



Main article of page 2

# EBRD Core Principles for a Modern Concessions – Law

## selection and justification of principles

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### Introduction

The EBRD Core Principles for a Modern Concessions Law (the Core Principles) underpin the EBRD's design of legal reform projects in the area of concessions/Public Private Partnership (PPP). The purpose of the Core Principles is to identify and promote sound modern principles of concessions laws in the EBRD's countries of operations. By promoting clearness, fairness, stability, predictability and flexibility among their major objectives, the Core Principles aim to protect both investors and the public sector from unfair treatment and abuses. The Core Principles are based on maximum transparency of procedures, thus ensuring benefits to all parties. They were first published on the Bank's web site in January 2005 as a discussion paper soliciting public comments, and now appear in their final version.

Further information on the Core Principles, along with their text in English, Russian and French, may be found on the EBRD's website at <http://www.ebrd.org/country/sector/law/concess/index.htm>.

The present paper is aimed at explaining the meaning of the Core Principles and the sources from which they were derived. This paper may be read in conjunction with, and complemented by a [draft] paper prepared by the EBRD Banking Department in July 2006 and entitled Public Private Partnerships and EBRD Discussion Paper, which provides an overview of various forms of PSP from a banking/financing standpoint.

### The EBRD Core principles for a Modern Concession Law

The Core Principles are based on key internationally accepted standards and best practices, as refined and tested on the Legal Transition Team's (LTT) technical assistance projects, including regional studies, sector surveys and assessments<sup>1</sup>, as well as LTT's participation in international standard setting initiatives (such as the UNCITRAL Model Legislative Provisions on Privately Financed Infrastructure Projects).

The following international texts were used in drafting the Core Principles:

- UNIDO Guidelines for Infrastructure Development through Build Operate Transfer (BOT) Projects, 1996 (UNIDO BOT Guidelines);
- OECD Basic Elements of a Law on Concession Agreements, 1999-2000;
- UNCITRAL Legislative Guide on Privately Financed Infrastructure Projects, 2000 (UNCITRAL Legislative Guide);
- UNCITRAL Model Legislative Provisions on Privately Financed Infrastructure Projects, 2003 (UNCITRAL Model Legislative Provisions).

The following regional texts were used in drafting the Core Principles:

- European Commission Interpretive Communication on Concessions Under Community Law (2000/C 121/02);
- European Commission Guidelines for Successful Public-Private Partnerships, 2003;
- European Commission Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, 2004.

The UNCITRAL Legislative Guide and the UNCITRAL Legislative Provisions are the primary sources used for drafting the Core Principles as they closely relate to concession-type projects and provide guidance as to the effective legal framework aimed at fostering an attractive investment environment for privately financed projects. The other source documents served mostly as general guidelines as they provide information on the nature, structure and characteristics of PPPs<sup>2</sup> (including the definition of "concessions"<sup>3</sup>) and on the legislative and regulatory framework for their effective implementation.<sup>4</sup>

### Principle 1 A Modern Concession Law (MCL) should be based on a clear policy for Private Sector Participation.

Explanation: Like a sound legislative framework, clear government policy/strategy for the Private Sector Participation (PSP) is important for signalling the commitment of the government to develop a stable and attractive investment environment and to reflect its efforts in improving the legal environment. Such strategy should generally be developed on the level of a government approved document.

Sources: UNIDO BOT Guidelines stress the importance of adopting the government PSP strategy in order to communicate the commitment of the state to promote favourable political, legal and regulatory conditions and thus enhance the interest of potential investors.<sup>5</sup>

### Principle 2 MCL should create a sound legislative foundation for concession.

Explanation: Effective participation of the private sector in the development of infrastructure and effective functioning of the concessions regime requires an enabling legal framework. An enabling legislative foundation is important for establishing roles and responsibilities of all parties and estimating a so-called country risk by potential investors. The concession legal framework may be represented by

either a specific concession law or a comprehensive set of sector-specific laws that foster a clear, fair, predictable and stable legal environment for concession projects.

