



PRIVATE INITIATIVE MECHANISM IN CONCESSION LEGISLATION: DEVELOPMENT OUTLOOK FOR RUSSIA

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ABSTRACT

Dynamic development of concession laws according to the author of the article results in growing number of concession projects. The article analyzes effects of recent key amendment to Russian Federal Law on Concession Agreements

and Contracts that enhanced legal field for initiative of private investors. The development of legislation takes into consideration market demand and provides for quality enhancement of contracts and implementation tools in the PPP sphere.

Key words: public-private partnership, concession, private initiative, law, legislation, economics, project development, implementation conditions.

Background. At present, concession agreement is the most common form of public private partnership in Russia. The immediate effect there-of is a dynamic development of the concession legislation in Russia. The Federal Law 115 «On Concession Agreements and Contracts» [1] adopted in 2005 has undergone a dozen alterations. Recent amendments made in the summer 2014 by the Federal Law 265 to the Federal Law 115, have become truly revolutionary in terms of guarantees for private investors.

Objective. The objective is to analyze tools of implementation and possible impact of newly amended legislation with a view to enhancing possibilities to develop public private partnerships.

Methods. The article is based on legal analysis, comparative case study and economic assessments.

Results. The adopted amendments cover various aspects of concession projects implementation – beginning from the stage of preparation and ending with guarantees in case of concession agreement termination to parties which await results (benefits).

The main objective of the adopted changes is to give further impetus in order to see the growing of number of infrastructure projects, implemented on the basis of concession agreements. In particular, after amendments, implied by the Federal Law 265 and entered into force from May 1, 2015, it became possible to conclude concession agreements by private initiative of potential concessionaire (private initiative). This legislative innovation creates a legal framework for cooperation and negotiation of the grantor and the potential concessionaire in relation to concession project implementation since initiate stage of the project.

I.

Innovation can also be assessed positively in the context of improving the efficiency of budget spending, as the pre-investment study of the project is conducted not by the state, but by the potential private partner. It should be noted that relevant rules are formulated in strict compliance with competition basis of organizing and conducting concession tenders [4, p. 11].

According to the new edition of the Federal Law 115 it is possible to conclude a concession agreement under «private initiative» mode without tender procedures only in case if the initiator of the project is actually the only one wanting to sign it on proposed and accepted conditions of the grantor.

The decision on initiation of procedures to make a concession agreement previously was always taken by a public partner. To do this, the public authority had previously to develop technical parameters of the project, organizational and legal framework, feasibility study and other documents for the project, which then laid the basis for the tender documentation (in case of competition).

As a rule, preparation and coordination of these documents with departments take at least six months before a decision is made on the project. The obvious disadvantage of such a procedure for a private partner is lack of consideration of concessionaire's interests in the preparation of project documentation, in particular the imbalance in parties' risks, which often hamper fundraising in the project on more favorable terms, as well as the duration of preparation.

We will try to carry out an analysis of advantages and disadvantages of private concession initiative in comparison with classic concessions. The advantages of private initiative can be deemed to be:

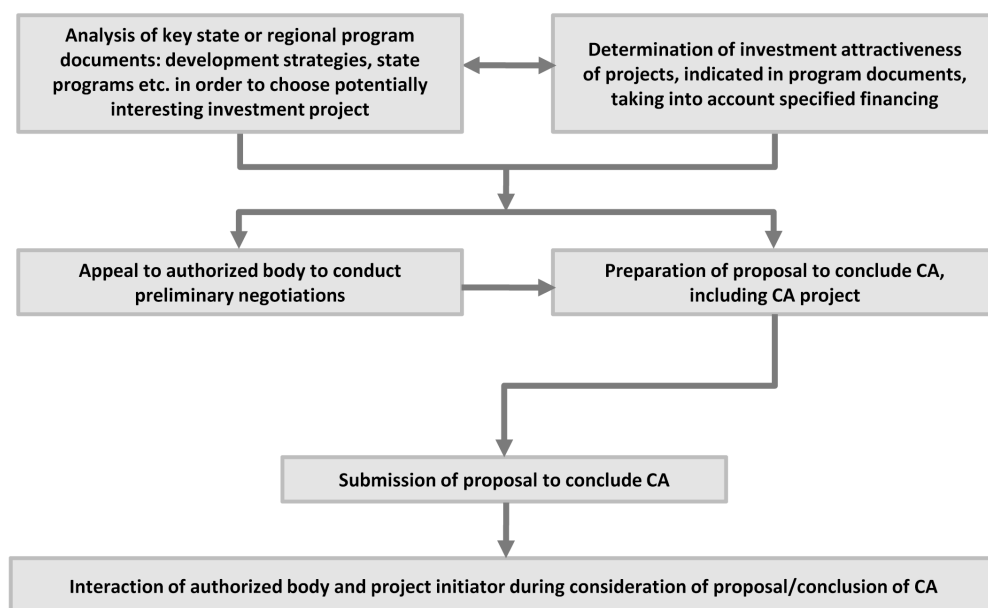
1. encouragement of initiatives of private investors, increasing the number of potential concession projects;
2. shortening the preparation of documentation;
3. lowering costs of grantor for documents preparation;
4. a shorter period for proceeding with a concession agreement, if a tender is not required;
5. improvement of the quality of documents, particularly due to possibility of harmonizing conditions of the concession agreement through preliminary negotiations.

