

THE PUBLIC-PRIVATE  
PARTNERSHIP  
LAW REVIEW

FIFTH EDITION

**Editors**

Bruno Werneck and Mário Saadi

THE LAWREVIEWS

THE PUBLIC-PRIVATE  
PARTNERSHIP LAW  
REVIEW

FIFTH EDITION

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**Editors**

Bruno Werneck and Mário Saadi

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# PREFACE

We are very pleased to present the fifth edition of *The Public-Private Partnership Law Review*. Notwithstanding the number of chapters in various publications in The Law Reviews series on topics involving public-private partnerships (PPPs) and private finance initiatives (in areas such as projects and construction, real estate, mergers, transfers of concessionaires' corporate control, special purpose vehicles and government procurement), we identified the need for a deeper understanding of the specific issues related to this topic in different countries.

In 2014, Brazil marked the 10th year of the publication of its first Public-Private Partnership Law (Federal Law No. 11,079/2004). Our experience with this law is still developing, especially in comparison with other countries where discussions on PPP models and the need to attract private investment in large projects dates from the 1980s and 1990s.

This is the case for countries such as the United Kingdom and the United States. PPPs have been used in the United States across a wide range of sectors in various forms for more than 30 years. From 1986 to 2012, approximately 700 PPP projects reached financial closure. The United Kingdom is widely known as one of the pioneers of the PPP model; Margaret Thatcher's governments in the 1980s embarked on an extensive privatisation programme of publicly owned utilities, including telecoms, gas, electricity, water and waste, airports, and railways. The Private Finance Initiative was launched in the United Kingdom in 1992, aiming to boost design-build-finance-operate projects.

In certain developing countries, PPP laws are more recent than the Brazilian PPP law. Argentina was the first country in Latin America to enact a PPP Law (Decree No. 1,299/2000, ratified by Law No. 25,414/2000). The Argentinian PPP Law was designed to promote private investment in public infrastructure projects that could not be afforded exclusively by the state, especially in the areas of health, education, justice, transportation, construction of airport facilities, highways and investments in local security. In Mozambique, Law No. 15/2011 and Decree No. 16/2012 govern the Public-Private Partnerships Law and other related PPP regulations, which establish procedures for contracting, implementing and monitoring PPP projects. In Paraguay, a regulation establishing the PPP regime has been enacted (Law No. 5,102) to promote public infrastructure and the expansion and improvement of services provided by the state; this law has been in force since late 2013.

In view of the foregoing, we hope a comparative study covering practical aspects and different perspectives regarding PPP issues will become an important tool for the strengthening of this model worldwide. We are certain this study will bring about a better dissemination of best practices implemented by private professionals and government authorities working on PPP projects around the world.

With respect to Brazil, the experience evidenced abroad may lead to the strengthening of this model. One specific feature of the PPP law in Brazil, for instance, is state guarantees. This



feature permits that the obligation of the public party to pay a concessionaire be guaranteed by, among other mechanisms authorised by law: a pledge of revenues; creation or use of special funds; purchase of a guarantee from insurance companies that are not under public control; guarantees by international organisations or financial institutions not controlled by any government authority; or guarantees by guarantor funds or state-owned companies created especially for that purpose.

The state guarantee pursuant to PPP agreements is an important innovation in administrative agreements in Brazil; it assures payment obligations by the public partner and serves as a guarantee in the event of lawsuits and claims against the government. This tool is one of the main factors distinguishing the legal regimen of PPP agreements from ordinary administrative agreements or concessions – one that is viewed as crucial for the success of PPPs, especially from a private investor's standpoint.

Nevertheless, the difficulty in implementing state guarantees on PPP projects has been one of the main issues in the execution of new PPP projects in the country. This is made worse by the history of government default in administrative contracts.

In other jurisdictions, however, state guarantees are not a rule. Unlike PPP projects in developing countries, government solvency has not historically been a serious consideration in other jurisdictions. That is the case in countries such as Australia, France, Ireland, Japan, the United Kingdom and the United States.

We expect that the consolidation of PPPs and the strengthening of the government in Brazil may lead to a similar model, enabling private investments in areas where the country lacks the most.

Brazil must adopt cutting-edge models for awarding PPP agreements. The winner is usually chosen based solely on the price criterion (offering of lower prices or highest offers), which sometimes leads to projects lacking advanced or tailor-made solutions. Despite the legal provisions on the role of technical evaluation of offers, they are becoming less relevant. However, some ongoing discussions regarding amendments to the Brazilian procurement legislation and new criteria, which are based on the international experience, could (fortunately) be approved.