Sources: The importance of an enabling legal framework for concession projects is reflected in Recommendation 1 of the UNCITRAL Legislative Guide.<sup>6</sup> The Recommendation emphasises the importance of solid concession legislation not only for clarity and stability of the investment regime but also for signalling a political commitment of the state.<sup>7</sup>

### Principle 3 MCL should provide clarity of rules.

Explanation: The concession law should clearly define the scope of its application, i.e. the legal relations to which the law extends. Such clarity is essential for the predictability of the concession regime, for the stability and validity of the concession agreement as well as for the prevention of ungrounded arbitrary actions by the contracting authorities. With this purpose, the MCL should provide an exhaustive definition of "concession", a list of sectors concerned, contracting authorities, and eligible concessionaires.

Sources: Principle 3 is largely based on Recommendations 2-5 of the UNCITRAL Legislative Guide. The Recommendations stress the importance of identifying in the concession law the bodies/officials at various levels of government empowered to act as contracting authorities,<sup>8</sup> as well as sectors in which concessions may be awarded.<sup>9</sup> In order to ensure clarity with

regard to the object of concession, the Guide appeals to the importance of "interpreting" the meaning of "concession" in the law, i.e. its form and type/purpose (BOT, Build Own Operate (BOO), etc.)<sup>10</sup> as well as indicating the exclusivity of the right granted by concession and its geographical scope.<sup>11</sup> For the purposes of defining "concession", the EU Commission Interpretive Communication may prove useful as it provides definitions of the "works concession"<sup>12</sup> and "service concession",<sup>13</sup> as well as a generalised definition of "concessions".<sup>14</sup> The clarity and the scope of the authorisation for the procurement and implementation of concession projects are also stressed in the UNIDO BOT Guidelines.<sup>15</sup> (See also UNCITRAL Model Legislative Provisions 3, 4).

### Principle 4 MCL should provide a stable and predictable concession legal framework.

Explanation: As a rule, privately financed projects are long-lasting. However, many different factors influencing projects may change in the course of their implementation, one of them being legislation. The risk of changing legislation may endanger the validity of the project agreement and thus the sustainability of the project itself. In order to ensure the stability of the project agreement and the parties' capacity to carry out their rights and duties, the state should avoid frequent changes to concession-related legislation and the concession law should foresee a mandatory provision in the agreement stipulating the surviving applicability of the regime in force at the moment of agreement or other mechanisms for dealing with legal risks.

Sources: Recommendation 58 of the Legislative Guide states that concession law should require the concession agreement to address the potential legal risk and set forth provisions regarding compensation for the negative consequences of legislative changes as well as mechanisms for revising the terms of the agreement following the occurrence of such changes.<sup>16</sup> The OECD Basic Elements of a Law on Concession Agreements also contain a so-called "stability clause" that is meant to protect the concessionaire from the possible changes in legislation.<sup>17</sup> (See also UNCITRAL Model Legislative Provisions 39-40).

### Principle 5 MCL should promote fairness, transparency and accessibility of concession rules and procedures.

Explanation: This principle relates to the fairness, transparency and accessibility of the rules and procedures governing the selection of concessionaires, awarding and further implementation of a concession. Under this principle, the MCL should foresee the process which would guarantee a transparent and competitive selection process (including exceptions from competitive procedure), equal treatment of potential investors, opportunity to challenge the rules and decisions of contracting authorities and competitive rules for unsolicited proposals.

Sources used: A number of the UNCITRAL Legislative Guide recommendations have been used in drafting this principle. Specifically, Recommendations 9 and 10 of the Guide state that regulatory procedures and rules on concessions should be objective, transparent and accessible (made public).<sup>18</sup> Moreover, Recommendation 10 also stresses the importance of having in place the procedures for a review of the regulatory decisions by an independent body.<sup>19</sup> Fairness and transparency of the concession rules and procedures is also reflected in Recommendation 14 of the UNCITRAL Legislative Guide, which refers to the importance

of guaranteeing fair competitive procedures for the selection of concessionaires<sup>20</sup> and in Recommendation 39, which guarantees the right to apply for a review of the contracting authorities' acts<sup>4</sup>

during the selection procedure.<sup>21</sup> The UNCITRAL Legislative Guide also suggests having a procedure in place for non-competitive proposals (Recommendation 28) and unsolicited proposals (Recommendation 30-35). Principle 5 is also supported by the European Commission's Interpretive Communication, the European Commission Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions and the OECD Basic Elements of a Law on Concession Agreements.<sup>22</sup> (See also UNCITRAL Model Legislative Provision 6, 18-23, 28).

