UNICE
Union of Industrial and Employers' Confederations of Europe
Union des Confédérations de l'Industrie et des Employeurs d'Europe

50/3corr. **23 June 1999**

PUBLIC PRIVATE PARTNERSHIPS

Comments by UNICE's "Public Procurement" Working Group

1. There is a growing use of Public Private Partnerships across Europe. PPPs are being developed in a range of ways and for a range of purposes. Increasingly, governments are keen to secure private sector involvement in some or all of the design, financing and operation of services, infrastructure and utilities. The introduction of private sector skill and capital is helping to boost overall capital and service provision, by generating value for money savings and creating new sources of capital finance. There are substantial benefits in terms of keeping public spending under control while improving public service delivery, alongside boosting European competitiveness.

2. UNICE welcomes the priority the Commission attaches to updating the EC Public Procurement framework so as to facilitate public private partnerships. We agree that there is some uncertainty over the application of the current legal framework and we believe that some changes to the law are needed.

3. UNICE supports the Commission's approach of issuing a draft communication for genuine consultation. It is extremely useful to have sight of the Commission thinking across an extremely wide canvass of issues and circumstances.

4. Undoubtedly debate is complex. One indication of that is the lack of common legal terminology to describe or label the various purchasing and contracting models that are developing. Terms such as outsourcing, sub-contracting, Private Finance Initiative, concessions and joint ventures have various meanings and connotations. Public Private Partnerships (PPP) seems to be increasingly accepted across Europe as the umbrella term for such projects.

5. The Commission needs to be aware, however, that the term PPP has very wide and diverse usage in some member states. It certainly captures relationships between the public and private sector that could not be seen as in the nature of procurement – and it is even used to include informal networks and ways of public sector consultation with the business community.

6. This paper is in three parts:

   - Part I describes some features common to at least most Public Private Partnership models of service delivery, and where appropriate reacts to some remarks in the draft Communication on these points

   - Part II responds to the Commission's core analysis of the current legal position and suggests how the rules might be updated in future

- Part III gives some examples of current Public Private Partnership initiatives and models in various member states – the aim is to illustrate current diversity, not to give a comprehensive picture.

PART I: COMMON FEATURES OF ALL PPPS

7. The Communication is right to identify some features common to at least most forms of PPP. However, we would challenge some of the detail of the Commission's analysis.

Risk

8. It is true that in PPP deals, the private sector assumes significant risk. Ideally, the risks in any partnership will be allocated to whichever party is best able to manage them, in order to maximise value for money. It is true that in conventional contracts, the private sector may be asked to assume similar categories of risk. But PPPs will involve the private sector assuming risk on a far greater scale, even to the extent of jeopardising the entire payment or income stream and the return on the capital investment. Risks taken on by the private sector may include some of the following:

- Demand risk: where the payment stream varies in accordance with the degree of usage (eg number of users). The private sector would be assuming demand risk whether the end user was paying directly (eg through tolls) or the Government was paying on the public's behalf (eg through shadow tolls) – so long as the payment varied with volume. In some projects, where the private sector could not control or predict usage, it would not make value for money sense for the private sector to assume demand risk.

- Operational risk: transferring substantial operational risk to the private sector operator provides a main source of value for money savings. Basing payment on availability and performance motivates the operator. Operational freedom should be transferred alongside operational risk: the public sector should leave operators free to choose how best to manage the risks they inherit

- Construction risk: these include risks of completing the construction work satisfactorily and on time

- Design risk: PPPs to date have demonstrated the value of transferring design risks, in terms of improving the fitness for purpose

- Risk of changes in legislation: typically project negotiations include debate on whether the public or private sector is best placed to carry risks of changes in, say, regulations on environment, employment, tax or other subjects that can affect the demand and cost base for the service

- Obsolescence risk: obviously an issue in technology deals but arises in other instances

- Residual value risk: this can motivate the private operator to maintain the underlying asset.

9. Our main concern with the Commission's approach is that it concentrates on demand risk, essentially implying (and probably unintentionally) that without the private sector taking demand risk, a project is largely risk-free and therefore not a PPP. Arguably, the complexity for the Commission arose in setting out at the same time a description of commercial practice and an analysis of the legal position. The current legal definition of a concession (in the Works Concession rules) rests on the existence of "exploitation" which seems to be demonstrated by the private sector assuming demand risk.