We highlighted some discussions regarding the amendment to the Federal Procurement Law (Federal Law No. 8,666/1993), which is expected to expedite public procurement in Brazil. One of the main innovations proposed in this debate is the competitive dialogue, a type of bid in which the authority engages with bidders to discuss and develop one or more solutions for the tendered project. After the conclusion of the dialogue phase, the authority will establish a term for the submission of bids.

Competitive dialogue is a reality in many jurisdictions (e.g., Australia, Belgium, China, France, Ireland, Japan and the United Kingdom). In Japan, for example, some projects are procured through the competitive dialogue process. This process may be adopted if a relevant authority is unable to prepare a proper service requirement, in which case it proposes a dialogue with multiple bidders simultaneously to learn more about the specific service it seeks to implement. As another example, in France a dialogue will be conducted with each bidder to define solutions on the basis of the functional programme. At the end of the dialogue period, the procuring authority will invite the candidates to submit a tender based on the considered solutions. After analysis of the tenders, a partnership contract will be awarded to the bidder with the best price in accordance with the criteria established in the contract notice or in the tender procedure. We hope the importance of this tool is recognised in Brazil and reflected in our legislation.

Further, the Investment Partnerships Programme, as established in Federal Law No. 13,334/2016, is a legal plan regarding infrastructure development in the country, providing conditions for the attraction of investments in infrastructure projects and creating environments for greater integration between public and private sectors.

The PPI is comprised of two relevant bodies within the federal government: the PPI Board and the PPI Secretariat. The first one evaluates and recommends to the President the projects that should be part of the PPI, as well as decides on subjects concerning the execution of partnership contracts and privatisations. The second one is a taskforce that acts in support of the Ministries and Regulatory Agencies to execute the PPI's activities. These entities, together with other bodies and controlling agencies, are expected to act in an articulated manner as to ensure stability, legal certainty, predictability and effectiveness of the investment policies.

With regard to the plans of the president-elect for infrastructure investments in Brazil, the responsible governmental team has already confirmed the continuity of the PPI, linked to the presidency and preserving the members of its current technical team. In addition, the new government team endorses the development of a programme by PPI to support public-private partnerships of states and municipalities, which would mainly cover sanitation and public lighting sectors. Given the lack of operational, technical and economic-financial ability of municipalities to manage such programmes, the federal government is expected to act closely with local entities to boost projects in priority areas.

In the fifth edition of this book, our contributors were drawn from the most renowned firms working in the PPP field in their jurisdictions. We would like to thank all of them for their support in producing *The Public-Private Partnership Law Review*, and in helping with the collective construction of a broad study on the main aspects of PPP projects.

We strongly believe that PPPs are an important tool for generating investments (and development) in infrastructure projects and creating efficiency not only in infrastructure, but also in the provision of public services, such as education and health, as well as public lighting services and prisons. PPPs are also an important means of combating corruption, which is common in the old and inefficient model of direct state procurement of projects.

We hope you enjoy this fifth edition of *The Public-Private Partnership Law Review* and we sincerely hope that this book will consolidate a comprehensive international guide to the anatomy of PPPs. We also look forward to hearing your thoughts on this edition, and particularly your comments and suggestions for improving future editions of this work.

**Bruno Werneck and Mário Saadi**

Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados

São Paulo

March 2019

# PORTUGAL

*Manuel Protásio and Catarina Coimbra<sup>1</sup>*

## I OVERVIEW

The public-private partnership (PPP) model started to be widely used from the 1990s onwards, with the purpose of equipping the country with modern infrastructure and services. The sectors that attracted more private investment in PPP have been, mainly, the road infrastructure and health sectors, with the innovative feature of placing clinical National Health Service (NHS) hospitals under private management with an aggressive risk allocation to the private sector. Such PPP activity was boosted further after the international financial crisis of 2008, with the purpose of enhancing the Portuguese economy's poor performance.

As a consequence of the sovereign debt crisis of 2011 and in the context of the bailout advanced by the European Union (EU) and the International Monetary Fund (IMF), the Portuguese government was forced to introduce an austerity programme. As a result, public funding for investment in public infrastructure was materially reduced and the government endeavoured to reduce the significant payments to be made by the Portuguese state under PPP contracts.

With this aim in mind, the government started a negotiation process with PPP concessionaires in January 2013. In several roads PPPs the negotiation process was successful and agreements were reached.

During this period, companies have also experienced difficult conditions, mainly owing to liquidity constraints and to the slowdown of the Portuguese PPP and construction markets in connection with the economic crisis, leading many of those companies to search for new opportunities in foreign markets, in particular in the Portuguese-speaking countries in Africa.