### Principle 6 MCL should be consistent with the country's legal system and particular laws.

Explanation: MCL should be consistent with the rest of the country's legislation so as to avoid unnecessary collisions of laws and inconsistency in their application. Appropriate amendments should be made to legislative acts to ensure the coherence and consistency of the legislative base.

Sources: Recommendation 1 of UNCITRAL Legislative Guide states the importance of the conformity of the concession law to constitutional provisions, both as regards restrictions and guarantees.<sup>23</sup>

### Principle 7 MCL should allow for negotiability of concession agreements.

Explanation: Freedom to negotiate concession agreements is important because it allows the factoring in of a greater variety of circumstances while allocating risks between the parties and thus elaborating a more creative and financially efficient approach to risk allocation. Successful implementation of this principle also requires the clear identification in the concession law of the body authorised to negotiate the agreement, implement and monitor the performance under the agreement, including the clear division of powers between central and local authorities.

Sources: According to Recommendation 2 of the UNCITRAL Legislative Guide, in order to ensure the effective negotiation and further implementation of a concession project, it is important to identify persons or offices empowered to enter into commitments at different stages of agreement negotiation.<sup>24</sup> It is also important to foresee in the concession law the proper allocation of powers between the different levels of government (central and local authorities) during the negotiation and implementation of the project.<sup>25</sup> In order to consider a wide range of factors and thus allocate risks effectively, Recommendation 12 of the UNCITRAL Legislative Guide

advises against drafting legislative provisions that limit unnecessarily the negotiating ability of the parties.<sup>26</sup>

### Principle 8 MCL should allow for enforceable court or arbitral determinations.

Explanation: According to this principle, the MCL should ensure the possibility to protect the rights and interests of both parties under an effective system of dispute resolution (including the possibility for international arbitration and enforcement of arbitral awards). This principle is especially important for creating a more secure, predictable and attractive climate for investors.

Sources: This principle is largely based on the Recommendation 69 of the UNCITRAL Legislative Guide, which stresses the importance for the MCL law of awarding parties the freedom to agree to a dispute settlement mechanism that is regarded by them as the most suitable according to the nature of the project.<sup>27</sup>

### Principle 9 MCL should allow for state undertakings and guarantees.

Explanation: This principle refers to the importance of the MCL containing provisions that allow the government a possibility to support the project financially or guarantee the contracting authority's proper fulfilment of its obligations. Government support is often essential for increasing the level of comfort of potential investors, enhancing the attractiveness of investment as well as for supporting the execution of projects.

Sources: Recommendation 13 of the UNCITRAL Legislative Guide suggests that the MCL should contain clear provisions with regard to both the type of authorities that may provide support and the type of support provided.<sup>28</sup>

### Principle 10 MCL should accommodate security interests.

Explanation: As a rule, only approximately 30% of a concession project is financed by the concessionaire itself. The other 70% is usually borrowed from the banks (lenders) under a security arrangement according to which the concessionaire gives to the lenders security over its rights under the concession agreement. However, in order for this security to be effective, the state should also provide an assurance that in case of the security's enforcement, the proper procedures would allow the concession to be carried out and the lenders to "step-in" to the concession agreement.<sup>29</sup> Thus, this mechanism guarantees the continuation and sustainability of the concession project and effectiveness of the investment.