Rights and freedom to operate

10. In PPPs, the private sector will have considerable operational freedom and will typically bring innovation.

Remuneration

11. The remuneration will depend heavily on the successful operation of the service. It is worth pointing out that this can be the case irrespective of whether or not the private sector's assumes demand risk in any form. So it can be the case whether or not the income stream is paid direct by end-users or by the public sector – and whether or not the payment is based on availability or usage. The entire risk profile will be reflected in the payment stream.

PART II: RESPONDING TO THE COMMISSION'S CORE ANALYSIS OF THE CURRENT LEGAL POSITION AND SUGGESTING CHANGES TO THE LAW

12. The entire European legal framework, including the Treaty, public procurement and competition law, needs to facilitate a wide range of PPP models. We are conscious of the dangers of an inappropriate framework which might:

- introduce partial solutions whose application perhaps makes sense for one form of PPP but would be unworkable for other forms of deals
- distort decisions - purchasers may end up choosing a particular partnership vehicle on the basis of what gives rise to the fewest legal hurdles, rather than because of what will deliver best value for money
- damage public and private sector confidence in using PPP. Innovation in developing PPP models would be stifled by legal uncertainty and questions over the application of legislation or Treaty principles.

13. We welcome the Commission's recognition of these key points in the draft Communication, which aims to look fundamentally at the Treaty as well as the Public Procurement Directives.

14. UNICE members' views vary on the Commission's approach to defining Public Private Partnerships which are governed in a common way by a set of Treaty articles. Some UNICE members welcome the global approach, and see it avoiding discussions around definitions, which might stifle progress. Others are concerned that the Commission is effectively grouping arrangements together which are and are not in the nature of procurement, and would argue that Treaty goals would not be met, nor would value for money be achieved, through applying

procurement rules or procedures inappropriately. Clearly, the Public Procurement Directives should regulate procurement – there is concern within UNICE that the Directives should not be extended beyond their legitimate remit.

15. While the analysis of the legal position of PPPs at the level of the Treaty articles may be helpful as an interpretative approach to the Treaty, a part of the UNICE membership is concerned the general provisions ot the treaty will remain formless in practice, compared to the concrete regulations within the EU directives on public procurement.

Further consideration is required on the appropriate scope of the Communication. While having divergent views on the broad approach, UNICE members are united on the need for more detailed consideration of some of the terminology in the Commission's definition of the situations covered. Notably, more work is needed to capture better the sense behind the indication that the Commission is examining only the delegation of management of services "for which the authority would normally be responsible". Judgements on an authority's normal responsibilities will vary across member states and over time.

An improved definition of concessions

16. UNICE recognises that understanding of what is meant currently by the term "concession" differs across member states. There are different interpretations of what is meant by contractual arrangements that include the right for the operator to exploit the works or services. This has led to different judgements about when to apply which element of the procurement rules. At least, there needs to be:

- a clearer and more consistent understanding across Europe of what constitutes a concession (with operational examples), notably whether a concession should or should not be defined in terms of the majority of the operator's income stream taking the form of direct payments from end users

- a consistent approach to all forms of concessions, ending the divergent approach to works and services and supplies concessions

- an examination by member states of whether, in practice, they are using different labels for what are in fact concessions and, consequently, not applying the procurement rules where they currently apply or would apply if there were rules on services and supplies concessions.

17. It is also worth considering whether to use a new term to describe the range of situations to be covered. The problems with the term concessions are as follows. The term has certain national and "layman" meanings, alongside the strict definition in the Public Procurement Directives. Some member states would use other terms for what are, in fact, concessions. The problem with the phrase Public Private Partnerships is that it captures a wider set of relationships – going well beyond relations in the nature of procurement. In this paper, we use the term "concessions", but on the understanding that it might need changing.

New rules for concessions and similar forms of Public Private Partnership

18. UNICE's wish to see a consistent approach to all forms of concessions certainly implies the need for further regulation (because currently there are no detailed rules governing supplies and services concessions).

    UNICE would be keen to discuss further with the Commission how best to put this proposal into practice. We recognise that there are two main options:

    - to keep the concessions rules in one place, though a specific regulation
    - to keep works concessions rules in the Works Directive and introduce Services and Supplies concession rules into the Services and Supplies Directives.

19. In the long term this debate would become irrelevant through consolidation of the public sector directives. In the short term, whatever the structure, the priority would be to have consistency across the rules for all forms of concessions.

20. We would want sufficient clarity regarding the application of these concession and PPP rules to clearly allow the practitioner to estimate if a project were to be qualified as a PPP and what would be the legal consequences. This would contribute to avoiding currently existing severe legal risks which arise from uncertainties about the relationship between PPPs and the provisions of the directives on public procurement.

