ISTANBUL PPP WEEK 7

16 - 19 JAN 2023

PPP: INVEST IN

PEOPLE | CLIMATE | ECONOMY

Allocating Roles, Risks & Rewards

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DECADE OF ACTION

Today’s menu

Stakeholders, structure & secrets

“ We're all working together; that's the secret ”

Direct agreement, step-in rights, hedging agreements, delay events, compensation event, risk allocation, back-to-back, DRB, ADR, availability payments, output specs, bid bonds, LTA, EPC, MTC, interface agreements, availability date, TLA, DBFM, DBM, DBFMO, equity provider, …

Alain Fayard, 1999

"PPP" is one of those handy neologisms used to describe an ill-defined trend that is still in progress. It is sufficiently precise to identify the novelty, i.e. co-operation between public and private sector interests in the completion of a project.

Yet it is sufficiently vague to convey all aspirations of those involved, namely the politicians who think that they have fond a way of by-passing financial constraints, the government officials who would readily see themselves es the heads of a new type of enterprise, and private groups which would like to think they have found the magic words that will open the door into new markets and at the same time confer upon them the gravitas of public services, of citizen enterprises."

Roles, risks & rewards: “The same but different”

No project
is the same as another

No sector
is the same as another

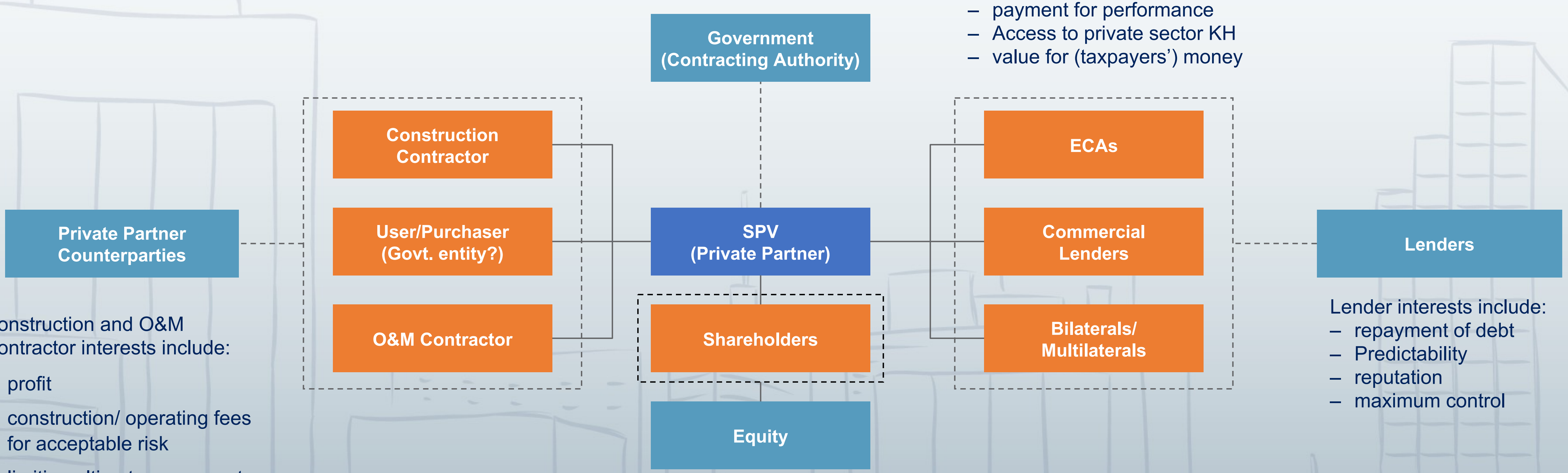
No country
is the same as another

Different risks,
different roles & risks

BUT
same principles!

Roles & goals of the parties/(some)stakeholders

Contracting Authority interests include:
– Timing
– payment for performance
– Access to private sector KH
– value for (taxpayers') money



