i>Andrew Griffiths, Nicholas Carney and Lan Wei</i>	
Chapter 3	BELGIUM ..... 28
<i>Christel Van den Eynden, Frank Judo, Aurélien Vandeburie, Jan Vreys and Maurits Arnauw</i>	
Chapter 4	BRAZIL..... 43
<i>Bruno Werneck and Mário Saadi</i>	
Chapter 5	CHINA..... 58
<i>Hui Sun</i>	
Chapter 6	DENMARK..... 71
<i>Henrik Puggaard and Lene Lange</i>	
Chapter 7	FRANCE..... 82
<i>François-Guilhem Vaissier, Olivier Le Bars and Diane Houriez</i>	
Chapter 8	GERMANY..... 100
<i>Jan Bonhage and Marc Roberts</i>	
Chapter 9	IRELAND..... 110
<i>Mary Dunne and Fergal Ruane</i>	
Chapter 10	JAPAN..... 120
<i>Noriko Yao, Kiyomi Kikuchi, Kazuyuki Wakasa and Shubei Oi</i>	



## Contents

---

Chapter 11	KOREA .....	132
	<i>Soong Ki Yi, Joon Man Shim and James Jin Chung</i>	
Chapter 12	KUWAIT .....	140
	<i>Ibrahim Sattout and Akusa Batwala</i>	
Chapter 13	LEBANON .....	154
	<i>Hadi Melki</i>	
Chapter 14	MEXICO .....	162
	<i>Federico Hernandez and Julio Zugasti</i>	
Chapter 15	MOZAMBIQUE.....	172
	<i>Taciana Peão Lopes</i>	
Chapter 16	NIGERIA.....	178
	<i>Fred Onuobia and Okechukwu J Okoro</i>	
Chapter 17	PARAGUAY .....	188
	<i>Javier Maria Parquet Villagra and Karin Basiliki Ioannidis Eder</i>	
Chapter 18	PORTUGAL.....	199
	<i>Manuel Protásio, Frederico Quintela and Catarina Coimbra</i>	
Chapter 19	RUSSIA .....	211
	<i>Olga Revzina and Lola Shamirzayeva</i>	
Chapter 20	SPAIN.....	222
	<i>Manuel Vélez Fraga and Ana María Sabiote Ortiz</i>	
Chapter 21	TANZANIA.....	235
	<i>Nicholas Zervos</i>	
Chapter 22	THAILAND .....	242
	<i>Weerawong Chittmitrapap and Jirapat Thammavaranucupt</i>	
Chapter 23	UNITED KINGDOM .....	252
	<i>Mark Richards, Katherine Calder and Alexander Hadrill</i>	

*Contents*

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Chapter 24	UNITED STATES .....	271
	<i>Robert H Edwards Jr, Randall F Hafer, Mark J Riedy, Christian F Henel and Ariel I Oseasohn</i>	
Chapter 25	VIETNAM .....	287
	<i>Kazuhide Ohya, Vu Le Bang and Nguyen Van Trang</i>	
Appendix 1	ABOUT THE AUTHORS .....	301
Appendix 2	CONTRIBUTING LAW FIRMS' CONTACT DETAILS.....	321

# PREFACE

We are very pleased to present the fourth edition of *The Public-Private Partnership Law Review*. Notwithstanding the number of chapters in various publications in *The Law Reviews* series on topics involving public-private partnerships (PPPs) and private finance initiatives (in areas such as projects and construction, real estate, mergers, transfers of concessionaires' corporate control, special purpose vehicles and government procurement), we identified the need for a deeper understanding of the specific issues related to this topic in different countries.

In 2014, Brazil marked the 10th year of the publication of its first Public-Private Partnership Law (Federal Law No. 11,079/2004). Our experience with this law is still developing, especially in comparison with other countries where discussions on PPP models and the need to attract private investment in large projects dates from the 1980s and 1990s.

This is the case for countries such as the United Kingdom and the United States. PPPs have been used in the United States across a wide range of sectors in various forms for more than 30 years. From 1986 to 2012, approximately 700 PPP projects reached financial closure. The UK is widely known as one of the pioneers of the PPP model; Margaret Thatcher's governments in the 1980s embarked on an extensive privatisation programme of publicly owned utilities, including telecoms, gas, electricity, water and waste, airports, and railways. The Private Finance Initiative was launched in the United Kingdom in 1992, aiming to boost design-build-finance-operate projects.

In certain developing countries, PPP laws are more recent than the Brazilian PPP law. Argentina was the first country in Latin America to enact a PPP Law (Decree No. 1,299/2000, ratified by Law No. 25,414/2000). The Argentinian PPP Law was designed to promote private investment in public infrastructure projects that could not be afforded exclusively by the state, especially in the areas of health, education, justice, transportation, construction of airport facilities, highways and investments in local security. In Mozambique, Law No. 15/2011 and Decree No. 16/2012 govern the Public-Private Partnerships Law and other related PPP regulations, which establish procedures for contracting, implementing and monitoring PPP projects. In Paraguay, a regulation establishing the PPP regime has been enacted (Law No. 5,102) to promote public infrastructure and the expansion and improvement of services provided by the state; this law has been in force since late 2013.