At the beginning of 2014, the Portuguese government approved the Strategic Plan for Transport and Infrastructure, which selects some infrastructure projects that may bring positive economic effects to Portugal between 2014 and 2020. The modernisation of the Portuguese rail freight sector, the development and increase in capacity of major Portuguese ports, a few projects in the road sector deemed essential to complete the road network, as well as the increase of cargo capacity at Lisbon Airport, are some of the priority projects. Owing to diverse aspects, such as limitations of the new European funds framework, some of these future infrastructure projects may be launched and executed under a PPP model.

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<sup>1</sup> Manuel Protásio is a partner and Catarina Coimbra is an associate at Vieira de Almeida.

## II THE YEAR IN REVIEW

Over the past few years the growth of the PPP business in Portugal has been slow, with few greenfield projects coming to the market.

In addition to the recurring renegotiations within the existing road PPP contracts, the international public tender for design, construction, financing, operation and maintenance of the Hospital Lisboa-Oriental Complex, having already been postponed twice, has seen proposals submitted on 31 January 2019; its current stage concerns the analysis and evaluation of those proposals in order to select a maximum of three bidders to move to the negotiation phase. This is the first time in Portugal that a PPP in the health sector has been launched solely for the construction, operation, maintenance and management of the hospital building, staying the responsibility of the management of the clinical services in the hands of the NHS and not in the hands of a private entity.

2018 was also the year in which the Portuguese government approved the extension of the PPP contract concerning the management of the clinical services of the Hospital of Cascais until 31 December 2021, by which time a new public tender will be launched. Conversely, regarding the Hospital of Braga (which is, according to the Court of Auditors, one of the most efficient of the NHS, with less cost per patient than any other hospital), the existing PPP contract will expire on 31 August 2019 and the Portuguese government has already approved the launch of a new public tender for the management of clinical services of the hospital under a PPP model.

Further, the tender procedure concerning the extension of the Porto underground system launched in 2017 is now reaching its final stage, the beginning of the construction works being expected in 2019.

Nonetheless the award of these new PPP contracts, the renegotiation and restoring of the financial balance of the existing road PPP contracts (that covered the reduction of service requirements and availability payments and, in some road PPP contracts, the possible extension of the maximum duration of the concession contracts) is still the main subject matter and they still substantially contribute to the public expenditure.

Portugal is still one of the European countries with the highest costs assigned to PPP projects (mainly in the road sector), notwithstanding the slowdown in relation to new PPP-based projects over the past few years. In fact, according to the statistical information provided by the European Commission, Portugal recorded the highest ratio of PPP over total gross fixed capital formation between 2000 and 2014, which demonstrates the relative weight of PPP projects within the Portuguese economy.

Evidence of this is the choice of Portugal as the host country for the International Centre of Excellence on PPPs in water and sanitation, on May 2017, with the signing of a memorandum of understanding between the UNECE Executive Secretary and the Secretary of State for the Environment in Portugal. The Centre, affiliated to the UNECE International PPP Centre of Excellence in Geneva, will be hosted by the National Laboratory of Civil Engineering (LNEC) in Lisbon and was created with the aim of assist low- and middle-income countries to utilise PPP-based projects for water supply and sanitation services.

## III GENERAL FRAMEWORK

### i Types of public-private partnership

Decree Law 111/2012 of 23 May 2012 revoked the initial PPP legislation and establishes the general rules applicable to any PPP launched by the Portuguese state.

It introduced several amendments to the previous PPP regime, in particular regarding the preparation, launching, execution and modification of PPP.

Both institutional and contractual PPP structures are available in Portugal. However, institutional PPP structures are not commonly used. In fact, the majority of PPP projects closed to date in Portugal are based on project finance contractual structures and typically follow a build–operate–transfer or design–build–finance–operate model.

The underlying contractual framework of a PPP transaction in Portugal traditionally includes a concession contract giving the project company the right to carry out the project or the relevant activity, equity subscription and shareholders' agreements to regulate the relationship between the sponsors or project company's shareholders and the equity contributions to the project, a typical set of finance documents, as well as project implementation and sector-related commercial contracts. Among these, there is typically a construction contract and an operation and maintenance contract in infrastructure PPP projects. Supply agreements, sales agreements or both may also be entered into in connection with the project.

In the vast majority of the Portuguese PPP transactions closed to date, the concession-based construction contracts used do not follow any standard form, such as those issued by the International Federation of Consulting Engineers, the Joint Contracts Tribunal, or the Institution of Civil Engineers. Hence, the form of construction contract used in each case has varied depending on the sector of industry at stake or the sponsors involved.

In relation to the infrastructure projects closed in Portugal in the 1990s and early 2000s, it was generally accepted that, given the need to adapt the legal structure of the facility agreements to international syndication, the whole financing package other than the security documents had to be governed by English law, while the project documents, notably the concession contract, were subject to Portuguese law. That ceased to be the case from the mid 2000s onwards, at which point the project financiers active in Portugal had become sufficiently comfortable with the Portuguese law and, therefore, most finance documents executed thereafter are governed by Portuguese law, notwithstanding closely following the structure of a typical English law project finance documentation package.

