

**Short Term High Quality Studies to Support Activities under the Eastern Partnership  
HiQSTEP PROJECT**

**STUDY ON THE ANALYSIS OF LICENSING AND FISCAL  
FRAMEWORKS FOR CONCESSION AGREEMENTS IN THE  
ENERGY SECTOR IN THE EASTERN PARTNER COUNTRIES**

**EXECUTIVE SUMMARY**

**OCTOBER 2018**

This report has been prepared by the KANTOR Management Consultants Consortium. The findings, conclusions and interpretations expressed in this document are those of the Consortium alone and should in no way be taken to reflect the policies or opinions of the European Commission.

Preface

## Preface

The present report summarises three Component Reports of the **Study on Analysis of Licensing and Fiscal Frameworks for Concession Agreements in Energy Sector in the Eastern Partnership Countries**, carried out in the framework of the EU funded project **Short Term High Quality Studies to Support Activities under the Eastern Partnership – HiQSTEP, EuropeAid/132574/C/SER/Multi**. The HiQSTEP Project is implemented by an international consortium under the leadership of Kantor Management Consultants. The present study supported the activities of Platform III “Energy security”– of the Eastern Partnership.

The EaP Platform III Work Programme 2014-2017 has identified Public Private Partnerships, including licensing and concessions for the energy sector as a priority area. The DG NEAR and DG ENERGY are the driving forces in cooperation with the EaP Countries on this theme.

The study was implemented by a team of international and local experts under the leadership of **Vagn Bendz Jørgensen** - Study Team Leader and international energy expert; and composed of **Evangelia Vassilaki** – international legal expert and the following national experts: **Vardan Grigoryan** (Armenia), **Asya Chalabova** (Azerbaijan), **Maxim Shapelevich** (Belarus), **Tamta Nutsubidze** (Georgia), **Tatiana Vieru** and **Elena Stratulat** (Moldova) and **Vitaly Radchenko** (Ukraine).

**Przemysław Musiałkowski**, Team Leader of the HiQSTEP Project, was responsible for overall supervision, quality check and management.

Sincere thanks go to the national experts and stakeholders in all six countries who provided information through interviews and responses to questionnaires and contributed to the practical implementation of the study.

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## Abbreviations and acronyms

AM	Armenia
AZ	Azerbaijan
BOO	Build-Own-Operate
BOOT	Build-Own-Operate-Transfer
BRT	Build-Rent-Transfer
BT	Build-Transfer
BY	Belarus
CA	Contracting Authority
CHP	Combined Heat and Power Production
CSI	Centre for Strategic Initiatives, Armenia
DK	Denmark
EaP	Eastern Partnership
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
EPEC	European PPP Expertise Centre hosted by EIB
EU	European Union
EUD	Delegation of the European Union
GE	Georgia
HiQSTEP	High Quality Studies for the Eastern Partnership
IPP	Independent Power Producer
MD	Moldova
ME	Ministry of Energy
MEAT	Most economically advantageous tender
MoE	Ministry of Economy
MoF	Ministry of Finance
PFA	Private Funding Initiative
PPA	Power Purchase Agreement
PPP	Public Private Partnership
PSA	Production Sharing Agreement
PQQ	Pre-Qualification Questionnaire
STL	Study Team Leader
TA	Technical assistance
TFEU	Treaty on the Functioning of the European Union
UA	Ukraine



## 1. BACKGROUND

In 2014, the European Commission introduced three new directives regulating concessions and PPPs in the energy sector:

1. Directive 2014/25/EC on coordinating the procurement by entities operating in the water, energy, transport and postal services sectors, repealing directive 2004/17/EC.
2. Directive 2014/23/EU on the award of concession contracts.
3. Directive 2014/24/EU on public procurement, repealing directive 2004/18/EC.

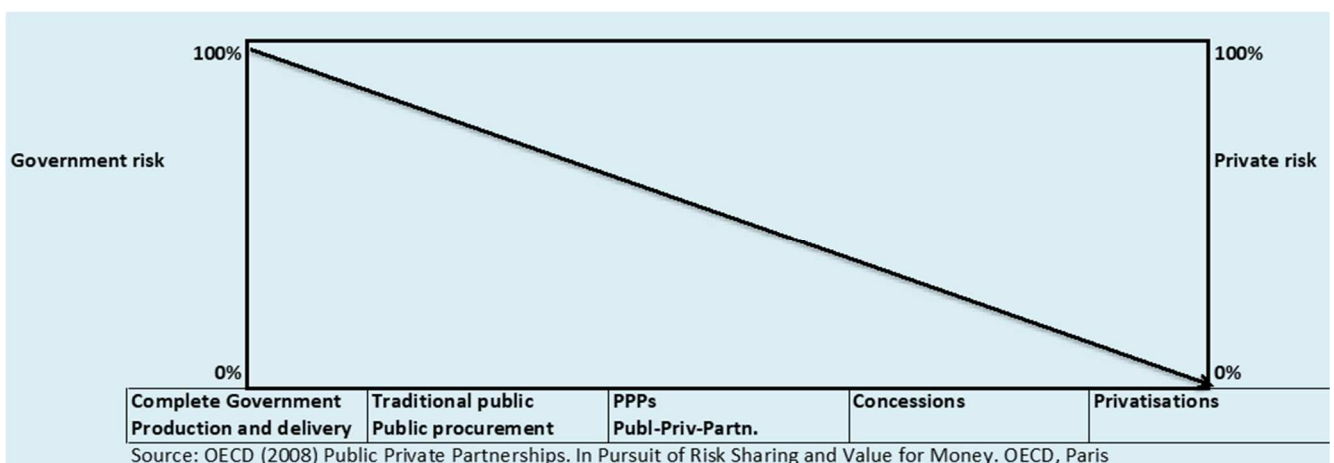
For oil and natural gas exploration and production concessions, the Directive 94/22/EC on the Conditions for Granting and using Authorisations for the prospection, exploration and productions of hydrocarbons is still valid.