In view of the foregoing, we hope a comparative study covering practical aspects and different perspectives regarding PPP issues will become an important tool for the strengthening of this model worldwide. We are certain this study will bring about a better dissemination of best practices implemented by private professionals and government authorities working on PPP projects around the world.

With respect to Brazil, the experience evidenced abroad may lead to the strengthening of this model in our country. In our last preface, we called your attention to one specific

feature of the PPP law in Brazil: state guarantees. This feature permits that the obligation of the public party to pay a concessionaire be guaranteed by, among other mechanisms authorised by law: (1) a pledge of revenues; (2) creation or use of special funds; (3) purchase of a guarantee from insurance companies that are not under public control; (4) guarantees by international organisations or financial institutions not controlled by any government authority; or (5) guarantees by guarantor funds or state-owned companies created especially for that purpose.

The state guarantee pursuant to PPP agreements is an important innovation in administrative agreements in Brazil; it assures payment obligations by the public partner and serves as a guarantee in the event of lawsuits and claims against the government. This tool is one of the main factors distinguishing the legal regimen of PPP agreements from ordinary administrative agreements or concessions – one that is viewed as crucial for the success of PPPs, especially from a private investor's standpoint.

Nevertheless, the difficulty in implementing state guarantees on PPP projects has been one of the main issues in the execution of new PPP projects in the country. This is made worse by the history of government default in administrative contracts.

In other jurisdictions, however, state guarantees are not a rule. Unlike PPP projects in developing countries, government solvency has not historically been a serious consideration in other jurisdictions. That is the case in countries such as Australia, France, Ireland, Japan, the United Kingdom and the United States.

We expect that the consolidation of PPPs and the strengthening of the government in Brazil may lead to a similar model, enabling private investments in areas where the country lacks the most.

Brazil must adopt cutting-edge models for awarding PPP agreements. The winner is usually chosen based solely on the price criterion (offering of lower prices or highest offers), which sometimes leads to projects lacking advanced or tailor-made solutions. Despite the legal provisions on the role of technical evaluation of offers, they are becoming less relevant. However, some ongoing discussions regarding amendments to the Brazilian procurement legislation and new criteria, which are based on the international experience, could (fortunately) be approved.

In last year's edition, we highlighted some discussions regarding the amendment to the Federal Procurement Law (Federal Law No. 8,666/1993), which is expected to expedite public procurement in Brazil. One of the main innovations proposed in this debate is the competitive dialogue, a type of bid in which the authority engages with bidders to discuss and develop one or more solutions for the tendered project. After the conclusion of the dialogue phase, the authority will establish a term for the submission of bids.

The competitive dialogue is a reality in many jurisdictions (e.g., Australia, Belgium, China, France, Ireland, Japan and the United Kingdom). In Japan, for example, some projects are procured through the competitive dialogue process. This process may be adopted if a relevant authority is unable to prepare a proper service requirement, in which case it proposes a dialogue with multiple bidders simultaneously to learn more about the specific service it seeks to implement. As another example, in France a dialogue will be conducted with each bidder to define solutions on the basis of the functional programme. At the end of the dialogue period, the procuring authority will invite the candidates to submit a tender based on the considered solutions. After analysis of the tenders, a partnership contract will be awarded to the bidder with the best price in accordance with the criteria established in the

contract notice or in the tender procedure. We hope the importance of this tool is recognised in Brazil and reflected in our legislation.

In this edition, we wish to call your attention to the creation of the Investment Partnerships Program, as established in Federal Law No. 13,334/2016. The Investment Partnerships Program is a legal plan regarding infrastructure development in the country, providing conditions for the attraction of investments in infrastructure projects and creating environments for greater integration between public and private sectors. According to information recently released by the federal government, PPI figures are impressive, particularly concerning the total value of projects that have been concluded: 142 billion reais. The expectation is that investments of this size will bring more employment and income in the coming years, ensuring the continuation of Brazil's development.<sup>1</sup>

In the fourth edition of this book, our contributors were drawn from the most renowned firms working in the PPP field in their jurisdictions. We would like to thank all of them for their support in producing *The Public-Private Partnership Law Review*, and in helping with the collective construction of a broad study on the main aspects of PPP projects.

We strongly believe that PPPs are an important tool for generating investments (and development) in infrastructure projects and creating efficiency not only in infrastructure, but also in the provision of public services, such as education and health, as well as public lighting services and prisons. PPPs are also an important means of combating corruption, which is common in the old and inefficient model of direct state procurement of projects.

We hope you enjoy this fourth edition of *The Public-Private Partnership Law Review* and we sincerely hope that this book will consolidate a comprehensive international guide to the anatomy of PPPs.

We also look forward to hearing your thoughts on this edition, and particularly your comments and suggestions for improving future editions of this work.

**Bruno Werneck and Mário Saadi**

Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados

São Paulo

March 2018

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1 Information available online: <http://www.avancarparcerias.gov.br/-lquote;avancar-parcerias-rsquo;-concrete-results-and-retake-of-economic-growth-?PortalMessage=Status+Alterado>.