PPP major projects in the health sector, the second most relevant sector concerning PPP projects, also have some particularities in Portugal. The specific framework for PPPs in health sector, set out in Decree Law 185/2002 of 20 August 2002, as amended by Decree-Law 111/2012, of 23 May 2012, is still in place. The Decree Law, as amended, governs the development of PPPs for the construction, financing, operation and maintenance of healthcare units forming part of the NHS. An important feature of these PPPs is that they may envisage the private partner not only managing the hospital facilities but also providing clinical services as part of the NHS. When both managing facilities and clinical services provision are foreseen, two separate project companies must be incorporated. In such case, both project companies are bound to comply with their own obligations under a sole concession agreement, and one concessionaire is liable before the other provided that the non-compliance of its own obligations may give cause to the other concessionaire's infringement under the concession agreement. The health sector concession agreements set out different contractual periods for each concessionaire (10 years for the clinical services providers – which may be extended for additional 10-year periods up to a maximum of 30 years – and 30 years for the concessionaires responsible for the design, construction and operation of the hospital buildings).

In 2016, PPP projects in the health sector were subject to an evaluation by the Health Regulatory Authority (ERS), in order to assess the quality of healthcare provided under the mentioned projects. According to this study, the quality of clinic services provided by the private partner is similar to that of the services provided by the state-run public utilities. Notwithstanding the positive performance, the Portuguese government has set a target to reduce the public burden of PPP projects in the health sector. Therefore, renegotiations with the private partners are ongoing to reduce public payments. In this context, as mentioned above, the PPP regarding the Hospital of Cascais was extended for an additional three-year period and the Portuguese government has approved the launch of a new public tender for the management of clinic services of the Hospital of Braga.

In the road sector, different solutions were put in place regarding the concessionaires' payment mechanism and risk matrices. Shadow toll systems were introduced in some road projects during the 1990s and onwards, but in all those projects such payment systems were replaced by road availability payments and real toll payment systems. An exception was made in Madeira and Azores, where the regional political authorities chose to maintain the shadow toll systems previously adopted in their respective road projects. More recently, real toll payment mechanisms were also substituted by road availability solutions under the recent renegotiation process on the PPP projects of the road sector. This renegotiation process also brought about specific solutions, including a set-off mechanism against toll revenues for the benefit of the concessionaires and an upside-sharing mechanism to encourage concessionaires to promote traffic in their concessions. At a municipal level, PPP activity took place through the launch of several projects for municipal water supply, wastewater treatment and waste management; Decree Law 90/2009 of 9 April 2009, and Decree Law 194/2009 of 20 August 2009, as amended, established the rules applicable to PPPs in the aforementioned sectors.

## **ii The authorities**

In general terms, the sector ministries (energy, infrastructure, transports, health, etc., and (when applicable) environment) are responsible for the launching, licensing and major regulation of the projects, either directly or through their governmental departments.

The approval of the Ministry of Finance is also required when the project involves public investment or, more generally, where the PPP legal framework applies.

Decree Law 111/2012 introduced several amendments to the previous legal regime, in particular regarding the preparation, launching, execution and modification of PPPs.

The main purpose of this new legal framework is to reinforce supervision, scrutiny and consistency of the decisions of the public partner and contemplates the creation of the Technical Unit for Monitoring Projects, which centralises and executes all main tasks related to the preparation and execution of PPP contracts.

Other PPP projects at a municipal or regional level are prepared and executed by the respective public structures and such projects are not subject to the Technical Unit for Monitoring Projects's control.

## **iii General requirements for PPP contracts**

The legal framework applicable to the PPP projects expressly foresees the need to accommodate the type of expenditure within budgetary regulations and requires the preparation of economic and financial surveys to confirm the figures for the public sector comparator, as well as establishes general procedure rules applied to any type of PPP contracts.

Projects that require a global public cost above €10 million and an investment not higher than €25 million for the entire contractual period are not subject to the legal regime of the Decree Law 111/2012 of 23 May 2012.

Since the previous PPP Decree Law, dated 2003 (Decree Law 86/2003 of 26 April 2003), procurement procedures may only be launched and awarded after approval of the relevant environmental impact declaration and once the relevant environmental and urban planning licences and permits have been obtained, in order to ensure an effective transfer of execution risks to the private partner.

The regime concerning environmental impact assessment for each project was approved by Decree Law 151-B/2013 of 31 October 2013, as amended, pursuant to which any application for an environmental approval must enclose a detailed environmental impact study, the procedure for granting the relevant environmental impact decision implying a coordinated effort between a different array of entities for better assessment of the environmental risks associated with each project.