The international donor community assisted the Eastern Partner (EaP) Countries in aligning their national legislations with these directives. Especially the EPEC (European PPP Expertise Centre at EIB), the EBRD, the World Bank and the European Commission have been active in providing technical assistance, guidelines, case-studies and assessment reports as well as awareness raising and information sharing activities.

Most of the EaP Countries have been active in developing legislation to replace previous, unclear, conflicting or obsolete laws that were in place. These efforts are ongoing. As such, this report presents the situation until August 2017. However, there has been an update of the status for Armenia and Georgia in October 2018, as at the time that the missions took place, several activities associated with PPP Units and laws were in the process of approval.

Two major tools are being discussed in the study reports: Public Private Partnership (PPP) and concessions. It can be difficult to distinguish between them, as concessions are a sub-category of PPPs. As a rule, the economic risk for the private sector is higher with PPPs compared to concessions.

**Figure 1. Public and private participation classified according to risk and mode of delivery**



*In general, a concession is defined as the right to undertake and profit from a specified public activity over the long term and is subject to the economic risks related to the activity. In some cases, the concessionaires obtain an exclusive right to develop the activity within an area, but there could also be more concessionaires working in the same field.*

In the Terms of Reference of this study, a concession is defined as a “long term (25-30 years) complex public-private partnership (PPP), where the concessionaire assumes responsibilities and risks traditionally borne by the contracting authorities and normally falling within their remit. The main feature of a concession is that the right to exploit the works and/or services always implies the transfer to the concessionaire of an operating risk of economic nature involving the possibility that the concessionaire will not recoup the investments made and the costs incurred in operating the works or services awarded under normal operating conditions, even if a part of the risk remains with the contracting authority or contracting entity”.

Concessions are normally used when a public owned natural monopoly outsources the activity to an economic operator. A concession is a sub-category of public-private partnerships and can take various forms.

Public Private Partnerships involve a combined effort by both the public and the entrepreneur.

For oil and natural gas exploration and extraction projects, concessions are used in all EaP Countries. Production sharing contracts are the dominant form for agreements. For electricity, transmission and distribution there are examples of concessions, but some of these functions are still managed by the public. For electricity production, power purchase contracts are widely used and often in connection with feed in tariffs or feed in premiums (the contracts are often referred to as PPPs because there is a guaranteed price for a period.)

The reports also present European case studies:

1. Concession practices for exploration and extraction of oil/natural gas in Denmark
2. Concession practices for electricity network operations in Germany (Schleswig-Holstein).
3. Concession practices for wind generators off-shore in Denmark

## **2. COMPONENT 1 – CONCESSIONS AND PPPs**

The legal systems of the six Eastern Partner Countries vary significantly in terms of regulating PPPs and concessions , while in most of the six EaP Countries , the definition of “concession” is not in line with the EU criteria.

In some countries, PPP law is supplemented by a concession law, which is again supplemented by public procurement legislation (Moldova, Ukraine). It should be stressed that PPPs/concessions are rarely regulated by a single legal document, but rather by various legal texts of different hierarchy (laws, decrees, governmental decisions, policies etc.). In three Eastern Partner Countries, PPP laws coexist with concession laws (Belarus, Moldova, Ukraine). In Armenia (where concessions constituted part of the procurement law), a combined PPP/concession law was recently approved. In Georgia and Ukraine old concession laws exist. However, they have never been applied in practice and an ad hoc special framework has been elaborated by the Ministries of Energy of both countries for all PPP projects in the field of energy. New legislation on PPP and concessions is currently under development.

None of the EaP Countries’ legislation includes a law specific to PPP/concessions within the energy sector. A specific provision in the Ukrainian law according to which the gas distribution and supply, and electricity generation, distribution and supply sectors are eligible for PPP, constitutes the sole exception.