# SPAIN

*Manuel Vélez Fraga and Ana María Sabiote Ortiz<sup>1</sup>*

## I OVERVIEW

According to the Spanish National Association of Construction Companies, between 2003 and 2011, Spain generated over 500 public-private partnership (PPP) transactions worth approximately €50 billion. However, since 2012, the PPP market fell to 2005 levels mainly as a result of budget cuts by the Spanish governments. The economic crisis and changes in financial markets affected ongoing PPP projects, those under construction and those recently awarded.

In view of the budget restrictions and the tight levels of public debt, PPP projects are an opportunity to foster investment in public infrastructures as the financing is mainly assumed by the sponsor and the public expense is prorated along the project life. In short, PPP can help the authorities overcome short-term budget constraints by making the most of the PPP advantages available, such as whole-life cost management and payment tied to service delivery, not asset provision.

There is a general conviction that infrastructure development contributes towards economic growth, and privately financed PPPs could be an option to deliver key infrastructure as they limit short-term pressure on both debt and deficit.

According to a report by A T Kearney regarding priority areas for sustainable investment in infrastructures in Spain, the country is in a good position with regard to certain infrastructures (namely high-capacity roads, high-speed railways, airports and ports), but it has deficiencies in the maintenance of current infrastructures, the transport of goods, accessibility and urban mobility, as well as secondary nets. In its analysis, A T Kearney recommends investment in eight priority areas: water, energy, social care, transport, environment, IT, urbanism (smart cities, mobility and urban integration) and infrastructure maintenance. PPP schemes are a way of obtaining that investment in view of the limited public funds.

The beginning of the recovery of the Spanish economy together with the strengthened conception of PPP projects as the opportunity to foster investment in public infrastructures is contributing to initiate a new stage of the public investment in Spain through PPP schemes after the crisis period.

## II THE YEAR IN REVIEW

After the deadlocks in the Spanish elections during 2016, the formation of the Spanish government at the end of 2016 and the beginning of the recovery of the economy has

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<sup>1</sup> Manuel Vélez Fraga is a partner and Ana María Sabiote Ortiz is an associate at Uría Menéndez.

contributed to boosting new actions in public investments at the national level. During 2017, the Spanish Infrastructure Ministry announced the approval of several investment plans, mainly in roads, that will be articulated through PPP schemes throughout 2018.

In 2017, a new bill on public sector contracts was enacted (Law 9/2017 of 8 November). The new bill transposes into Spanish law both Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement, and repeal Directive 2004/18/EC and Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts. The new bill will come into force on 9 March 2018.

The political situation in the region of Catalonia has also played a significant role in the whole Spanish market, mainly during the last quarter of 2017. After the measures adopted by the Spanish government, and regional elections last December, the general atmosphere seems to have started to calm down, and the next few months will be key in clarifying the current period.

### III GENERAL FRAMEWORK

#### i Types of public-private partnership

In the Spanish market, PPP is not a legal concept strictly speaking, but a type of public policy or management method that entails collaboration between a public entity and a private partner. This collaboration aims to implement, finance and manage public infrastructures in broad terms, including facilities, services and utilities. This clarification serves to avoid misidentifying PPP in general, with a specific and single contract form under the Spanish Public Procurement Law.

Under the Spanish Public Procurement Law currently in force,<sup>2</sup> there are three main types of PPP contracts: (1) public works concession contracts; (2) public service management contracts; and (3) partnership agreements between the public and the private sector. The new Law on public sector contracts (Law 9/2017) that will come into force on 9 March 2018 will repeal the Spanish Public Procurement Law.

#### *Public works concession contracts*

Traditionally, public works concession contracts are conceived under Spanish law as a contract under which the concessionaire develops a public works project and is remunerated for it through the right to operate the project (by collecting a fee or toll from users), at its own risk, during the term of the concession.

This type of contract is the most commonly used in practice for new categories of projects such as: (1) projects that require the involvement of the private contractor in defining the project; (2) projects in which the contractor does not manage the public infrastructure or facility directly for private individuals, but for the public entity, which uses the infrastructure as a physical base for the provision of public services to citizens, which are provided by the public authority itself (using its own resources); and (3) projects in which the contractor is not remunerated directly by users, but by the public entity (either based on the number of

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2 Namely, Royal Legislative Decree 3/2011 of 14 November approving the Consolidated Public Sector Contracts Law.

users using the infrastructure (payment for demand) or on the conditions under which it is made available to the public authority (payment for availability)). This type of contract keeps its main characteristics under the new Law on public sector contracts.

This broad concept of public works concession is firmly accepted under Spanish law. Currently, public works concession contracts can be executed for the following reasons according to Spanish law:

- a* the concessionaire may also be in charge of preparing the relevant project, on the basis of the preliminary plan or study approved by the contracting government department;
- b* the purpose of the public works concession contract includes not only the construction of new infrastructure, but also the renovation and repair of existing constructions, as well as the preservation and maintenance of the constructed elements. This broadens the potential use of this contract, which can now cover not only new infrastructures but also the operation of existing ones that require a significant investment with regard to renovation or maintenance; and
- c* they also include agreements under which the concessionaire uses the public infrastructure to make it available to the public entity (or to an indirect operator), so that it can use it to provide a public service. In this case, use consists of operating the infrastructure. The operation must be undertaken in accordance with its particular nature and purpose. Since the concession involves a public infrastructure, its nature determines that it must be established as an instrumental support to perform different activities and services of public interest, or for general use or enjoyment, in exchange for remuneration fixed through one of the mechanisms provided by law.