Among the shortcomings we can note:

1. a short timeframe for a decision on the possibility to enter into a concession agreement or on refusal to conclude it;
2. possible absence of sufficient resources at grantor's disposal to handle a large number of proposals on conclusion of concession agreement, as well as to conduct series of negotiations;
3. limited possibilities for pre-selection of participants in case of tender procedures if they are provided for.

Certainly, participation of private partners in development and concession project implementation will allow taking into account the interests of both partners to expand the pool of projects.

It is worth noting that despite a capacity of a private partner to take the initiative, the procedure for concluding such a concession agreement is still based on the rule of competition protection law. According to the law on concessions, before the conclusion of the concession agreement under private initiative mode, a grantor should publish a notice and wait for the expiration of a period when potential participants can express their desire to take part in the competition on conditions, proposed by the initiator and coordinated by the grantor. Only in the absence of those who wish to conclude an agreement on the proposed terms, it can be negotiated with the initiator without competition. Otherwise, if there are applications, expressing willingness to participate in the competition for the



Pic. 1. Possible actions of an investor within the frame of private concession initiative.

conclusion of the concession agreement, the agreement is concluded on a competitive basis in accordance with the law on concessions.

Another important benefit of the application of the mechanism of private concession initiative for both business and state is reduction in the timing of the launch of concession projects by one and a half if the conclusion of an agreement takes place without a tender. If the tender is held, the difference in terms is insignificant. The cost of preparation of projects decreases also for the state (the grantor) by transferring most of the costs of pre-investment study of the project to the initiator.

Thus, amendments established two ways to come to a concession agreement at the initiative of the private partner:

- organizing a concession tender;
- conclusion of a concession agreement without tender with the initiator of the project.

As a general rule, a proposal to sign a concession agreement, once it has been positively considered by the body authorized by the relevant public-law entity, which owns the object of the concession agreement, is published on the Internet in order to obtain offers from other persons that meet the requirements of the Federal Law 115 addressed to the concessionaire. If within the statutory period the authorized body receives applications of readiness to participate in tender for conclusion of concession agreement, then conclusion of concession agreement is performed on a competitive basis. In the absence of applications concession agreement is concluded with the initiator of the project on the terms contained in the proposal, without competition.

Considering the proposal of the potential concessionaire the authority may also offer to conclude a concession agreement on other terms agreed by the parties during further negotiations. Further, according to the results of the negotiation initiator amends the proposal, previously submitted, and re-submits it for consideration by the authorized body. Thus, the amendments to the Federal Law extend the procedures of negotiation to noncompetitive procedure for

concluding a concession agreement. In addition, the parties are free to negotiate prior to submission of the initial offer.

Thus, basic principles of private initiative can be summarized as follows:

- the initiator of the Concession Agreement determines conditions of the concession agreement independently;
- the agreement can be adjusted in the negotiations, carried out by initiator and the authority;
- concession agreement is concluded without competition if there are no other applicants on conditions, proposed by the initiator.

II.

What is the procedure for an investor initiative for concluding the concession agreement?

Let's start with the fact that investor- initiator may be:

- an individual entrepreneur;
- a Russian or a foreign legal entity;
- two or more of these legal entities operating without a legal entity under a partnership agreement (joint activity agreement).

Investor-initiator submits a proposal to sign a concession agreement (including its project) to the owner of the object of the concession agreement, namely:

- Government of the Russian Federation;
- the Government of the constituent entity of the Russian Federation;
- Administration of the municipality.