In Azerbaijan, there is no PPP law. However, procurement is conducted according to the Subsoil Act and the Energy Law as well as according to the Law on Implementation of Construction and Infrastructure Facilities under Special Funding of 2016. In practice, any Production Sharing Agreement (PSA) for oil and natural gas is approved by a law and overrules any other potentially conflicting law.

The details of a PSA have to be negotiated with the line ministries involved. Given the considerable amount of national resources of oil and natural gas in Azerbaijan, abundance of PSAs is expected. The Government's programme for 2020 foresees the elaboration of a PPP legislative framework to be implemented by the Ministry of Economy.

It can be stated that within the Eastern Partner Countries, activities towards alignment to the new EU directives are still ongoing, often with support from donors. The legal framework of the six EaP Countries is therefore in constant development.

The areas covered by the present report are related to the observance of the principles of transparency, equal treatment, and non-discrimination in the Eastern Partner Countries. In this framework, targeted elements are the existence of a regulatory framework for concessions/PPPs, procurement of concessions/PPPs, and contract management (not covering monitoring, i.e. government's ability to monitor the project during contracting and operation phase).

As a general remark, the enacted or envisaged to be enacted legal framework in the Eastern Partner Countries tends to initiate a more structured approach on entering concessions or PPPs. Although in some countries (Belarus, Moldova, Armenia and Ukraine) PPP /concession legislation have been approved quite recently, revisions are already under way in Belarus, Moldova and Ukraine to achieve EU convergence. In Georgia, pertinent authorities are currently elaborating a PPP legal framework including concessions. In most of the countries, the implementation of the envisaged or the existing PPP legislation is supported by the establishment of PPP Units offering advice and, in some cases, quality control of the procedures. The PPP Units are typically established centrally under the Government or within the Ministry of Economy.

In Azerbaijan a different approach was followed, mainly due to the focus – until recently- on oil and gas, managed through production sharing contracts (PSAs). However, a State Agency for Alternative and Renewable Energy Sources was established to promote alternative energy sources. In addition, the Government's programme foresees activities aiming to improve the regulatory framework for PPPs by 2020 including a support mechanism for the development of PPPs in which could potentially evolve in a PPP Unit, , The Ministry of Economy is responsible for this programme and few details are available to date.

So far, few projects in the energy sector are being implemented in accordance with the new legal frameworks. Typical areas of investor interest are IPP (power projects) and especially renewable energy projects, such as hydropower, photovoltaic and a few wind projects. In spite of the fact that transmission in the electricity sector is typically under government control, certain distribution companies have been privatised. In addition, , new projects at local level are emerging on waste management and incineration.

In the oil and gas sectors (exploration/production), Production Sharing Agreements are the most common form of contracting.

The following chapters demonstrate that each of the Eastern Partner Countries adopts its own approach concerning regulation of concessions and public private partnerships. As a result, to capture a general understanding of each country's regulations and their assessment thereon, a rather detailed review is required to cover not only the relevant legal acts and secondary legislation and practices but also the broader energy market environment. Therefore, the Component 1 report provides an overview of the energy environment, the applicable legal framework as well as forthcoming initiatives, along with an assessment of each EaP country's legislation, as well as identification of gaps. The Annexes of the

Procurement of PPPs in most of the Eastern Partner Countries and the selection of the private partner is, in principle, carried out through a tender process following either the public procurement rules or



specific rules especially adopted for PPPs or concessions. The mandatory elements which have to be included in the tender documentation cover bidders' access to procurement related information, a minimum period for the preparation of bids, answers to bidders' requests for clarification and the contents of the bidding documentation. Often a draft contract and the bid selection criteria are included. The next steps are negotiation during the award phase and publication of the award notice.

In this respect, Armenia and Moldova seem to perform closer to recognised and generally accepted good practices. In Belarus, certain law deficiencies have been identified, whereas in Georgia low compliance with international practice is observed. However, in Georgia efforts have been initiated for the establishment of a new legal framework ensuring the observance of detailed procedures. In Ukraine there is no uniform tender procedure neither for PPPs nor concessions. Indicatively, according to the data collected:

- The legal systems in Armenia, Georgia (in PPP Policy), Moldova and Ukraine are lacking the principles of transparency and non-discrimination. A minimum period for the preparation of bids is specified which is not shorter than 30 days in the following EaP Countries: Armenia, Belarus (PPP), Moldova and Ukraine;
- Public procurement notice is included in the bidding documentation in the following EaP Countries: Armenia, Belarus, Moldova and Ukraine;
- Clarifications are provided on bidding documents in the following EaP Countries: Armenia and Moldova;
- Draft contracts are included in the bidding documentation in the following EaP Countries: Armenia, Belarus, Moldova (PPP) and Ukraine;
- Publication of award notice is part of the procurement procedure in the following EaP Countries: Armenia, Belarus, Moldova (PPP) and Ukraine.

In Azerbaijan there is no information available on timeframes concerning tender notifications. The Government's programme for 2020 foresees the development of such timeframes as part of improving the regulatory framework related to PPP.

