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Types of partnerships between the Romanian authorities and private investors

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MAIN TREND

In recent times, and in part precipitated by the current economic crisis, industry groups and trade chambers have been voicing their need for a more flexible legal framework covering public private partnerships in Romania. It is hoped that this will both increase the numbers of public projects (without affecting the budgetary deficit), and allow for public projects to be structured in line with the efficacy and management conditions applicable to the private sector. The construction market in Romania has registered record losses over the last few years, and many construction business are only surviving as a result of public works contracts, many of which are financed through different EU programmes. It has been argued that the legislation concerning concessions and PPPs should be revised, to provide more opportunities (in addition to the classic partnership that can be structured under the current legislation) for both construction businesses and public authorities to start new projects using both private and public resources.

In line with the European Commission's Communication on Public Private Partnerships of 2009 (aimed at introducing new financial engineering instruments and recommending ways to make the combination of EU grants and PPP structures more attractive and accessible), the Romanian Government (through the Department for Infrastructure, Projects and Foreign Investments) published a draft new PPP law at the beginning of 2013 (*www.dpiis.ro/draft-legislation-on-inter-ministerial-consultation-77/*) aimed at clarifying the numerous issues which have made the current PPP law (that is, Law No. 178/2010) unattractive to investors. It also aims to clarify the rules for PPPs in line with the legislation concerning concessions. Following consultations with the European Commission, the new draft PPP law is expected to be enacted by Parliament during September/October 2013.

LEGAL FRAMEWORK: SCOPE OF EACH APPLICABLE REGULATION

Law No. 178/2010 which governs PPPs (Law No. 178/2010) does not apply to public works and public services contracts, which remain regulated by the Government Emergency Ordinance No. 34/2006 on the award of public procurement contracts and on the award of public works and services concession contracts (GEO No. 34/2006). Law No. 178/2010 also does not apply to concessions of public assets which remain regulated by the Government Emergency Ordinance No. 54/2006 on the regime of concession contracts for public assets (GEO No. 54/2006). Indeed, it remains doubtful whether the current Law No. 178/2010 which governs PPPs can ever be applied to projects involving the concession of public assets or services.

The main distinction between GEO No. 54/2006 and GEO No. 34/2006 is as follows:

- GEO No. 54/2006 should be applied in cases where the concession of a public asset is granted without any requirement regarding the further exploitation of that asset for the construction of a public project or for the supply of a public service.
- GEO No. 34/2006 should be applied where the concession of a public asset contains certain provisions regarding the operation of that asset, or regarding a certain service which is to be provided by the concessionaire.

In practice, it is generally accepted that where the provisions contained in the concession concern either the project reaching a certain value, or the concessionaire hiring a certain number of employees, this will still fall within the scope of GEO No. 54/2006 and GEO No. 34/2006 will not be applicable.

CONCESSION AGREEMENTS OF PUBLIC WORKS AND SERVICES

Parties to the concession agreement

Under GEO 34/2006, a contracting authority (strictly for the purpose of concession agreements) means:

- Any state body, public authority or public institution, acting at a central, regional or local level.
- Any public law entity (other than those mentioned above) set up in order to satisfy a public interest, without having a commercial or industrial character, which is one of the following:
  - majorly financed by a state body, public authority or public institution, or by another public law entity;
  - subordinated to or controlled by a state body, public authority or public institution, or by another public law entity;
  - has more than half of the members of its board of directors appointed by a state body, public authority or public institution, or by another public law entity.
- An association formed by more entities belonging to a state body, a public authority, a public institution or a public law entity.

The concessionaire can be any national or foreign economic operator, supplier of works or services (either publicly or privately owned), or an association of such persons. In some cases, the concessionaire is a legal entity constituted specifically for the purpose of the concession agreement (for example, a special purpose vehicle (SPV)). The SPV structure is similar to the "project company" concept established by Law No. 178/2010, and the contracting authority may also decide to participate in the share capital of the SPV.

The most notable aspect of a public works or services concession agreement is that the concessionaire, after having executed the works/service, is also entitled to exploit/operate the assets resulting from those works or services for a determined period of time, in exchange for a royalty which is paid to the contracting authority. A contracting authority may also decide to enter into a concession agreement in order to outsource a public utility service.

Awarding procedure

The contracting authority must comply with the transparency principle set out in GEO No.34/2006 and publish both the participation notice and the award notice in the Electronic System for Public Procurement, as well as in the *Official Journal of the European Union*, if the value of the agreement exceeds the equivalent of EUR5 million in Romanian new lei (RON).