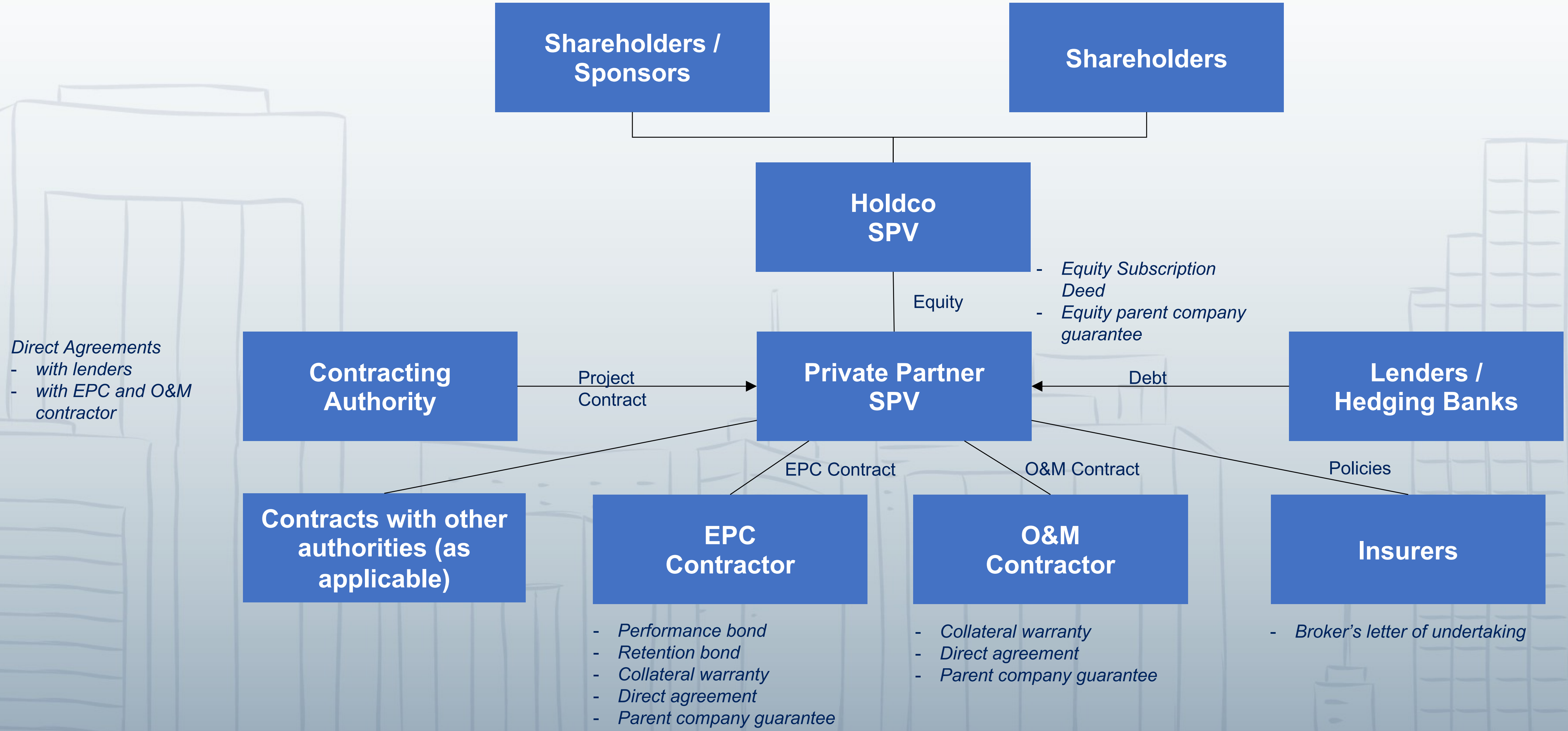
Construction and O&M Contractor interests include:

- profit
- construction/ operating fees for acceptable risk
- limiting ultimate exposure to liability

Lender interests include:
– repayment of debt
– Predictability
– reputation
– maximum control

Shareholder interests include:
– profit
– construction/operating fees for acceptable risk
– off balance sheet financing.

Roles in a simplified PPP structure



Tender process risk per phase

1. Pre-launch
2. Publication
3. Selection of PQQ
4. Offer(s)
5. BAFO

Tender process risk per phase

6 Preferred Bidder (waiting room)

7 Award Contract Close Financial Close

8 Construction

9 Maintenance

10 “The End”

Risk management in the tender phase

Specifics of PPP tendering

1 **Stakeholders/interface**

Consortia, equity, lenders, insurance, advisers², public stakeholders²
But ONE project agreement with SPV