Eastern Partner Countries handle renegotiations and early termination differently: either by addressing it in the regulatory framework (Belarus, Moldova, Ukraine), or by considering it to be solely a contractual matter (Georgia). In Armenia, the existing law does not foresee special provisions. No information on contract management is available for Azerbaijan.

As regards compensation, in Armenia general provisions of the Civil Code apply; in Belarus and Ukraine the law foresees the specific cases where compensation may be sought; in Georgia compensation is treated as a contractual matter; in Moldova and Azerbaijan no such legal provisions exist. (

While some of these remarks might be considered sceptical, the fact that continuous and great efforts to establish adequate legislation and practices are being made should not be overlooked.

## 3. COMPONENT 2 – PPP UNITS

### 3.1 EU

The World Bank Group, in a report on PPP published in 2017, defined a PPP unit as “any organisation set-up with full or partial aid of the government to ensure that necessary capacity to create, support, and evaluate multiple public-private partnership agreements made available and reside in the government”<sup>1</sup>. The World Bank recognises that as PPPs are regulated in different ways, the development of PPPs can take place within different institutional arrangements and with different tasks.

In August 2014, EPEC - the European PPP Expertise Centre established by the European Investment Bank, the European Commission, EU Member States and some accession candidates - published a report on Establishing and Reforming PPP Units, which also included an analysis of EPEC Member PPP Units and lessons learnt.

At the time of report EPEC had 24 member states of which 18 had established PPP units. Meanwhile EPEC’s membership increased to 41 countries. A country can have several PPP Units, some of which are regional.

The EPEC report lists 3 main categories and sub-tasks which PPP units could perform. It is recognised that the tasks and mandates differ considerably between the countries and only a few PPP units perform all the listed tasks. Differences in PPP units’ responsibilities can be explained by the fact that they should follow national requirements and the actual legal framework, rather than general guidelines. Often the functions of a PPP unit change over time, as new needs are identified while others could lose relevance.

The following main priorities of work were identified in the 18 units of EPEC:

- **Policy functions and support**, capacity building, market monitoring: 12-17 units out of 18.
- **Project delivery activities**, support to procuring authorities: 18 out of 18 units, feasibility studies: 10 out of 18 units, support to procuring authorities during project preparation stage: 5-8 out of 18, support to procuring authorities during the procurement stage: 1-6 out of 18.
- **Approval and quality control functions**, approval of procedures and contracting: 4-6 out of 18.

As can be seen from the overview on functions, the majority of PPP units are involved in development of *legislation and provision of guidance concerning the preparation and operations* of PPPs. All of the PPP Units except from one are involved in sharing good practices and promoting PPPs. In addition, most PPP Units develop standardised PPP contracts. For the second category *programme and project delivery support* there is less involvement of the PPP Units, but about half of them participate in some kind of steering committee and assesses if a PPP is a relevant model. Regarding the approval of PPP projects, about one third of the PPP Units have a mandate to reject projects. This is also the case for approval of tender documents.

In several EU countries institutions other than PPP units are involved in prioritising PPP projects and their selection. In such cases, the PPP unit will often rather have an advisory role than an executive one. It should be noted that the PPP units’ role depends on the country in question. Some countries

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<sup>1</sup> Benchmarking Public-Private Partnership Procurement 2017. World Bank Group.

have regional PPP units, e.g. in Belgium and the UK. Other countries such as Germany, for instance, have a central federal PPP unit as well regional PPP Units in the “Länder”.

### 3.2 Eastern Partner Countries

As mentioned in the Component 1 report, differences in the legal and administrative practices are considerable across the EaP Countries. This also applies PPP which are therefore difficult to compare, although some similarities can be observed. It should be noted that the PPP units are not regulated through any EU directive or regulation. It is therefore a purely national responsibility to select the model to be applied.

Among the Eastern Partner Countries, PPP units were already established in Moldova, Belarus and Ukraine. In Armenia and Georgia, the establishment of PPP units was ongoing during the study and expected to be finalized during 2018. In Georgia a PPP Unit was finally established in October 2018, in Armenia the process has not been finalized yet. In Azerbaijan, PPP units might be established by 2020 as part of the Government’s programme aiming to improve the regulatory framework for PPPs , however, no such decision has been taken yet.

The Component 2 Report provides details on the functioning of PPP units in the EaP Countries. Several institutions involved with PPP management and/or advice have also been identified:

- Armenia: no PPP unit, a draft law of September 2018 foresees its establishment. Between June 2017 and September 2018, the Centre for Strategic Initiatives of the Government of Armenia played a role in promotion of foreign investment and capacity building related to PPP projects, but it was dissolved in September 2018.
- Azerbaijan: the Bid Commission at MoF. It has some relevant functions but does not constitute a PPP unit. The establishment of support mechanisms for PPPs has been scheduled for 2020 and could include a dedicated PPP unit.
- Belarus: Public Private Partnership Centre of Belarus. MoE and MoF have some functions related to coordination of PPPs.
- Georgia,: a PPP unit was established in October 2018
- Ukraine: a PPP unit is situated within MoE.