The contracting authority must base its decision to organise a tender on a "substantiating study", in which it should thoroughly analyse whether a concession agreement is the most suitable option for its purpose. In accordance with the provisions of Government Decision No. 71/2007 regarding the award of the contracts governed by GEO No. 34/2006, the substantiating study must contain more or less similar information to a feasibility study (that is, the technical, economical and financial feasibility of the project).

The tender documentation must contain, amongst other things, the following:

- Minimal qualification criteria.
- Technical and financial proposals.
- The tender book.
- Detailed explanation of the selection criteria (the most advantageous offer from a financial point of view).
- Mandatory contractual clauses.
- Ways to appeal against the tender.

The awarding procedures concerning a concession agreement are as follows:

- **Open procedure.** Where any economic operator can participate.
- **Restricted procedure.** Where any economic operator can submit its offer, but only selected candidates are invited to participate in the tender.
- **Competitive dialogue.** Used for complex projects, where the contracting authority will address the selected candidates in order to find the solution which best fits its needs, after which the selected candidates draft their final offers.
- **Direct negotiation.** Applicable in situations where no corresponding offer was identified after carrying out one of the abovementioned procedures.
- **Request for offers.** Where the contracting authority requests offers from more economic operators.
- **Design contest.** Where the contracting authority procures, mainly in the domain of land use planning, town planning and landscape design, architecture or data processing, a plan or a project, by selecting it on competitive basis through a jury, with or without granting prizes.

The open procedure and the restrictive procedure are usually utilised, and the other procedures can only be applied by way of exception, under special circumstances.

Financing and security

The funding of the public works or services is secured by the concessionaire and originates in private equity sources, usually obtained through loans contracted by the concessionaire. In a typical concession agreement the risks are mainly allocated to the concessionaire, since it is the party which is entitled to exploit the public works or services. If the risk allocation is shared between the concessionaire and the contracting authority, the concession agreement must specify the financial contribution which is borne by the contracting authority. Usually, the investment is recovered by the concessionaire from either taxes incurred to end users, or from allocations from the budget of the contracting authority. Penalties are determined in the agreement and will be incurred if the works or services executed by the concessionaire do not correspond to the quality and performance criteria set out in the tender book.

The concessionaire must provide the contracting authority with two types of securities:

- A guarantee for participation, in order to secure the offer.
- A guarantee for execution of the agreement, which will be enforced by the contracting authority if the concessionaire does not perform its obligations as per the concession agreement.

In order to mitigate the risks of receiving lower budgetary allocations than those agreed with the contracting authority, concessionaires also have the possibility to request penalties for delayed payments made by the contracting authority.

Allocation of risks

Under Romanian law, the allocation of risks among the parties is important in order to determine whether the contract will follow either:

- The public procurement award procedure.
- The procedure for the concession of public works and services.

In general, where the concessionaire is granted the right to exploit the works he has executed or to operate certain public services, and has undertaken the majority of the risks associated with the project, the contract will be considered to be a concession of work and/or services. Where this is not the case, it qualifies as a public procurement contract.

Duration

The term of concession agreements is not fixed by the legal provisions and is determined on a case-by-case basis. The ownership rights in the assets created by the concession project are transferred to the contracting authority at the end of the term of the concession agreement. Some key factors must be taken into account when establishing the duration of the concession agreement, including:

- Cost efficiency.
- Potential distortions of the competition.
- The prices which will be borne by the end users.

The duration of the concession agreement must not be shorter than the one of the loan agreements entered into by the concessionaire, in effect avoiding problems with the repayment of the loan and a possible forced execution of the bank guarantees.

Amendments

With respect to the possibility of making amendments to concession agreements related to public works or services, modifications are only possible:

- If they are necessary to complete the scope of the contract.
- When the amendments are not separate from the initial contract (from a technical and economical perspective).
- Where they amount to no more than 50% of the value of the original concession agreement.

Termination

A concession agreement will end on the expiry of its term. If one of the parties does not fulfil its obligations, the other party can also terminate the agreement.

The provisions of GEO No. 34/2006 allow the contracting authority to request that the concessionaire subcontract at least 30% of the value of the works to third parties (in the case of concession agreements for public works). The concessionaire and the subcontractor can also subsequently increase the subcontractor's share from the initial contract.