Depending on the sector of industry in question, a project may also be subject to environmental licensing under the new integrated pollution prevention and control legal framework, approved by Decree Law 127/2013 of 30 August 2013. The environmental licence (which is required, in particular, for industrial projects) must be obtained before operation commences and must be successively renewed during the entire period of operation of the plant, although simplified licensing procedures may be in place in accordance with the scope of the activities carried out.

Furthermore, in the context of the EU emissions trading system, for projects in certain industrial sectors and meeting certain conditions or thresholds, the operators must hold a permit to emit greenhouse gases, and be the holder of emission allowances.

Other industrial and construction licences and permits may be required depending on the type and specific conditions of each project to be implemented.

Finally, it should be noted that compliance with all legal conditions and procedures is subject to validation by the Court of Auditors. After the execution of a PPP agreement by any public entity, the Court of Auditors will verify and confirm whether all legal requirements are fulfilled and payments under those contracts can only be made further to such validation.

#### **IV BIDDING AND AWARD PROCEDURE**

Decree Law 111-B/2017 of 31 August has amended the Portuguese Public Procurement Code (PPC) approved by Decree-Law 18/2008 of 29 January.

The PCC applies to every public tender procedure launched by a public authority. The Code sets out different procedures for the procurement process applicable to administrative contracts, including those to be entered into in connection with PPP projects: the direct agreement, the public tender, the limited tender by pre-qualification, the negotiation procedure and the competitive dialogue. Unsolicited bid mechanisms are not foreseen in Portuguese law. Unlike the former legal framework for public procurement, the PCC does not automatically require a public tender for public works concessions or public services concessions, the awarding entity being entitled to choose between the launch of a public tender, limited tender by pre-qualification or a negotiated procedure.

In each procedure allowed by the PCC, administrative principles of equal treatment, legality, transparency and competition are duly reflected in the respective regulation. Moreover, such principles are directly applicable to each procedure and may be invoked

by any interested party. If an interested party considers that an act under the procurement procedure does not comply with applicable regulation and principles, it may claim directly to the awarding entity but also to a court. In such case, the interested party may ask the court to declare the suspension of all subsequent acts in the procurement procedure by means of a temporary injunction, in order to ensure that its rights are not irreversibly threatened.

Substantive provisions dealing with public works and the public services concessions are included in the PCC, some of which are mandatory in nature. These mandatory provisions refer to relevant features of a PPP, such as termination by the contracting authority, and sequestration or step in. Other substantive provisions of the PCC will only apply in the absence of express provision in the relevant contract.

The granting of the approval by the Court of Auditors is a condition for the contracting authority to make any payments under the contract; the contract may, however, enter into force prior to the validation and all rights and obligations contained therein may be performed, except for public payments.

In February 2014, the European Parliament and the Council adopted Directive 2014/25/EU (procurement in the water, energy, transport and postal services sectors), Directive 2014/24/EU (public works, supply and service contracts) and Directive 2014/23/EU (concession contracts). The new Public Procurement Directives were published in the Official Journal of the European Union on 28 March 2014 and entered into force on 17 April 2014.

The recent economic crisis in Europe has made it necessary to reform public procurement rules: first, to make them simpler and more efficient for public purchasers and companies, and second, to provide the best value for money for public purchases, while respecting the principles of transparency and competition. The Directives comprise major changes to the European public procurement regime with the aim of:

- a* promoting environmental policies, as well as those governing social integration and innovation;
- b* improving the access of small and medium-sized businesses to public procurement markets;
- c* implementing stronger measures preventing conflicts of interest and corruption; and
- d* new simplified arrangements for social, cultural and health services listed in the Directives.

Decree Law 111-B/2017 introduced in the Portuguese legislation the European Union Directives, and puts forward several modifications to the existing legal framework. Among other things, the new Public Procurement Code introduced the following amendments:

- a* the most economically advantageous tender becomes the rule criterion for awarding;
- b* the value of the performance bond is reduced to a maximum of 5 per cent of the contract price;
- c* a simplified procedure for the provision of health and social services is foreseen; and
- d* the report obligations of the awarding authority on practices susceptible of distorting competition rules are enhanced.

## **V THE CONTRACT**

### **i Payment**

Remuneration mechanisms diverge considering the different sectors of activity and the different PPP projects.



In the road sector, different solutions were put in place regarding the concessionaires' payment mechanism. Real toll systems and shadow toll systems coexisted under different projects but the shadow toll systems were generally replaced by road availability payments and real toll payment systems. In addition, some real toll payment mechanisms were substituted by road availability solutions under the recent renegotiation process on the PPP projects of the road sector. Upside-sharing mechanisms were set out thereunder to encourage concessionaires to promote traffic in their concessions.