Alleged actions of the investor as part of a private investment initiative are shown in Pic. 1:

Let's consider in more detailed manner the procedure for making state decision on conclusion of concession agreement on the initiative of the investor [3].

The institute of private initiative provides for a competitive procedure of submission of a proposal to an executive authority to sign a concession agreement. The authorized body within 30 calendar days considers this proposal of the investor- initiator and makes one of two solutions: the possibility to enter into a concession agreement or refusal to its conclusion. The concession





agreement may be concluded on terms proposed by the initiator or the executive authority can return the documents for revision.

In case that the State decides on the need to change the terms of the concession agreement, the authorized agency is negotiating with the investor-initiator in order to agree new conditions of the project.

If a decision is made about the possibility of signing the Concession Agreement, the proposal of the investor-initiator and the project of the concession agreement (or new agreed terms of the concession agreement) are placed on the official website of the Russian Federation on Internet intended for placement of information about tenders – www.torgi.gov.ru.

In the absence within 45 days of requests from other market participants about interest in participating in the tender with original or modified in course of negotiations terms, the Concession Agreement is concluded with the initiator without tender. It should be noted that in this case, the decision of an agreement is made within 30 days. In the case of a positive decision with respect to the initiator of it within 5 working days the draft concession agreement is sent, which should be signed within a period not exceeding one month. Before making a decision on the conclusion of the concession agreement, the initiator shall indicate the sources of funding for the execution of the concession agreement and confirm the possibility of receiving them. This level of supporting funding is not less than 5% of the total cost of the project (only CAPEX is taken into account).

The decision to refuse the conclusion of the concession agreement on the initiative of the investor can be taken in the following cases:

- establishment and / or reconstruction of the object of the concession agreement do not correspond to program documents of federal, regional and municipal levels;
- the state has no funds for the concession agreement on the proposed terms;
- creation of the object of the concession agreement is not required;
- the object of the concession agreement does not require reconstruction;
- the object of the concession agreement is withdrawn from the market / limited in circulation;
- the state has no property right to the object of the concession agreement;
- the object of the concession agreement is not free of third party rights (except in cases where the project may attract third party, which has a right to the object);
- the proposal does not comply with the approved scheme of heat supply, water supply and sanitation – respectively for the objects of this type;
- the activity of the investor- initiator on operation of the object of the concession agreement is prohibited by law;
- the investor- initiator refused negotiations on changing the proposed terms of the concession agreement or negotiating parties have not come to an agreement;
- In other cases, directly stipulated by federal laws (now these named cases are not specified by the federal law).

In order to ensure the practical implementation of «private initiative» by Resolution of 31 March 2015 № 300 the Government of the Russian Federation approved the form of proposals for conclusion of a concession agreement with a person who is taking an initiative to sign a concession agreement (hereinafter – the form of the

offer). The adoption of the form is provided for in paragraph 4.3 of Article 37 of the new edition of the Federal Law 115.

Adoption by the Government of the Russian Federation of the form of the offer will allow initiators now start preparing the first pilot projects carried out under the new procedure.

The form of the offer overlaps with provisions of Article 37 of the Federal Law 115 as for the requirements for an initiator and initiatives such as:

- the absence of a decision on liquidation of the legal entity – initiator;
- the absence of a court decision on initiation of bankruptcy proceedings against the initiator;
- lack of arrears of taxes, debts on other mandatory payments;
- information on the availability of financing sources for execution of a concession agreement and confirmation of collectability of not less than 5% of the total project cost.

This form partially sets new requirements for information, indicating by the initiator for the initiative, for example, information about presence / absence of project documentation, estimated cost of the project, information on the use of innovative technologies.

Nevertheless, the use of a single form of proposals will unify information provided by initiators for the initiative, thus simplifying preparation of documents necessary to the initiator and its consideration by the authority.

However, it should be said that the document still does not answer a number of questions: for example, how it is confirmed that the initiative complies with program documents? How the initiator can independently define a period for the transfer of the object of concession agreement and (or) other property by the grantor to the concessionaire, if the object is created from scratch? Or how to determine which authority will exercise powers of the owner in relation to the type of property that is the subject of the concession agreement?

At the same time, the form contains directions of the range of information to enable the competent authority to decide on project feasibility: for example, technical and economic characteristics of the object of the concession agreement, description of goals and objectives of the proposed project, and so on.

III.