21. Regarding the content of new rules on concessions, UNICE member views vary in detail. Nevertheless there is recognition that once a PPP procurement has been made in open competition, the operator's purchasing should – as a rule – not be governed by the procurement regulations (at least not by the whole set of procurement provisions). In deciding how to take forward this principle, the debate will need to weigh up various factors:

    - that in general the open competition places substantial value for money pressure on the concessionaire, so that it will want to purchase on the basis of value for money and non-discrimination – so the need for compulsion through the public procurement directives should become redundant
    - the need to give concessionaires sufficient operational freedom to manage the risks they have taken on
    - but against those factors, there is the need to ensure transparency, to reduce the risks of long term concessions closing off market opportunities and to enhance the chances of small and medium enterprises to participate in concession projects.
    - Recognizing the differences between civil customers and privatized public entities; therefore the regulation of Art. 3 para 3 of the public works directive which implies that a concessionaire being himself a contracting authority has to comply with that directive, should be maintained according to the opinion of a considerable part of UNICE membership. On the other hand it will have to be safeguarded that private partners of PPPs will not be treated as a contracting authority only for the reason that they take part in the PPP.

As far as a concessionaire is not himself a contracting authority, a part of UNICE members suggest that the concessionaire should not be obliged to comply with the whole procurement regime but should have to place a notification concerning his procurement vis a vis third parties according to Art. 3 para 4 of works directive, which should be extended to the supplies and services directive. Such a solution would contribute to ensure transparency and enhance the chances of small and medium sized enterprises to participate in concession projects.

22. A consistent approach is needed to determine whether the private sector operator's purchasing is governed by the public procurement rules. UNICE is convinced that where there is genuine competition for the award of the initial PPP, that places sufficient commercial pressure on the operator to achieve value for money and to gear purchasing accordingly. The consumer is also protected because the operator must adhere to the contractual stipulations on price and quality of service, agreed with the public authority at the outset.

23. The Commission has embraced the principle that, once a consortium had won a TENs [1]contract in competition, it could award work "in-house" to consortium members without further competition. UNICE proposes taking that line of argument further, recognising that for PPP contracts (whether concessions or not):

- ·the rules need to cater for the likelihood that consortium members will change over time. Latecomers to the consortium should be deemed to be in-house;

- ·competition to win a PPP contract (whether or not a concession) will apply sufficient value for money pressure on the operator, removing the need to regulate its procurement.

The need to improve some detailed aspects of the public procurement directives

24. Whatever the overall structure of the legislation, the detailed rules should make commercial sense, enabling the public sector to secure value for money, and achieve fair competition.

25. The Communication appears not to acknowledge that there are some PPPs that are currently let under the Works or Services Directive. This is largely so in circumstances where, despite the private sector assuming substantial risks, the deals would not be considered to entail "exploitation" as defined in the Directives (basically because demand risk is not transferred).

26. Here follow the main areas where a need exists to improve the regime for PPPs currently let under the Works or Services Directives. Many of these points are already on the Commission's agenda:

- Pre-tender dialogue: the Commission has clarified that pre-tender dialogue is permissible

- Competitive dialogue / negotiation

[1] TEN : Trans-European Network

- Flexibility for the operator to respond to changing customer demands over the life of the contract. Here the onus is partly on the Commission to clarify that some flexibility is acceptable but also on the client to specify requirements in output terms (so while sticking to the originally specified outputs, the operator's methodology might change with technological advances)

- Commercially sensible length of contracts. UNICE would not want too prescriptive legislation on this point. On the one hand it will have to be recognized that contracts must be long enough to deliver a return to the operator, taking into account the scale of investment and risk transfer. On the other hand it has to be safeguarded that concessions should only be awarded in a way that competition will not be limited to an unacceptable extent.

- The need to keep tendering costs to a manageable level and attract private sector innovation. This implies a commercially realistic attitude on the number of bidders involved at each stage of the process and flexibility regarding the selection process (without jeopardising the principle of non-discrimination).

PART III : ILLUSTRATING THE DIVERSITY OF PPP MODELS AND SUGGESTING SOME COMMON FEATURES

27. Across Europe, there is a diverse range of Public Private Partnerships, with differences in how partnerships are formed and regulated. Here are some examples - not a comprehensive listing - but illustrating the diversity (and some of the approaches ascribed to a particular member state are also found elsewhere).