Dispute resolution

The selection procedure and the awarding procedure are subject to appeal in the following ways:

- Any prejudiced person can file a complaint before the administrative jurisdictional body (that is, the National Council for the Settlement of Contestations (Council)) against any act undertaken by the contracting authority which is considered to be illegal. This procedure is mandatory for the economic operator and relates only to the selection procedure. The Council can request the contracting authority to take a particular action or can impose other remedies. The Council can only decide whether the contracting authority can continue the selection procedure, or it can cancel it, but it cannot force the contracting authority to award the contract to a certain bidder.
- Against the decision of the Council, the bidder can file a complaint with the competent court. As a result, the court may rule the annulment of an act issued by the contracting authority, request it to take a particular action, or take any other necessary measures.

The contracting parties can elect that all disputes related to the fulfilment of the contract are settled by way of arbitration.

CONCESSION AGREEMENTS OF PUBLIC ASSETS

The award of concession agreements of public assets based on the provisions of GEO No. 54/2006 is governed by the same principles as those applicable to GEO No. 34/2006, with the following differences.

Parties to the concession agreement

The contracting authority is represented by:

- For state-owned assets, ministries or any other bodies of the public central administration.
- For assets owned by the local authorities, local councils or public institutions of local interest.

The concessionaire can be any national (or foreign national) natural or legal person.

Awarding procedure

The concession contract can be awarded either:

- Through an open procedure, which requires the participation of at least three bidders in order to be valid.
- Through direct negotiation, which can only be used when, after repeating the initial open procedure, less than three valid bids were submitted.

Duration

The duration of the concession agreement will be established based on the substantiating study that must be concluded prior to the start of the awarding procedure. The duration cannot exceed 49 years, though the duration may then be extended further for a period of not more than half the original term of the concession agreement.

Amendments

Amendments to concession agreements are only valid where they do not change either:

- The terms imposed by the tender book.
- The essential terms of the offer.

Any contrary interpretation to this would imply that an authority could negotiate the terms of the awarded contract, which would completely undermine the legal requirement that an open tender procedure must be used (effectively putting in its place a negotiation procedure).

The concessionaire cannot subcontract its rights and obligations assumed under the concession agreement.

If amendments to the concession agreement are required in the national or local public interest, the contracting authority can unilaterally make amendments to the agreement, provided that it:

- Notifies the concessionaire in advance.
- Provides the concessionaire with a reasonable indemnity (if the concessionaire incurs damage).

Termination

A concession agreement concluded under GEO No. 54/2006 will end at the expiry of its term or can be terminated unilaterally, in the case of default, by the non-defaulting party. Termination of the agreement can also occur if the continuation of the agreement is contrary to the public interest, in which case the contracting authority is entitled to unilaterally terminate the agreement, on condition that it indemnifies the concessionaire.

Dispute resolution

Any disputes concerning the award procedure, the conclusion, the execution, the amendment or the termination of the concession

agreement are subject to the administrative claims procedures. The applicant must first submit a preliminary complaint to the contracting authority. If that authority fails to favourably solve the complaint, the applicant can address the court which has territorial jurisdiction over the headquarters of the contracting authority.

WHY THE DRAFT OF THE NEW PPP LAW?

Clear applicability frame

One improvement made by the draft of the new PPP law is that it more clearly defines its own scope, particularly as regards the present concession legislation. Under the draft of the new PPP law, a public authority can only award a PPP contract where a substantiating study conducted before the award is made shows that incomes to be obtained by the project company are going to be mostly generated by payments effected by the public partner.

The draft of the new PPP law also clearly distinguishes between this type of projects, and projects where the income generated by operating activities are ensured from tolls or fees collected from the final users (where the new law cannot be applied). These latter projects can only be agreed under the provisions of GEO No. 34/2006. For example, in the case of setting up a kindergarten, the new PPP law can only be applied if the generated incomes are provided by a public authority (which will bear the operating expenses), and not by the parents who will enrol their children at that kindergarten.

Clarifying the title granted to the project company over the public assets involved in the project

The present law stipulates that the public partner can only participate in the project where it makes a "contribution in kind", by it does not specify whether this contribution must consist of assets from the public or private domain of the public authority, or if it can also consist of a concession right or leasing right. An interpretation which allows public assets to be granted to the project company in the absence of a concession right or leasing right would conflict with the constitutional provisions which govern the legal ways in which public assets can be used by public authorities.

This unclearness has been clarified in the draft new PPP law, which makes it possible to conclude a contract between the private and public partners by either:

- Granting concession or leasing rights over assets in the public domain of the public authority.
- Granting rights of superficies or leasing rights over assets in the private domain of public authorities.