As we understand it, on the one hand, the introduction of private concession initiative may result in additional private investment in the infrastructure of the Russian Federation and budget savings in the preparation of projects. On the other hand, the initiator of the project will not have guarantees that an agreement will be concluded with him, and that the project will be supported in principle, as competent authorities have a list of grounds for refusal to the conclusion of concession agreement by private initiative. Meanwhile, this issue is crucial for initiators of the project. In this context, the question of cost compensation of the private partner is crucial, if he did not win (and the agreement has not been concluded with him without tender), as well as the possibility of granting bonuses to the initiator of the project at the tender.

If we speak about the world experience, the institution of private initiative in the implementation of public-private partnership projects for many years has been used successfully overseas, in most countries (such as Italy, USA, Chile, Argentina, Australia).

In a number of countries measures to encourage initiators are applied. The most common measure of compensation for the costs of the applicant is original recording amount of cost compensation of the initiator

for project preparation if he is not a winner in the tender documentation (if there is a tender). The burden of reimbursement of the initiator lies to tender winner.

Based on the experience of foreign countries in this regard, there are three categories of countries, classification basis of which is a particular incentive mechanism [3]:

- “Bonus system». The essence of this system lies in the fact that in an open call for proposals the initiator's proposal will be considered winning if its value exceeds the value of the best offers by no more than a certain percentage, usually 5%. The bonus depends on the amount of public investment needed for the project. The more budgetary funds are required for the project, the lower is the bonus provided to the proponent. Such a system is used in Chile and South Korea;

- “Swiss system». In accordance with this approach in an open bidding proponent initially has no advantage in the form of a bonus, but in the event of a better offer from another party, the initiator has a right to conclude an agreement on the same terms. A similar mechanism is used in Italy and the Philippines;

- “Mixed system». Project initiators are consistently provided with first bonus and then right of the last offer. If the cost of initiator's proposal exceeds the value of the best offer by no more than 5%, then the winner is the initiator, and if the value of the initiator's offer exceeds the value of the best offer by 5–20%, then both parties have a right to change their proposals. However, at this stage of the evaluation of proposals initiator's bonus is not taken into account. Such a system is used in Argentina and South Africa.

In contrast to the international experience the Russian legislation to date does not provide for granting of any incentives to the initiator and compensation of his costs. In the future, any of above mechanisms can be adapted to the Russian order to enter into agreements within private concession initiative.

Currently, an important and unresolved issue is the procedure for compensation of initiator's expenses, if as a result of the tender a concession agreement will be concluded with another person. International experience shows that, as a rule, if a concession agreement is concluded not with the initiator, costs incurred for the development of proposals, are offset by the winner. The concession legislation does not prohibit the payment of expenses to the initiator. At the same time, the use of such a

mechanism in the Russian practice is unlikely now. However, it is worth noting that in foreign countries the principles of competition protection are complied with in this case by the initial recording in the tender documentation compensation amount of the applicant's costs for preparation of the project. The difficulty is in determining the scope of the applicant's costs. Usually, in some countries it is a fixed percentage of the cost of the proposal, for example, in Argentina it is 1% of the value of the initiator's offer. In Chile, the initiator's costs evaluation is based on the average market price for the services used in the preparation of the proposal. In Italy, the compensation is made in accordance with calculations made by the initiator and included in the business plan as a part of the proposal for concession agreement conclusion. The amount of compensation includes the cost of work on the preparation of a proposal for concession agreement conclusion, and the cost of the proposal taking into account the costs of intellectual property rights.

It should also be noted that one more gap in a private initiative procedure is an unresolved question about whether the initiator of the concession project has to provide to the authority any guarantee of the Concession Agreement in the event that there are no others, who are wanting to participate, and, accordingly, whether other participants should provide them, expressing their desire to take part in the tender. Initiation and the ability at any time to withdraw from the project lead to financial and time losses of executive body for consideration and study of the project.

Conclusion. However, in spite of above mentioned problems and many other questions, private initiative mechanism can be assessed positively and be effective for a number of investment projects, e. g. for unique projects where the competition level is low, or for those, which are interesting for a limited number of investors.

Private initiative mechanism gives a chance to the initiator to accelerate the launch of the project (provided that the executive authority takes a decision on its implementation) and enter into an agreement without a tender (if none of the potential participants declares their intention to participate in the tender). Time will tell whether this mechanism will be sought after by investors, and whether it will lead to a significant increase in the number of concession projects and improve the quality of their preparation.

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