Payments due under the PPP projects in the health sector are linked to the clinical services provided in accordance with a list of medical acts and complexity levels, and also to the availability of the hospital facilities. Both concessionaires are subject to payment deductions if any contractual requirements are not totally fulfilled, and additional revenues can be obtained through the performance in the hospital facilities of other related activities (the revenues of which are to be shared with the awarding entity).

Water supply concessions are generally paid by consumers – both at bulk and retail level – in accordance with the water consumption, the applicable tariff being determined in accordance with the concession agreement.

## **ii State guarantees**

The law establishes a type of sovereign guarantee which may be granted by the Portuguese government to secure payments by the state and related parties, such as state-owned companies or government departments. The maximum amount of the guarantees that may be provided in any given year must be approved and set out in the relevant state budget. However, PPP projects in Portugal usually do not include any type of sovereign guarantee to secure payments from the government or other public entities.

## **iii Distribution of risk**

According to Decree Law 111/2012 of 23 May 2012, project risks are to be shared between the public and private partners according to their capacity to manage such risks. Moreover, a PPP project should imply an effective and significant transfer of risks to the private partner. The concession contract, which is the most common form of PPPs, allocates the relevant project risks between the contracting authority and the project company. The risks that remain with the contracting authority are usually covered by the financial rebalance mechanism, which is a key concept in all concession-based transactions in Portugal.

Typical financial balance events include unilateral variations by the contracting authority, *force majeure* events, specific change of law and construction delays caused by the contracting authority.

Traditionally, archaeological and ground risks were borne by the public partner. That was, however, not the case in the PPP1 Poceirão-Caia high-speed rail project closed in May 2010 (which was cancelled as part as the austerity-led review of PPP projects) and in the PPP hospital projects, where that risk was partially assumed by the project company and transferred by the latter to the contractor.

Nationalisation, expropriation or requisition of private property can only take place on the grounds of public interest and provided that private entities are duly compensated. Public interest may also constitute grounds for termination of the concession contract by the contracting authority, in which case the contracting authority shall compensate the project company for all the damages caused (which may include loss of profit). Some concession

contracts set out the method for calculating the damages incurred by the project company in case of termination by reason of public interest. Such calculation usually takes into account the status of construction.

Other political risks, such as war, civil disturbance or strikes may be considered as events of *force majeure* and, therefore, the project company shall be relieved from its obligations under the concession contract to the extent affected by the relevant event of *force majeure*. *Force majeure* events may trigger the financial balance mechanism and, hence, the project company (and consequently, the construction contractor) shall be compensated. In the case of prolonged *force majeure* or if the restoration of the financial balance of the concession proves too onerous, the concession contract may be terminated.

Changes in law may also be treated as a political risk. Only a specific change in law entitles the project company to financial rebalance. The risk of change in general law is typically assumed by the project company.

In water concession projects additional events may give cause to apply the financial rebalance mechanism, as it is the case of water consumption levels below certain limits or additional infrastructure investment requirements.

The project company generally passes on to the contractor all design and construction obligations, liabilities and risks under a construction contract, which is fully back-to-back with the concession contract.

The contractor usually undertakes to perform the design and construction obligations on a turnkey and fixed-price basis and, hence, it bears the risk of price escalation of the material, equipment or workers. In some cases, the contractor is allowed to revise the price annually to reflect inflation.

Other risks that are transferred by the project company to the contractor under a classic concession-based construction contract include the delay in the completion of the works, approval risk, the risk of damage to the works and defects during the defects liability period.

The risks generally covered by the financial balance under the concession contract do not entitle the contractor to suspend the works or in any way relieve the contractor of its obligations under the construction contract. The contractor shall, however, be entitled to compensation in accordance with the 'back-to-back, if and when' principle, (i.e., the contractor will only receive compensation for any of the relevant events to the extent the project company is compensated for those same events under the concession contract).

With regard to limitation of liability, under general Portuguese law, any party is liable before the other for the breach of its obligations under the relevant contract. All damages caused by such breach must be compensated, including all direct damages and loss of profit but excluding indirect or consequential damages. Portuguese law expressly forbids prior general waivers of the right to compensation, although specific waivers after the occurrence of the fact giving rise to the right to compensation are permitted. It is possible, however, for the parties to agree an amount of liquidated damages for breach of obligations, provided that it represents a reasonable estimate of the damages that may result from such breach. Caps on liability are also generally admitted.

Portuguese project concessionaires usually have unlimited liability under the respective contracts. In recent years, the subcontracts executed by concessionaires with construction and operation and maintenance contractors set out liability caps in line with the commercial practices in other countries.