This appears to enable a derogation from the way in which these kinds of rights are usually granted (that is, under GEO No. 34/2006 or other such regulations).

A unitary awarding procedure

The current legislation leaves it to the public partner's discretion to elect which specific law will apply when starting a new project out of the relevant laws applicable to the public procurement sector (that is, either GEO No. 34/2006 or GEO No. 54/2006). The draft new PPP law clearly sets out three awarding possibilities:

- Open tender.
- Closed tender.
- Competitive dialogue.

The procedures for each of these three awards will now be regulated by the procedures established under GEO No. 34/2006.

Guarantees offered to the financing parties

The draft new PPP law not only allows for the income of the project company to be generated by payments effected by the public partner (which is questionable under the current PPP law), but it also allows for certain guarantees over the shares owned by the private party in the project company. These guarantees do not cease at the expiration of the PPP contract, but can be transferred, in case the PPP contract terminates before the expiration date. In addition, the new law also allows for the possibility of the project company constituting guarantees over the receivables and over other rights established in favour of that company, including over the rights granted to the project company by the public partner. However, where guarantees are granted to the project company by the public partner, they must be exclusively in favour of the project sponsors.

As a means of securing the rights of the sponsors, the draft new PPP law has also allowed for direct agreements to be concluded between the public partner and the financing agent. Under these agreements, the private partner and/or the project company can be replaced by the public partner from the project (at its own initiative or at the initiative of the financing agent (that is, the public partner's step in right)) where they either:

- Fail to fulfil their obligations under the PPP contract.
- Fail to fulfil their obligations undertaken towards the financing agent.

The new private partner will be appointed by the public partner together with the financing party, using the same qualification criteria as was used in the initial appointment procedure.

A more flexible way to establish the technical and economic parameters of the project

The awarding procedure starts with the public partner conducting a "substantiating study" of the PPP project. The public partner can engage specialist technical, economic and legal consultancies during this process. The substantiality study will analyse the following matters:

- The project sustainability.
- The risk distribution.
- The reference to the public deficit and public debt.
- Project financing and economic efficiency.

Conducting a substantiating study before commencing the award procedure has the following advantages:

- For the public partner, it avoids the more costly feasibility studies that would otherwise be required under the provisions of the old public procurement and concession legislation.
- For the private partner, which will no longer be restricted in the development of the project as a result of the feasibility study that would otherwise have been conducted.

The proposals concerning the allocation of risk are also very important for the success of the PPP award procedure, since they determine the degree of joint interest for the investors and sponsors and will influence the successful completion of the project. It must therefore be clearly established what the risks are, and which risks are undertaken by each party, taking into account each party's expertise and their ability to influence each respective risk.

A high degree of diligence will be required of the public partner who draws up the risk allocation proposal, since without a rigorous set of regulations which set out the conditions concerning the availability of the PPP project, either:

- The project will become uninteresting to the investors or financers (where the burden of risk allocated to them is too great).
- The project may be seen as a waste of public funds which is being made under the pretext of private management.

CONCLUSION

In conclusion, the draft new PPP law has the potential to constitute a fresh start for the economic and social development of Romania, an opportunity that should be welcomed to assure steady future economic growth.

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Anca's main focus is commercial property and industrial greenfield investment and development. In addition, she has a broad road and rail infrastructure and conventional and renewable energy expertise, which includes project development and project financing, public procurement, infrastructure acquisitions and investments and acquisition financing. She has particular expertise in EU financing, as she has been involved in financing projects from Romania's initial access to EU funds. Her industry expertise covers industrial manufacturing, energy, infrastructure and utilities.

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The range of his expertise includes conducting complex due diligence exercises, assisting clients on regulatory matters and negotiating commercial contracts, as well as in all subsequent phases of projects through to completion and disposition. Occasionally he has also been involved in real estate disputes.

- Actively involved in specialised committees of the American Chamber of Commerce in Romania (AmCham) and is currently involved providing support and expertise in AmCham's initiatives in relation to infrastructure projects, PPPs and public procurement. Nicolae is an elected vice-president of AmChams Infrastructure & PPP Committee.
- Involved as a trainer on legal protection of biodiversity in the "National awareness campaign on the importance of biodiversity conservation through Natura 2000 network in Romania", a project initiated in 2012 by the National Centre for Sustainable Development Foundation.

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Her practice includes drafting lease, sale and purchase, supply and other commercial agreements. She was involved in conducting due diligence reports and drafting legal opinions for various clients in the industrial manufacturing and energy sectors. Sonia is interested in the pharmaceutical, energy, media and technology industries.

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