### ***Public service management contracts***

The public service management contract is an agreement under which the public entity entrusts a third party to manage a public service on its behalf. The standard public service management contract is generally classified as follows:<sup>3</sup>

- a* Public service management concession. A contract under which the public authority – responsible for a public service – awards the management of such service to a private entity to operate it at its own risk. The private entity may be paid by the users, the public entity or both.
- b* Special agreement. This is another subcategory of the public service management contract. It is characterised by the fact that the public entity awards the management of the service to an individual or legal entity that already provides similar services to the relevant public service. It is common in the education and health sectors.
- c* Public service management by a semi-public company. The semi-public company is a type of institutionalised PPP under which a company is incorporated through a contract between private and public capital, to then become a public contractor with the characteristic rights and obligations of a concessionaire. Semi-public companies have a long tradition under Spanish law in managing local public services.

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3 The new draft bill on public procurement being prepared by the Spanish parliament envisages important changes to the public service management contract. According to the current draft, the public service management contract will be mainly to reduce the public service concession, although certain forms of the traditional public service management contract remain for local entities. This issue must be further analysed in view of the final bill.



- d* There is also a fourth subcategory of public service management contract under the Spanish Public Procurement Law: stakeholder management, under which the public entity and the company share the operating profits of the service in the proportion agreed in the contract.

The new Law on public sector contracts has widely modified these categories. Under the new Law, only the type of contract 'service concession' remains as a PPP scheme for public services. The special agreement, the public service management by a semi-public company and stakeholder management disappear as general schemes (although the semi-public company can still be used by local entities under certain circumstances, and special agreements are still feasible under sectorial regulations). The service concession differentiates from the simple service contract in the risk assumed by the contractor. Whenever there is a transfer of the operation risk to the contractor, the Law considers it as a concession agreement. On the contract, if there is no a transfer of risk, the contract will be considered a service agreement, not a concession one.

### ***Partnership agreements between the public and the private sector***

Partnership agreements between the public and private sector were implemented in Spain in 2007.

The main characteristics of this partnership agreement are the combination of two elements:

- a* the execution by the contractor of a complex operation, which includes one or more of the following activities: (1) the execution of complex works, equipment, systems and utilities, as well as the maintenance, updating or integrated operation; (2) the integrated management of complex facilities; and (3) the provision of other complex services associated with the public authority's performance of its specific responsibilities; and
- b* the initial financing by the contractor of the tangible or intangible investments required for the services that constitute the first of the elements.

Very few examples of this type of contract can be found in practice at national, regional or local level. Some examples can be found in areas such as energy efficiency. In general, public entities have seldom used partnership agreements between the public and private sector.

The new Law on public sector contracts eliminates this type of agreement.

## **ii The authorities**

Spain is a regional state, which means it is a decentralised state formed of 17 regions with their own regional authorities. In addition to the national and regional governments, the Spanish Constitution gives local authorities some administrative authority.

Therefore, Spanish authorities are mainly arranged at three institutional levels: national government and its corresponding public entities, regional governments and their corresponding public entities, and local governments and their corresponding public entities.

The three levels have different but concurrent and coordinated powers. Each authority level can exercise these powers through PPP projects. For instance, the national government has authority over transport and can exercise its powers through PPP on transport infrastructures. Regional governments have authority over health and social care and may

develop hospital infrastructures through PPP. Local governments have authority over local services such as water and waste collection, and may implement these services through PPP projects.

Any department of public authority on one of these three levels may enter into PPP contracts in their specific field. For instance, the Environment Department may call a procedure for the construction of water infrastructures under a PPP project. However, at national level, there are two main ministries involved in PPP projects: the Ministry of Infrastructure, as it has authority over all transports involving public works; and the Ministry of Finance and Public Administration, which administers the state budget and expenses – an important role because of public debt restrictions – and analyses the impact of PPP projects on public accounting.

There is currently no specific authority in charge of PPP projects in Spain. In October 2015, the national government created the National Evaluation Office to improve the quality of the investments made by public authorities. The National Office assesses the feasibility of public projects under public contracts, taking into account the rules governing budgetary balance. The National Office may also assist regional and local governments. However, the ruling officially implementing this National Office has not yet been issued, thus it is not yet operative, and, for now, is not regulated by law as a real PPP unit to foster PPP benefits or collect and improve PPP practices. Additionally, the new Law on Public Sector Contracts creates the Public Contracts Cooperation Committee and the Public Contracts Supervision Office. Both organisms intend to supervise the public entities' practice regarding contracts and coordinate interpretation criteria.