Sources: Recommendation 49 of the UNCITRAL Legislative Guide emphasises the importance of inclusion in the MCL provisions guaranteeing the right of a concessionaire to secure any financing required for the project with a security interest in its property, pledge of shares of the project company, proceeds and receivables or other suitable security.<sup>30</sup> This principle is also supported in Article 16 of the OECD Basic Elements of a Law on Concession Agreements, which states that the concessionaire can create security over its rights to any payments and receivables under the concession agreement. (See also UNCITRAL Model Legislative Provision 35).

### TERMINOLOGY

- BOO (Build Own Operate)
- BOT (Build Operate Transfer)
- Core Principles (EBRD Core Principles for a Modern Concession Law)
- EBRD (European Bank for Reconstruction and Development)
- LTT (Legal Transition Team)
- MCL (Modern Concession Law)
- OECD (Organization for Economic Development and Cooperation)
- PPP (Public Private Partnership)
- PSP (Private Sector Participation)
- UNCITRAL (United Nations Commission on International Commercial Law)
- UNIDO (United Nations Industrial Development Organization)

### PS

- 1- See in particular EBRD Concession Law Assessment at; <http://www.ebrd.com/country/sector/law/concess/assess/index.htm>
- 2- European Commission Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions (2004); European Commission Guidelines for Successful Public-Private Partnerships (2003).
- 3- European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02), Part 2.4.
- 4- European Commission Guidelines for Successful Public-Private Partnerships (2003); European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02).
- 5- UNIDO BOT Guidelines, Chapter 4, pp. 42-43.
- 6- UNCITRAL Legislative Guide, Recommendation 1.
- 7- UNCITRAL Legislative Guide, Chapter 1, para 10.
- 8- UNCITRAL Legislative Guide, Recommendation 2, Chapter 1, para 17.
- 9- UNCITRAL Legislative Guide, Recommendation 4, Chapter 1, para 18.
- 10- UNCITRAL Legislative Guide, Recommendation 3, Chapter 1, para 19.
- 11- UNCITRAL Legislative Guide, Recommendation 5, Chapter 1, para 20.
- 12- European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02), Part 2.1.
- 13- European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02), Part 2.2.
- 14- European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02), Part 2.4.
- 15- UNIDO BOT Guidelines, Chapter 4, p. 46.
- 16- UNCITRAL Legislative Guide, Recommendation 58.
- 17- OECD Basic Elements of a Law on Concession Agreements, 1999-2000, Art. 18.
- 18- UNCITRAL Legislative Guide, Chapter 1, para 46.
- 19- UNCITRAL Legislative Guide, Recommendation 10, Chapter 1, para 49.
- 20- UNCITRAL Legislative Guide, Recommendation 14, Chapter 3, para 10-16.
- 21- UNCITRAL Legislative Guide, Recommendation 39, Chapter 3, para 127-28.
- 22- European Commission Interpretive Communication on Concessions under Community Law (200/C 121/02), para 3.1.1. (rules for the selection of concessionaires should be made public, they should be equally applied; principle of competition should be adhered to); para 3.1.2. (transparency of the selection rules and procedures, advertising); para 3.2.3. (rules and decisions are available for a review); European Commission Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, para 29 (transparency of the selection procedure, advertising, competition); OECD Basic Elements of a Law on Concession Agreements, para 5.2.6.1 (transparency of the selection process); para 11.1 (clear regulation of non-competitive procedures).
- 23- UNCITRAL Legislative Guide, Chapter 1, para 7-9.
- 24- UNCITRAL Legislative Guide, Recommendation 2, Chapter 1, para 17.
- 25- UNCITRAL Legislative Guide, Chapter 1, para 17.
- 26- UNCITRAL Legislative Guide, Recommendation 12, Chapter 2, para 21.
- 27- UNCITRAL Legislative Guide, Recommendation 69. See also Model provision 49 of the UNCITRAL Legislative Provisions.
- 28- UNCITRAL Legislative Guide, Recommendation 13.
- 29- OECD Basic Elements of a Law on concession Agreements. Explanatory notes to Art. 16, p. 27.
- 30- UNCITRAL Legislative Guide, Recommendation 49.

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