PPP units usually perform a combination of three main functions under a complex legislative framework: (i) PPP policy support and related activities, (ii) programme and project delivery support and (iii) approval and quality control.

Bearing in mind that the legislation on concessions and PPPs is complicated, the provision of advice and support to the authorities involved is considered necessary. This is especially relevant to regions and municipalities, which may not have the know-how at hand. To this end, PPP units’ main task is to facilitate the way to successful Private-Public Partnerships.

PPP can be difficult to establish, because they normally involve a public activity being partly/ fully transferred to the private sector. The advantage is that the contractor, being a private operator, is expected to provide increased effectiveness to investments. However, in spite of the fact that the economic operator will be bearing the major economic risk, such transfers of public obligations entail a risk for the public authorities, which might in the end have to re-establish the situation before the

outsourcing, if the project fails. This is also the case, when a guaranteed delivery price for services – like IPP with power purchase agreements – is part of the PPP contract.

PPPs can come in a variety of models. They involve a complete private takeover of some functions or a partial takeover and co-financing with public and private partners as seen in several development projects within the energy sector. Nevertheless, PPPs can help to transfer investments from the public sector to private economic operators, as well as the associated economic risk.

A PPP unit must be prepared to at least advise authorities on how to handle such projects and to assess the risks involved. In some EaP Countries, independent risk assessment units are being established but they could also be part of the PPP units.

EC and EBRD have been actively involved in the establishment of the PPP units in the EaP Countries. It can be stated that the functions of the PPP Units in the EaP follow a more aligned approach than the units in Western Europe. They are, however, relatively small and lack legal expertise. Efforts should be prioritised towards resolving the lack of legal expertise: complicated rules on procurement and state aid must be respected in order to transfer public obligations. In case a project fails, the competent authority will be exposed to strong criticism, while a PPP unit can help prevent such situations .

Many PPP projects require technical expertise. Taking into account that it is not likely for PPP units to have in-house staff with an expertise in every sector, it is recommended to make funding for external technical expertise available.

In May 2017 a questionnaire was sent to the PPP units and the authorities responsible for establishing PPP Units in the six countries and covered several sections with the following headings:

1. Information on PPP unit’s establishment and Government institutions relations
2. Clients served by the PPP unit
3. Mandate of the PPP unit
4. Functions of the PPP unit
5. Project delivery support functions
6. Technical evaluation of feasibility of projects
7. Funding of the PPP unit
8. Staffing of the PPP unit
9. Capacity building needs
10. Number of assistance activities

Countries sent their replies between June and August 2017. The results of the questionnaire are presented below.

**Table 1. Current status of PPP Units**

Status	AM	AZ	BY	GE	MD	UA	DK
Operational	P	F	A 2014	P	2010	A	A
Part of Ministry	MoE/CSI	? (MoE)	MoE	G	MoE	MoE	(“MoE”*)

\*: Ministry of Industry, Business and Financial Affairs

A: Active P: In planning for 2018 F: Establishment possible in future, Pt: Partly, MoE Ministry of Economy, G: Government

Typically, the PPP Units are established within the Ministry of Economy, although Georgia was envisaging a more independent role with direct report to the Government (finally, the PPP Unit is responsible to the Prime Minister directly). This will probably also be the case for Azerbaijan where the Government is to approve all concessions and PPPs. It should be noted that in Denmark<sup>2</sup>, used as a comparative example regarding PPP units in Western Europe, the Ministry of Industry, Business and Financial Affairs is more oriented to enterprises than the Ministry of Economy. It has some of the functions normally vested within ministries of economy.

The following tables include a presentation of the planned but not yet implemented functions of PPP units in Georgia and Armenia.

**Table 2. Clients to PPP Units**

Client	AM	AZ	BY	GE	MD	UA*	DK
Government/president	P	n.a.	A	P	A	A	A
Ministries	P	n.a.	A	P	A	A	A
Regions	P	n.a.	No	P	A	A	A
Municipalities/Cities	P	n.a.	No	P	A	A	A
Public Institutions	P	n.a.	No	P	A	A	A

A: By now P: Planned \*: PPP Unit Ukraine also served NGO's and IFO.

The typical pattern for PPP units is to serve all public institutions with the exception of Belarus, where the PPP unit only serves the Government and Ministries.

**Table 3. PPP Units mandate in serving clients**

Competence	AM	AZ	BY	GE	MD	UA	DK*
Advice	P	UC	A	P	A	A	A
Checking legal compliance and procedures	UC/P	UC	A	P	A	A	A
Reviewing projects and feasibility studies	P	UC	A	P	A	A	A
Authorisation to approve or reject projects	No/P	UC	A	P	No	A	No
Part of tendering committee	No	UC	No	P	A	A	n.a.