Apart from the national, regional and local authorities, there are other public entities mainly governed by private law, such as the Railway Infrastructure Administrator, or the Port Authorities. These entities often enter into contracts to construct and operate public infrastructures and facilities that include some of the characteristics set out for the types of PPP contracts described in Section III.i above. However, although their names and legal frameworks may coincide, totally or in part, with the provisions for PPP contracts governed by the Public Procurement Law, the effects and termination of these contracts are governed by private law. The general regime for PPP described in this chapter only applies to contracts entered into by other public entities when such entities so decide in the contract in question.

### **iii General requirements for PPP contracts**

Public authorities must meet a series of internal requirements and approvals to enter into a specific PPP contract. Mainly, public authorities must evidence the need for which the PPP is to be executed and prove the advantages of using a PPP contract to cover that need over other types of contracts, or over the public authority implementing it directly. In addition, the public entity must make sure that there are sufficient funds to pay for the PPP contract before calling a public tender under a specific procedure. Likewise, the new National Evaluation Office must analyse the financial sustainability of the public works and public service, for example, whenever the price will be assumed totally or partially by the contracting authorities, not by the users.

In addition, prior to calling the public tender, the contracting authority must undertake to carry out a feasibility study that analyses the economic-financial basis for the contract. This study must provide an estimate of use demands and profitability of the contract, operational

and technological risks in the construction and operation phases, as well as an estimate of investment costs and the potential financing system to perform the work. This feasibility study constitutes the value-for-money assessment by the public authority.

Once the feasibility study has been prepared, and at all times prior to calling the public tender, the contracting authority must prepare the administrative and technical bidding terms that will govern the relationship with the awardee. These terms must be approved by the legal and technical advisers of the contracting body.

Once the internal requirements have been met and the bidding terms have been approved, the public entity can start the tender procedure.

Public works and public services concessions are subject to temporal limits established by law. Therefore, the term of the contract must be justified in the contract itself, taking into account the need to be satisfied and the recovery of the investment, but at all times in accordance with statutory limits, which, under the new Law on Public Sector Contracts are: (1) 40 years for public work concessions and for service concessions that include works; (2) 25 years for service concessions not including health services; or (3) 10 years if the service concession refers to healthcare services with no construction works.

In principle, there are no other general restrictions on the use of PPP to cover a public need. In any case, the services that involve exercising public powers cannot be managed by third parties and therefore cannot be entrusted to a contractor through a PPP project. They must be exercised by the public authority directly.

#### **IV BIDDING AND AWARD PROCEDURE**

The Public Procurement Law mainly regulates four types of procedures to select and award the contracts included under the PPP category (see Section III.i, above): open procedure, restricted procedure, negotiated procedure (with and without publicity), competitive dialogue and, under the new Law, association for innovation.

The open and the restricted procedures are called ordinary procedures because they can generally be used by the contracting authorities. Negotiated and competitive dialogue as well as association for innovation procedures can only be used under certain circumstances, such as if the matter is especially complex, in the case of competitive dialogue, or if the preliminary open or restricted procedure has been declared null, in the case of negotiated procedure.

In practice, the two main PPP contracts (public works and public service concessions) are awarded through open procedures, and rarely through restricted procedures. The preference for open procedures is because of the restrictions existing for using other procedures, the higher complexity of the other procedures and the aim of allowing as many participants as possible.

The open procedure results in mainly standardised PPP contracts, as the rights and obligations under the contract are mainly governed by standardised administrative and bidding terms. The bidding terms are not negotiable so they cannot be modified by the tenderers.

Our observations in the following subsections refer to the two most commonly used procedures (open and restricted) in PPP contracting in Spain.

##### **i Expressions of interest**

The Public Procurement Law used to not provide specific procedure for the awarding body to request information from interested parties. However, this request and assessment of interest

can be channelled through the public hearings in preparing the PPP contract: in particular, the public hearing of the feasibility study, which must last a minimum of one month, and the public hearing that may take place in certain complex public projects regarding the construction project. Under article 115 of the new Law on Public Contracts, the contracting authorities may undertake market studies and consultancies to the operators to correctly define the necessities to be covered in the future contract and inform the operators of the future contracting plans and the requirements to be complied with. The law does not prevent public entities from organising other hearings or consultations to obtain feedback from the market before calling a public tender.

Additionally, according to Spanish law, private third parties may submit feasibility studies on themselves in order to invite the public entity to cover a specific need through a public concession. Once the feasibility study has been submitted, the authority decides whether to proceed. If a public tender is called following a feasibility study, and the contract is awarded to another private party, the promoter of the feasibility study must be compensated for the expenses it incurred to promote such study plus 5 per cent. Despite this legal provision, private initiative in submitting feasibility studies has been practically non-existent in Spain. The new Law on Public Contracts adds that the promoter will obtain five extra points during the awarding procedure. If the promoter is not finally the awardee, the general compensation applies.

## **ii Requests for proposals and unsolicited proposals**

Once the public entities approve the file to enter into a specific PPP, they can launch the public tender procedure. The procedure starts with an advertisement in the Official State Gazette and the Official Journal of the European Union, or in the Official Gazette of the autonomous community or municipality in question. This advertisement is particularly important because it is the start of the term to submit offers.