In contracts where a liability cap is foreseen, the same is often equivalent to the contract price and, since no restrictions are made to the type of damages that are considered for

compensation purposes, the relevant legal provisions will apply. In recent projects, contractors have successfully demanded the introduction of tighter liability caps and the exclusion of loss of profit suffered by the project company.

#### **iv Adjustment and revision**

The risks that remain with the contracting authority are usually covered by the above-mentioned financial rebalance mechanism. If a financial balance event<sup>2</sup> arises, causing a deterioration in the levels of the project ratios, the contracting authority agrees to compensate the project company with a view to restoring the financial balance of the concession.

In general, any amendments to the PPP concession contracts should be subject to the procedures set out in Decree Law 111/2012 of 23 May 2012. These procedures include the creation of a negotiation committee to prepare and execute the negotiations with the private partner to reach a new agreement, which will be subject to a final report and approval process by the relevant government members. Other adjustment mechanisms not focused particularly on the payments are also set out, as is the geographic area the clinical services should encompass under hospital PPP projects. In fact, subject to certain constraints, the public health authority can modify the reference area for each type of medical treatment merely by a decision to be notified to the private partner.

#### **v Ownership of underlying assets**

Other than assets in the public domain (e.g., the hydric domain, mineral resources, roads, railways) which may not be appropriated by private entities, the ownership of land or other assets may be acquired by the private partner.

However, the exercise of a specific economic activity by use or operation of such assets may require a licence and, in the case of an asset of public domain, the attribution of a right of use (of the relevant asset, normally through a concession regime).

It is usual to set out that the private partner should deliver any assets at the term of the contract, even though such assets are owned by the private partner, provided that the same are required to perform the relevant activity under the agreement. The new Public Procurement Code further provides for new rules on the transfer of movable assets by public entities, pursuant to which the transfer may be temporary or permanent, including, for instance, the lease of the relevant assets to the private partner.

#### **vi Early termination**

Concession agreements may be terminated by either party owing to the infringement of the other party's obligations. Also, concession agreements usually foresee the possibility of redemption or early termination on grounds of public interest.

Some concession contracts set out the method for calculating the damages incurred by the project company in such situations, which usually takes into account the status of construction and in some circumstances the financing agreements entered into between the private partner for the purposes of implementing the project.

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2 i.e., an event that typically triggers a unilateral (but permitted) variation of the terms of the contract by the awarding entity or public party, a third party action or event (e.g., certain *force majeure* events), the risk of occurrence of which is allocated to the public party under the contract or the law.

Termination due to one party's failure to comply with its obligations usually does not entitle the non-compliant party to any compensation rights. However, in some PPP projects – as is the case of the hospital PPP projects – compensation may be due in such situations taking into consideration the significant investments made by the private partner that should revert to the public partner.

## **VI FINANCE**

Most the PPP projects in Portugal have been financed pursuant to the project finance structure. The use of project bonds or monoline structures to finance projects was not common until recently, but these instruments have now started to be considered as an alternative or complementary financing tool to traditional project finance (particularly in a brownfield context).

The finance package usually comprises a commercial bank credit agreement (as well as a European Investment Bank (EIB) credit agreement and an intercreditor agreement whenever the EIB is also providing finance to the project), an accounts agreement, a forecasting agreement, security documents and direct agreements between the lenders and the contracting authority or the major project parties, all in a form consistent with international market standards.

The two main types of security that can be created under Portuguese law are mortgages and pledges. Mortgages will entitle the beneficiary, in the event of a default, to be paid with preference to non-secured creditors from the proceeds of the sale of immovable assets or rights relating thereto or of movable assets subject to registration (such as automobiles, ships or planes). Pledges will confer similar rights to those created by the mortgages, but are created in respect of movable (non-registered) assets or credits. Portuguese law does not recognise the concept of a floating charge. Also, it does not permit the creation of security over future assets and, therefore, promissory agreements and assignments in security are entered into to overcome this hurdle. However, since Portuguese law does not recognise the concept of assignment by way of security as existing in most (if not all) common law jurisdictions, the instrument used is a true assignment of rights, with the occurrence of an event of default being either a condition precedent to the assignment or a termination event, depending on the bargaining power of the borrower and sponsors (as applicable). It also should be noted that Portuguese law does not foresee the concept of a security trustee, therefore, there is some uncertainty as to whether a Portuguese court would immediately recognise the authority of a security agent to enforce security interests on behalf of the secured creditors (the collateral takers), on terms similar to those accepted in a common law context.

Also, Portuguese law does not allow for remedies other than outright sale, other than in the case of financial pledges where appropriation of financial collateral is permitted on enforcement of the pledge, provided that the parties have agreed a commercially reasonable mechanism for evaluating the price. Financial pledges may be granted over cash on bank accounts or financial instruments (including shares but not quotas in Portuguese limited liability companies) and, more recently, credits over third parties.