A: Yes UC: unclear P: Planned \* Only advice and guidance provided

Most PPP units have the mandate to check procedures for PPPs and review feasibility studies. The PPP unit is authorised to reject PPP projects only in Belarus and Ukraine. Participation in the tendering committee is assigned to some PPP Units.

<sup>2</sup> Denmark is used as a typical example of well-established EU PPP units. It was selected as an example as all relevant data were easily available to the Study Team.

It can be assumed that most PPP units have a mandate to advise the clients but are not involved in direct decision making, as this is left to the line ministry or region/municipality.

**Table 4: PPP Units functions**

Function	AM	AZ	BY	GE	MD	UA	DK*
Input for legislation and strategies	P	N.a.	A	U	A	A	A
Providing standard contracts	P	N.a.	A	P	No	P	Some
Promotion of PPP and awareness raising	P	N.a.	A	P	A	A	A
Input on prioritisations of PPP projects	P	N.a.	A	P	No	P	A
PPP market analysis	P	N.a.	A	P	A	A	Some
Capacity building, training, seminars	No	N.a.	A	P	A	A	No

A: Actual (yes) P: Planned U: unclear N.a: No information available

More than half of the PPP units are involved in providing input for legislation and regulations. This is also the case regarding elaboration of standard contracts. All respondents are involved in promotion and awareness raising. 4 out of 6 PPP units are involved in prioritisation of projects. Market analysis appears to be a general part of the tasks and capacity building is only to be done by 5 PPP units.

**Table 5: Project Delivery Support**

	AM	AZ	BY	GE	MD	UA	DK*
Legal/procedural screening	U	N.a.	No	P	A	A	Pt
Advice on project implementation	P	N.a.	No	P	A	P	Pt
Assistance in preparing procurement and contracts	U	N.a.	No	P	A	A	No
Prioritising projects	U	N.a.	No	P	No	P	Pt
Risk assessment	P	N.a.	A	No*	A	A	Pt
Direct assistance on procurement	No	N.a.	No	N.a.	A	P	Pt
Reviewing feasibility studies	P	N.a.	A	P	A	A	Pt
Economic assessment	P	N.a.	A	P*	A	A	Pt
Technical evaluation of feasibility studies	P	N.a.	A	No	A	A	Pt

A: Actual (yes) P: Planned U: unclear N.a: No information available \*: Risk Management Unit planned. Pt: Partly

Concerning project delivery support the picture is a little more blurred. 5 out of 6 PPP units are actively involved in feasibility studies and economic assessment. However, less than half are involved in the other functions. As regards risk assessment, other institutions could be involved, this being the case for

Georgia. PPP Units to be established are counted as positive for each task, if their forthcoming tasks are described in the planning documents.

**Table 6: Approval and Quality Control Functions**

	AM	AZ	BY	GE	MD	UA	DK
Legal quality of project/contract	U/P	N.a.	No	P	No	P	No
Economical/financial evaluation	P	N.a.	A	P	No	P	No
Technical evaluation	No	N.a.	A	No	No	P	No
Mandate to recommend/reject projects	U/Tbc	N.a.	A	P	No	P	No
Keeping databases on PPP projects	P	N.a.	A	P	A	A	No
Follow up/monitoring PPP projects	U	N.a.	A	P	A	A	No

A: Actual (yes) P: Planned U: unclear N.a: No information available. Pt: Partly Tbc: To be decided

Armenia, Belarus, Ukraine and Georgia already have or are currently planning legal quality control systems. The aforementioned countries with the addition of Moldova are keeping track of PPP projects in relevant databases. Approximately half of the units carry out technical and economic evaluations.

Countries did not provide information for capacity building needs. , However, legal expertise is required. In general, the new PPP units in EaP appear to perform more functions than compared to the long-established European ones.

## 4. COMPONENT 3

The Component 3 Report comprises guidelines for a standardised procedure for procurement of concessions and PPP and three model concessions contracts for:

- oil/natural gas exploration and extraction
- electricity distribution
- power generation facilities

Guidelines and models are based on the EU directives, and namely: the Directive on the award of concession contracts (2014/23/EU); the Directive on the conditions for granting and using authorizations for the prospection, exploration and production of hydrocarbons (94/22/EC), the public procurement Directive (2014/24/EU) and the Directive on procurement by entities operating in the water, energy, transport and postal services sectors (2014/25/EU).

This Component Report is not easy to summarize as each country has its own legal framework and different policies to be respected. This is a rather complex issue and the report can be used as a handbook or a check-list for actual procurement processes.

## 4.1 Guidelines for procurement procedures

Guidelines or recommendations aim at facilitating the entire procurement process in accordance with the EU directives.

Public authorities use concession contracts to deliver services or construction/operation of infrastructure. Concessions involve a contractual arrangement between a public authority and an economic operator (the concessionaire). The latter provides services or carries out works and is remunerated by being permitted to exploit the work or service.