Under the open procedure, any third party may submit an offer. Submitting an offer implies the unconditional acceptance of the bidding terms, and the terms of the contract cannot be negotiated.

Between the call and the submission of offers, any interested party may request clarifications from the awarding authority. The queries made and answers provided during this phase must be generally available to all interested parties.

Unlike the open procedure, the restricted procedure is structured in two phases, during which a shortlist of offers is made. The existence of a preliminary selection phase means that, when preparing the contract (before its tendering), the contracting body defines the objective criteria of solvency in accordance with which it will choose the candidates (generally no fewer than five) that it will invite to submit proposals. These criteria are available from the moment the tender is announced. Only the pre-selected candidates may submit proposals.

## **iii Assessment of the offer and granting of the award**

Beyond the preliminary contract preparation phase during which the content of the contract is defined, its content cannot be altered or specified by negotiation under either the open procedure or the restricted procedure. Submitting a proposal entails that the tenderer accepts the bidding terms in full.

Once the proposals have been filed, the Public Procurement Law establishes the procedure to open and analyse the proposals under transparency and parity criteria. The awarding criteria in PPP projects usually include both economic and technical assessment

and must be previously defined in the bidding terms in accordance with the purpose of the contract. The criteria that cannot be assessed using an automatic formula will be scored before those subject to automatic criteria to ensure parity.

The contract will be awarded to the bidder with the highest score, and will come into force once both parties enter into the formal agreement. This formal agreement is usually short and merely restates the main obligations that are defined in the bidding terms and the bidder's proposal.

## **V THE CONTRACT**

### **i Payment**

The standard two methods of payment are suitable for PPP projects: by the contracting authority itself or by the users. However, payment can also be a combination of both methods. Therefore, the difference between the types of PPP contracts does not depend on who pays for the service provided by the sponsor. Direct payment by the users is usually regulated and capped by the contracting authority.

Likewise, payments made by the public entity may depend on the demand or level of use of the infrastructures (as in the case of shadow tolls), or on the availability of the infrastructure for the public entity measured in view of certain service standards or indicators.

There has been some debate over whether payment based on the availability of the public infrastructure to the public entity (payment for availability) is compatible with the existence of a risk for the concessionaire. Whenever the formulas for availability are defined in a clearly aggressive way to ensure that the concessionaire actually assumes the effects of inadequate performance of the contract, it can be said that the concessionaire assumes a real risk.

In practice, the misgivings regarding payment for availability have been precisely owing to the establishment of insufficiently sensitive parameters of availability, which, as a result, significantly reduce the risk for the concessionaire.

The remuneration resulting from the operation of the infrastructure may be accompanied by a price paid by the public entity, and by other public contributions to the construction and operation of the infrastructure, making the system of concessionaire remuneration quite flexible.

### **ii State guarantees**

Traditionally, public entities have been considered trustworthy and guarantees have not been required to secure payment. Because of the recent economic crisis, some public entities have had payment problems. This situation has been addressed by tightening the regulations to control public expenses and investments. Likewise, the state has implemented measures to support regional and local authorities in their obligations, but the Public Procurement Law has not been modified to introduce a scheme of guarantees to ensure payments by public contractors. The amendments have focused on a stricter control of the existence of funds and the economic feasibility of the contract before it is executed.

In connection with the above, the Public Procurement Law has been amended to introduce the following limits to public contributions and securities: (1) public contributions and any type of security, guarantee and other measures to finance the project must necessarily be stipulated in the bidding terms and their amount must be determined in the award procedure. This amendment does away with the possibility of contributions being made at

the end of the concession and the contribution being increased after the award resolution; (2) bidders will determine the exact amount of public contributions in their offers within the maximums established in the bidding terms; and (3) the bidding terms must state any reduction of the public contributions as an evaluation criterion for awarding the contract.

### **iii Distribution of risk**

A key element in public concessions is the construction and operation of infrastructures by the concessionaire at its own risk. According to this principle, the concessionaire must assume the consequences, in financial terms, that may arise from performing the contract.

Under Spanish law, the principle that the contractor assumes its own risk is compatible with the guarantee to restore the financial-economic balance when the contract's economic imbalance is caused by the public authorities, either by exercising their prerogative to modify the contract, or because of decisions of the contracting administration or other public authorities (including regulatory risk in general).

The risk principle is also compatible with restoring the concession's economic balance when that balance is disrupted by risks unrelated to actions not only of the concessionaire, but also of the public authorities. This is the case of force majeure events and unexpected risk. The Public Procurement Law expressly regulates the former. If force majeure has a significant disruptive effect on the economic side of the contract, it gives rise to a right to restore its economic balance and, if the contract can no longer be performed, to its termination in such a way that the recovery of the concessionaire's investment is guaranteed. However, the concept of force majeure under Spanish law is applied very restrictively and has traditionally been complemented with the concept of 'unexpected risk'. Under unexpected risk, economic imbalances arising during the performance of a contract as a result of the emergence of a risk that could not have been foreseen when the contract was executed can be corrected. This is the case if the risk in question significantly disrupts the conditions to perform the contract, to the extent that providing the agreed service has become much more burdensome than anticipated for one of the parties. Although the doctrine of unexpected risk is currently quite prevalent, it is not actually referred to in legislation.