2 **Duration**

Tender process, contract, complexity,…

3 **Costs & compensation**

Tender procedures, paper trail, …

4 **Specs**

Input vs. output specs

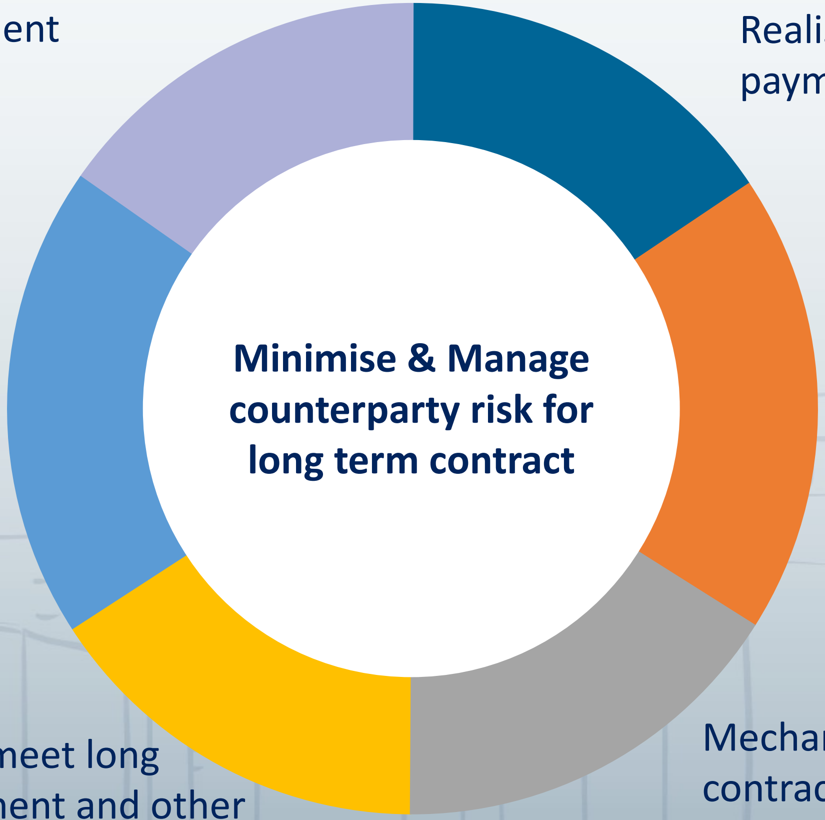
Key Risks


Surprises
1
Unsuitable bidders
2
No bidders
3
Partnering issues
4
Delays
5
Compliance +
6
Change in Law
7
Political risk
8
Bankability
9
Interface risk
10

What makes a good PPP Contract(or)?

Recognition of long-term commitment to terms and predictability

Realistic pricing and effective payment mechanism



Cooperative & flexible mindset & contract

Clear, predictable terms, balanced risk allocation for bankability - a partnership

Ability to meet long term payment and other obligations

Mechanism for adjusting contract / rebalancing risk allocation

Plan & predictability

Team & stakeholders

Transparency & information sharing

Flexibility

Risk management in contract phase

Traditional vs. PPP procurement in contract phase

1	Transfer of ownership/control/operation by Government/Authority to a privateSpecial Purpose Vehicle (SPV)	
2	SPV is usually owned by private sector entities, sometimes with Contracting Authority shareholding	
3	SPV's only "asset" is the exclusive right to develop the project $	
4	Project is the right of the SPV to own, construct, and operate the project asset/provide the service for a fixed period of time (eg 25 - 30 years) after which the asset may return to the Contracting Authority	
5	The only cashflows for the SPV are from the project contracts it enters into (typically the main PPP Contract) – lenders' rights are limited to these cashflows and the assets of the SPV ("**limited recourse**")	

Key Risks


Surprises
1
Social
2
Environmental
3
Partnering issues
4
Regulatory
5
Demand
6
Change in Law
7
Political risk
8
Land/expropriation
9
Interface risk
10

Reducing risk

Plan & predictability

Team & stakeholders

Transparency & information sharing

Realism & flexibility

Sharing or allocating risk

Risk sharing

Risk sharing

I like to have my cake and eat it too.

I'd also like to have your cake and eat it too.

Risk Allocation: who takes the risk?

Risks can either be:

- Assumed by Contracting Authority
- Assumed by Private Partner with parent support
- Assumed by Private Partner and priced
- Assumed by Private Partner and mitigated (e.g. insurance)
- Assumed by Private Partner and passed down to Construction/ O&M Contractors

Appropriate risk allocation maximises value for money, ensures bankability and competition.
Risk mitigation usually has a price.

Risk Allocation: how to allocate risk?

- Allocate risks to the parties best able to manage them and be acceptable to Lenders
- Consider bankability: for example in less mature PPP markets lenders expect government to take more risk
- Strike a fair, sustainable balance
- Incentivise all stakeholders to make the project work
- Ensure transparent understanding of risk allocation and the risk/return analysis

Managing & avoiding risk

A PPP never sleeps…

Rewards?

Contracting Authority	Sponsor/Shareholder	Lender
To achieve "value for money" within budget & timing	To extract profit – "investment return"	To make profit – "margins and fees"
To have adequate safeguards and assurances the project will be operated properly	To minimise interference with the project	To keep control – (i) to maintain project profile and protect cashflows (ii) to manage key project decisions
To regain control of the project as a matter of last resort	To retain control of the project for as long as possible in times of hardship	To take control over the project as soon as possible in times of hardship
Generally to avoid risk & transfer risk from public to private sector	To avoid & share the risk in carrying out the project	To avoid risk

Risk example: Change in Law Risk

The risk that a change in “law” adversely impacts on the PPP project, e.g. causes increased costs or decreased revenues

General changes in law often with sit the Private Partner (but depends on project circumstances, e.g. stability and predictability of legal regime)

Specific (including discriminatory) changes in law often sit with the Contracting Authority

– Discriminatory applies only to the project and not similar projects

– Specific applies to the project sector/type of services being provided

Risk example: Force Majeure Risk

Event is:
- beyond the control of the contracting parties
- which makes it impossible for one party to fulfil its contractual obligations
- which in some jurisdictions (usually civil) may have to be "unforeseeable"

Different approaches to defining Force Majeure
- Open ended "catch all" definition and non-exhaustive list
- Exhaustive list (sometimes with "catch all")

Depends on the specific project
- political/natural risks differ
- ability to manage risk and occurrence will differ

Consequences – Time/compensation; possible termination if prolonged, other adjustments

Questions?

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THANK YOU FOR LISTENING

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