Portuguese project finance documentation generally includes direct agreements between the lenders and the contracting authority and the lenders and any major contractors. All direct agreements contemplate step-in rights in favour of lenders, which may be exercised upon the occurrence of certain events: default of the concessionaire under the underlying contracts and, in certain cases, default of the concessionaire under the finance documents.

Shareholders are generally required to provide on-demand bank guarantees in order to guarantee their equity subscription and other funding obligations. Standby equity commitments to fund general investment, operational costs overruns or loss of revenues are often also supported by on-demand bank guarantees.

In health-sector PPPs, the shareholders have been requested to provide a corporate guarantee that, in the proportion of their shareholding in each project company (the ClinicCo and the InfraCo) and up to a certain amount, any lack of funds in the project and breach of the obligations of the project company.

## **VII RECENT DECISIONS**

No significant dispute under the existing PPP procurement procedures has been registered recently. However, some relevant disputes arose from the performance of those contracts. The main reasons evoked by the concessionaires included the variations imposed by the contracting authorities that were not settled by negotiation under the financial rebalance mechanism. In the first quarter of 2018, the total amount for the restoration of financial rebalances requested by the concessionaires to the state amounted to approximately €660 million. There are still some cases ongoing regarding legislative changes and changes in the corporate tax rates, which had a direct impact in some PPP roads projects. In these cases, the concessionaires are claiming considerable amounts to the state. According to the Stability Programme 2018–2010, presented by the Minister of Finance, the most relevant request of financial rebalance is in respect to one of the road PPPs.

## **VIII OUTLOOK**

The Portuguese economy is recovering, after the conclusion of the three-year EU–IMF adjustment programme in May 2014. There is, however, some uncertainty associated with political pressure – from left-wing parties supporting the government – to avoid PPP schemes, at least in areas of greater social sensitivity, such as health and public transport. Public investment in several infrastructure projects – mainly in the freight rail and port sectors, as stated in the Strategic Plan for Transport and Infrastructure 2014–2020 – is still expected. Whether under a PPP model, these investments should have a significant positive impact on the Portuguese economy and create many business opportunities for all stakeholders in the relevant sectors. Other opportunities may arise from the recent focus of the Portuguese government in developing the Green Economy and Green Growth in Portugal, in relevant areas such as climate and energy, water and waste management, biodiversity and sustainable cities.

The international public tender launched in the end of 2017 for the construction of the Hospital Lisboa-Oriental Complex, which is intended to replace six hospitals of Lisbon, is now reaching its negotiation phase, with the beginning of the construction works expected in 2020. This project includes the design, construction, financing, operation and maintenance of the hospital, and it is probably the most important project under a PPP model launched in recent years.

Public investment in several infrastructure projects is still expected. On the other hand, according to the recently approved State Budget Law for 2019, public expenditure on PPP projects will still be considerable (around €2 billion), especially in the road, health,

railway and security sectors, but it is expected to be slightly reduced compared to 2018, with a decrease particularly in the road sector, a result of the expected conclusion of the renegotiation processes on the existing road PPP contracts.

# ABOUT THE AUTHORS

## **MANUEL PROTÁSIO**

*Vieira de Almeida*

Manuel Protásio was born in Lisbon and graduated in law in 1984 from the College of Law of the Portuguese Catholic University in Lisbon.

He worked on secondment at a Deutsche Bank investment bank subsidiary in Lisbon for approximately one year and has been involved in project finance matters since 1992.

He joined VdA in 1991 and currently is the group executive partner of the infrastructure, energy and natural resources group, and heads the energy and natural resources practice. In this capacity he has participated and led teams involved in the most relevant transactions carried out in Portugal to date on the power (including the renewable energies), oil and gas, road, transport, water and wastes sectors. He has also been actively working in regulation and public procurement procedures of those sectors.

Manuel Protásio is admitted to the Portuguese and Timor-Leste Bar Associations.

## **CATARINA COIMBRA**

*Vieira de Almeida*

Catarina Coimbra was born in Viseu and graduated in law in 2011 from the College of Law of Lisbon University.

She obtained a master's degree in administrative law and public procurement from the School of Law of the Portuguese Catholic University in Lisbon in 2013.

She joined VdA in April 2016 as an associate in the infrastructure and mobility practice. Catarina Coimbra is admitted to the Portuguese Bar Association.

## **VIEIRA DE ALMEIDA**

Rua Dom Luis I, 28

1100-151 Lisbon

Portugal

Tel: +351 21 311 3400

Fax: +351 21 311 3406

mp@vda.pt

ccm@vda.pt

www.vda.pt



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