In addition to those described above, there is another group of risks that must be determined in the bidding terms as it is not established by either legislation or case law.

In the specific case of financing, the risk known as financial closure risk is particularly important. This risk is assumed by the concessionaire and worsens in times of credit market crisis.

Financial closure risk can be defined as the fluctuation in the cost of financing required by the concessionaire to perform the contract, from the time the bid is awarded to the time when the financing is definitively confirmed after being awarded the contract. Generally, unless the bidding terms state otherwise, the tenderers assume the financial closure risk, in such a way that any differences between the financing conditions foreseen when the bid is submitted and the conditions secured when the financing is finalised after the contract is awarded, are assumed by the tenderer, who is not allowed to pass on a higher financing cost than that offered in the financial-economic plan. In practice, the tenderers have attempted to cover this risk by negotiating derivatives of the main financing contract in order to cover exchange and interest rates. However, the coverage only comes into effect once the contract is awarded, and thus, until then, the risk continues to be assumed entirely by the tenderer.

#### **iv Adjustment and revision**

Public authorities have special prerogatives over the contractor, basically consisting of the power to: (1) construe the terms and conditions of the contract; (2) unilaterally modify the contract for public interest reasons; (3) impose penalties; and (4) unilaterally terminate the contract under certain circumstances set out by law and in the contract, and establish the effects of this termination.

Therefore, according to these prerogatives, the contracting authority will retain its right to modify aspects of the contract for new and compelling public interest reasons, provided that the contractor is paid compensation. This legal prerogative can be challenged in court when it does not fulfil the relevant mandatory provisions.

The grantor modifying the concession is one of the events that triggers the contractor's right to rebalance the financial terms of a contract, provided that the amendment affects the economic balance of the contract when it was awarded to the detriment of the concessionaire (beyond a mere reduction in the expected profits). The concessionaire can request the grantor to rebalance the financial situation by evidencing the unbalancing event and its actual effects on the existing financial plan approved as part of the contract. The rebalancing can be implemented by modifying any financial condition of the contract. The terms of the tender may limit when this financial rebalancing can be done.

The compensation to the concessionaire must be paid within the term set out in the bidding terms, which must not exceed the maximum legal term established by law, which is currently 30 days following the grantor's approval of the service rendered. Late payment triggers default interest. When late payment exceeds a joint period, the contractor may suspend the contract, or even request its termination as explained in Section V.vi below.

The review or update of the compensation under public contracts also depends on the bidding terms that cannot be contrary to the legal requirements. The review of the price in public contracts has recently been modified by Law 2/2015 of 30 March and further implemented for public contracts by Royal Decree 55/2017 of 3 February. Under these new regulations, the review can only take place when the investment return exceeds five years, and subject to the strict conditions set out in the regulations.

#### **v Ownership of underlying assets**

Assets in PPP contracts are owned by the public authority. Because of its connection to a public work or service, the public entity does not lose its right *in rem* over the assets during the contract, but the concessionaire is empowered to use them for the proper rendering of the service or the operation of the public works. At the end of concession contracts, the facilities must be returned to the grantor in adequate working condition to continue providing the services. To this end, the grantor may inspect the facilities to make sure that the grantor is complying with its obligations under the contracts.

Empowerment to use the assets to properly render the service or operation of the public works implies that the contractor can dispose of the assets with the assistance of the public entity, when necessary, to that end, and that the contractor may mortgage the concession itself in accordance with the mortgage legislation, and with the prior authorisation of the contracting authority. The mortgage cannot be used to secure obligations under contracts other than the relevant PPP.

According to the Public Procurement Law, the contract itself cannot be assigned without the grantor's prior authorisation. Spanish public procurement law has traditionally regulated the assignment of the contract. When the contract is silent, the transfer of the

contractor's shares does not require the grantor's prior authorisation, except when the transfer may be considered equivalent to assigning the contract. Transferring shares may be considered an assignment when it only relates to a company whose sole object is to operate public concessions and the transfer of shares entails a change in the person who controls the holder of the concession.

#### **vi Early termination**

The public authority can terminate the concession early under certain circumstances set out by law and in the contract, and establish the effects of this termination. The effects (compensation) of early termination vary depending on the specific termination event.

The Public Procurement Law currently establishes the following main early termination events for public concessions:

- a* the concessionaire loses its legal personality;
- b* the contractor enters into a creditors' agreement or files for insolvency;
- c* foreclosing the concession mortgage is unfeasible;
- d* mutual agreement between the public authority and the contractor;
- e* the concession has been seized by the authority for longer than the agreed maximum term;
- f* payment delays by the public authority for over six months;
- g* the contract is revoked by the public authorities at their discretion (this unilateral termination is not connected to the concessionaire's management);
- h* the exploitation of the public infrastructure or the public service is cancelled for public interest reasons;
- i* the infrastructure cannot be operated because of the contracting authority's decisions after the contract was executed; or
- j* the concessionaire fails to comply with essential contractual obligations.