Concessions are a particularly attractive way of carrying out projects in the public interest when state or local authorities need to mobilise private capital and know-how to supplement scarce public resources. Transfer of risks to the concessionaire is also an important aspect – few Governments will be popular if drilling for a number of unsuccessful exploration prospects; an international oil company has a large portfolio of prospects and will lose on some and profit on others.

Concessions have specific features compared to public contracts, which justify a special and more flexible set of rules for their award. Concessions are typically high-value, complex and long-term contracts which require appropriate flexibility during the award procedure to ensure the best possible outcome.

Further, the main elements of the EU concession Directive involve:

- A clearer and precise definition of concession (building on the Court's case law);
- Coverage of works and services concessions both in the utilities sector and in the classic sector (exempting water utility);
- Compulsory publication of concession notices in the Official Journal of the EU, when their value is equal to or greater than 5.186.000 EUR;
- Adequate solution for dealing with changes to concessions contracts during their term, notably when justified by unforeseen circumstances;
- Establishment of certain obligations with respect to the selection and award criteria to be followed by entities awarding concessions. These rules aim at ensuring that such criteria are published in advance, are objective and non-discriminatory. In general, they are simpler and more flexible than similar provisions currently applicable to public contracts.

A Concession involving private partners is a particular form of Public Private Partnership (PPP). Although PPPs have never been defined in the EU Public Procurement legislation, they are usually understood to be cooperation between a public authority and a private partner, where this cooperation bears risks that are traditionally borne by the public sector which is often also contributing to the financing of the project. Some PPPs are structured as public contracts, but, based on estimations by the European Commission services, over 60% of all PPP contracts would qualify as concessions<sup>3</sup>.

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<sup>3</sup> Directive of the European Parliament and of the Council on the award of Concession Contracts- European Commission Memo 2014



In international practice, selection of the form of PPP contract is determined especially by: a) the rights the private entity acquires on the (public) infrastructure (facility), namely exploitation and/or ownership, b) the services provided or the products to be produced, c) the allocation of risk between the authority and the private entity and the selection of the payment mechanism of the private entity as regards capital investment on the facility.

The following forms of PPP are used at international market:

1. Concession model, usage-based or user pay PPPs

In international practice, several variations of this model appear. More specifically, classical form of concession constitutes the BOT contract (Build-Operate-Transfer). Also, the BOOT contract (Build-Own-Operate-Transfer). In this case (of BOOT), if the concessionaire at the end of the contractual period does not transfer the ownership to the public entity (i.e. maintains the ownership of the facility), the model is named BOO (Build-Own-Operate)

2. PFI (private funding initiative) model, availability-based PPPs

3. BT (Build -Transfer) or BOT (Built-operate-transfer)

4. BOL (Build- Own -Lease) or BLOT (Build-Lease-Operate-Transfer)

5. BOM (Build -Own -Maintain) or BRT (Build-Rent-Transfer)

6. Management concession to a vehicle of special purpose

7. Joint Ventures Model (see for the term “joint venture”

**The proposed guidelines follow the structure of the procurement process and refer to :**

**1. Preparation stage**

This section describes the first stage of the process, which is critical for future activities of the contract.

During this phase the following issues are addressed:

**Project management** - Project organisation and resources; Human resources; Evaluation Committee; Conflicts of interest; Tender Documents; and Documentation and record keeping.

**Selection of procedure**

The decision which procedure to use is a critical and strategic one affecting the whole procurement process. The decision should be made and justified at the planning stage. Four options are mentioned below.

- **Open:** This is a process where all providers interested in the contract and who have responded to an advertisement can submit tenders.
- **Restricted:** This is a two-stage process where only those providers who have been invited may submit tenders. The selection and shortlisting are usually based on a Pre-Qualification Questionnaire (PQQ).
- **Competitive procedure with negotiation:** Under the Competitive Procedure with Negotiation, any economic operator may request to participate in the process. The contracting authority makes an initial evaluation of the candidates based upon the grounds of exclusion and the selection criteria published in the contract notice. It may limit the number of suitable candidates to be invited to participate in the procedure. The contracting authority then invites its chosen economic operators to submit an initial tender.

- **Competitive dialogue procedure:** Under this procedure, after final tenders have been submitted, tenders can still be clarified, specified and optimised at the request of the contracting authority; further clarifications and improvements can be allowed once the winning bidder has been appointed

## **2. Publication**

This section describes the procedures required for the publication of the tender and covers: Prior Information Notice; Contract Notice; tender documents; selection criteria; a draft contract; and specification drafting.

## **3. Submission of tenders and selection of tenderers**

This section describes the requirements for submission and the selection process of the applications. It covers the following elements: delivery of the tenders; obtaining and submitting tenders; observance of tendering instructions; safe keeping of tender documents; opening ceremony; and selection, minimum requirements and additional documentation.

## **5. Evaluation of tenders**

This section describes the requirements for evaluation of the applications and discusses in particular the following elements: the lowest price; the most economically advantageous tender; post tender negotiations; how the Evaluation Committee should reach its decision; and the Evaluation Committee decision.