28. Netherlands – local government/business partnerships: illustrates partnerships not based on procurement

29. In The Netherlands, local authorities often enter into public private partnerships which are not based around a local authority procurement, and so are not formed under the Public Procurement Directives. One example is where the local authority and private party jointly study the feasibility of a project, with the local authority's share of the cost of the study being below 50%.

30. Another example is where the local authority and private sector partner jointly form a new enterprise in order to develop a building site. This new enterprise will act as a privatised land management company. The land necessary for the realisation of the project is transferred to this new company. The company will have the land prepared for building, order services and sell the serviced plots. Usually this new company is not a public body (because there is no dominant contribution from the public side) and therefore not a contracting authority. The Public Procurement Directives would only apply if, under the terms of the partnership agreement, the joint company is given tasks that include carrying out contracts that fall under the scope of the directive.

France: "Contrat d'affermage" for water distribution: illustrates concessions

31. The contrat d'affermage provides for the transfer by a municipality of the water distribution to a private sector operator, referred to as a "fermier". The fermier is given special and exclusive rights to operate the service and takes on operating risk. Remuneration is derived from operating the service.

32. The contrat d'affermage is awarded under the "Sapin Law" which requires competition and non-discrimination in the award of a wide range of service concessions. Notification of the intention to award a contract must be published in the Official Journal and in a magazine of the relevant sector. The fermier may make innovative proposals in his offer, which might be integrated into the contract after the negotiation, which must meet the non-discrimination principle.

33. The water fermier's purchasing is covered by the Utilities Directive (93/38), because water is stipulated as an excluded sector. There are instances where concessions are awarded in sectors that are not covered by the Utilities Directive, which therefore would not apply. European procurement legislation may apply where there is a legal or contractual obligation of the concessionaire to subject certain operations (necessary to the performance of the service) to the requirements of the Public Procurement Code or if the contract covers a works concession subject to Directive 93/37.

UK - Private Finance Initiative: illustrates procurement-based partnerships

34. Under the Private Finance Initiative (PFI), the Government typically purchases capital-and-service package solutions, centred around the service requirements. For example, whereas historically the Government bought a prison building, separately employed prison wardens etc and let contracts for, say, catering and training, under PFI it now buys prison services. This includes requiring the private sector to deliver the prison building because it is part of what is necessary to deliver the service. The private sector must also fund the capital investment.

35. The operator's income stream typically takes the form of payments from the Government. The payment stream enforces the risk allocation and partnership-based approach. It is service-driven in that the income stream depends on the use or availability of the service (depending on whether demand risk is transferred). Either way, the risks taken on by the private sector in these projects are much greater than in general service contracting.

36. There are parallels to the prison example in various other sectors, eg transport, IT, hospital services, property (including office accommodation and housing), various defence-related services, education, power supply to hospitals etc. Typically, PFI contracts are let under the Works or Services Directives. Because to date PFI contracts have rarely involved the end user funding the bulk of the income stream, they have rarely been let under the concessions rules.

Concessions and PPP in the Italian system

37. The undertaking of public services is regulated in Italy by many laws both at local and sectoral level; so it is very difficult to have an exhaustive identification of them. At national level, no general regulation exists for public utilities. Examples of public services are:

- at national level, concessions to FS SpA (Italian Railways Company) and to ENEL SpA (National Integrated Electricity Company);

- at local level, the distribution of potable water, natural gas, and electricity; the activities of slaughter houses, cemeteries, waste disposal and so on.

38. The most significant law regulating local public services is the Law n.142/90 on local autonomies, which establishes some general principles and provides for new forms of management by local authorities.

39. The most usual forms of local authority intervention in the field of public services are:

- direct management;
- concessions;
- special companies;
- mixed private – public companies with the capital majority/minority owned by the local authority.

40. The Law n. 142/90 is now being reformed by the Parliament for adaptation to the new EU rules on privatisation/liberalisation and to the rules on public procurement.

41. It must be stressed in fact that in practice, in Italy, the concession model is progressively being overtaken by other management models for public service and, in particular, by Public Private Partnership.

42. The majority of public services are in fact managed through joint – stock companies with the participation of public capital (either majority or minority), that is through a juridical system which is considered by the Italian Law and by Courts as a completely separated phenomenon from that of concessions.

43. This distinction, whereby the concession is a contract based on a corresponding performance while a partnership means an associative contract, is undoubtedly grounded in the internal legislation. But it represents a fiction according to the Community law, as the two phenomena refer in reality to the same subject, that is to private sector management of public services.

44. The reform of the Law n. 142/90, which is now being examined by the Parliament, seems to be oriented to overcome such a distinction by transposing the new Community principles into the Italian system.

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