If the concession is terminated for public interest reasons, adequate compensation must be paid. According to case law, 'public interest' is an abstract notion that can only be determined and defined on a case-by-case basis and taking into account the characteristics and circumstances of a particular contract as a whole, such as its subject matter, purpose and nature. The grantor must justify its decision on public interest reasons, which can be challenged in court.

Among other consequences, rights arising for the contractor from an early termination event include the equity value of the investment, usually, albeit inappropriately, referred to as the pecuniary liability of the public authority (RPA).

The method of calculating RPA was modified in 2015. Following the modification of 2015, the provisions on RPA distinguish two calculation methods: (1) for cases involving a termination not attributable to the public authority, the RPA is determined in a new award process for the concession; and (2) in cases of termination not attributable to the concessionaire, the regulation on compensation for investments is similar, but specifies that straight-line depreciation will be used.

Termination is not automatic. The contracting authority must undergo a procedure in which the concessionaire is heard.



## VI FINANCE

The private funds involved in a PPP project may come from two sources: tenderers (usually as capital of the special purpose vehicle responsible for carrying out the project) or third-party financiers.

Financing PPP contracts in Spain usually follows the traditional scheme of bank financing. This scheme relies chiefly on pledges, and, in some cases, assignment to the financier of both the credit rights arising from the normal operation of the infrastructure (periodic cash inflows from the operation of the public works or services) and the credit rights arising from the early termination of the contract (the equity value of the investment or RPA, as explained above).

The financing is normally granted in the form of credit, which the concessionaire can obtain upon completing the project phases. The syndication mechanism is a response to the need to distribute the operating risks when they are too high to be assumed by a single entity. In the past few years we have seen growth in particular of uninsured or 'club deal' syndicated loans, under which each institution of the syndicate guarantees only its share, as opposed to other types where one or more institutions undertake to contribute all of the financing if they are unable to find enough institutions that wish to participate in the financing project.

Syndication of financing involves the execution of a contract by creditors including all the institutions in the syndicate that regulates, among other matters, the majorities required to adopt decisions related to financing and the rules to distribute the amounts obtained from the concessionaire company. Unless other debt and creditors' seniority is established, loan repayments are usually distributed in proportion to each institution's share in the financing.

To facilitate the operational management of the financing, one of the financial institutions assumes the role of agent bank. As such, it is responsible for delivering the funds to the company, distributing the repayments among all the financial institutions and channelling communications in each direction.

Given that the tendering procedure generally adopted to award concessions is a standardised one (open or restricted), negotiations with financial institutions begin in the phase prior to the contract, since the tenderer has to include the main characteristics of the financing that it will be able to secure in its financial bid. However, credit negotiations are only finalised *a posteriori*, once the tenderer is awarded the contract. At this time, the concessionaire's negotiating position is very much influenced by the urgency of the financing to fulfil the contractual obligations it has assumed with regard to the public authority. Moreover, the added cost with which the financing may be finally secured will generally, but not always, be assumed by the concessionaire, who has little chance of passing it on to the public authority.

Guarantees play a fundamental role in bank financing. In fact, the granting of financing is generally conditional upon the prior or simultaneous granting of guarantees over the different assets, goods and rights that constitute the equity of the concessionaire company.

On the other hand, the Public Procurement Law expressly regulates the issue of bonds by concessionaires, as well as the securitisation of credit rights arising from the concession. Given that the concessionaire generally has no revenue other than these credit rights, the bonds and securities that could potentially be issued would essentially be those resulting from securitisation. The issue of these securities will require prior administrative authorisation from the contracting authority, which can only be denied if this is justified by the successful outcome of the concession or another factor of public interest.

## **VII RECENT DECISIONS**

The main recent relevant jurisprudence relating to PPP has concerned public concessions for the construction and operation of ring roads in Madrid. However, this jurisprudence, mainly related to expropriation costs and calculation of damages for early termination events, varies depending on the specific circumstances of the case at stake and is limited to exceptional circumstances that may not apply on a general basis. There has not been an established line of jurisprudence to strengthen or weaken the PPP model, which is a popular scheme in Spain, through the concession model.

## **VIII OUTLOOK**

Traditionally, investing in infrastructure has contributed to fostering the economy through the improvement of the country's competitiveness and citizens' welfare. Despite the high level of transport infrastructures (see Section I, above), there is still a significant investment deficit in Spain in other priority sectors such as infrastructure maintenance, transportation of goods, social care (health and education) and water, compared with other European countries.

Alternative financing schemes are required because of public budget restrictions. In this scenario, PPPs are a perfect channel for private investment in infrastructures. This situation, together with the acceptance of the PPP model in Spain, the existence of brownfield opportunities and a new full political cycle ahead, provides an ideal setting for PPP projects in Spain in the coming years. Accordingly, the national government has announced the approval of several investment plans, mainly in roads. These new plans will be articulated through PPP schemes throughout 2018, as is the case for the public procurement to award the new concessions for the exploitation of the toll roads recovered by the national government expected for the second half of 2018 (the Extraordinary Road Investment Plan).

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