## **6. Publication of result and award**

This section describes the needed information for the successful candidate and the other applicants and discusses in particular the Award Notice; the right to appeal; and General principles and procedural guarantees for the awarding of a concessions contract.

## **7. Subcontracting and modifications of contract**

In concessions, it can be necessary for the concessionaire to sub-contract part of the work to entrepreneurs. Modifications to the contract in the course of project implementation may also be deemed necessary for unforeseen situations.

## **8. Drafting of the contract**

This section discusses the phases and elements of drafting the contract, and in particular: allocation of risks; rights and obligations of the parties; remuneration mechanisms of the private partner including the terms and payment modalities; sanctions and penalties that may be imposed in case of breach by the parties; reasons and procedures for which amendments related to the contract are permitted in the future; early termination, causes that justify the early termination of the contract and related procedures to be applied in such cases; Step in rights of creditors and the contracting authority; dispute resolution mechanisms.

## **4.2 Model contracts**

### **Oil and Natural Gas**

For oil and natural gas exploration and exploitation there are two major forms of concessions: Production Sharing Agreements (PSAs) and *Concessions*. Whereas concessions are normally part of

the national legal framework the PSA can be more “tailor made” to the concrete development plan. PSAs were introduced in the 1960’s as a model suitable to low/middle income countries with huge hydrocarbon resources – and particularly the international oil companies. In principle, the hydrocarbon produced is shared between the state and economic operator in such way that when actual production is started, part of the value of the oil is used to cover the investments and operational costs – *cost oil*. This could be 10% or higher. The value of the remaining production is shared between the state and the economic operator according to a negotiated formula, which could change with increased production – *profit oil*. Often the PSA overrules other national legislation (including taxation rules) and the value of the hydrocarbons are calculated in relation to international oil/gas prices in the international currency (normally USD). PSA are relatively simple to implement and can be advantageous when the nation in question has a less developed legal framework or conflicting legislation. In case the national currency is very volatile, it could be an advantage for both parties to connect the values to an international currency or deliver the state’s share *in kind* (physical delivery).

PSA are commonly used in the EaP Countries. Especially in Azerbaijan where the major hydrocarbon resources of the region are situated. Most of the PSAs in Azerbaijan were agreed upon during the 1990’ies and early 2000’s.

An oil/gas *concession* is an integrated part of the national legislation and normal taxes must be paid. In addition, in many cases a royalty (a % of the production value) is included as well as an extra tax in case of extraordinary large discoveries or high oil/gas prices – *windfall tax*. Alignment to the international oil/gas prices is normally used, but the final taxes are paid in national currencies. In many cases the state acquires a share in the production consortium, and thereby forms a joint venture like cooperation. This can be as a co-investor or on a “carried” basis. To secure that taxes for an oil/gas field are not avoided by subtracting other deficits, a ring fence is often introduced in the contract to secure full tax payment of the specific project.

In addition to these fees and taxes there are normally some concession/PSA clauses on how to deliver the oil/gas if there is a terminal or pipeline nearby.

In addition to the purely hydrocarbon regulations there will also be references in a contract to environmental legislation, work force regulation, safety regulations and metering standards. As all these regulations differ in each country, the standard contract has to be adjusted with national relevant details. However, many aspects in a model contract are standard such as rules for the change of consortium partners, guarantees how to end a concession and how to secure development in a satisfying manner for both investor and state.

### **Electricity distribution**

For an electricity distribution network concession, there are other factors influencing the contract. In case of an expired concession with a new operator, in some instances the value of the present network must be negotiated with the former operator and a compensation agreed upon. There will also be requirements to the “quality” of delivered electricity with regard to faults and voltage level and how to serve, meter and bill the customers. Also, in distribution there will be several references to important national laws like in the oil/gas contracts. It is also important to align contracts to the general regulations such as the *grid code*.

### **Power Purchase Agreement**

In the case of a power purchase agreement the mode of delivery to the grid and the “quality” of delivered electricity are important, because they can vary a lot. Too costly connectors to the grid/transformer

station can result in a project being rejected by the investor. Therefore, in major IPP projects the state or system operator provides a nearby delivery point. This is the case for several off-shore wind generator parks.

As already mentioned, many differences in the contracts are also due to the technologies involved. It is therefore not possible to present a standard contract for all energy projects. Even for the same technology there are differences in how the countries develop their own national legal framework and which governmental/regional institution is involved. Therefore, references to national legislation and country specific circumstances can be inserted into the templates for the standard contracts. These templates should present the relevant national legislation and at the same time, the text must respect the directives regulating these activities.

**Templates of Model Contracts for these three sectors are presented in the Report.**

## **5. COMPONENT 4 - ESTABLISHMENT OF A HOME PAGE**

A homepage with information on the HiQSTEP project became operational in December 2017. It includes information on each study carried out under the Project, including the Concession Agreements Study [www.hiqstep.eu](http://www.hiqstep.eu).