

Country Report

Ukraine

Public-Private Partnerships: The Homework on Establishing Attractable Legal Environment Is Almost Done, It Is Time for Implementation

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I. Introduction

In recent years, with strong support from the World Bank and the European Bank for Reconstruction and Development (EBRD), the Ukrainian legislation in the field of public-private partnerships (PPPs) has been fundamentally changed so that today it basically meets the best international standards. In recent years, with strong support from the World Bank and the EBRD, Ukrainian legislation in the area of PPPs has been fundamentally changed so that today it essentially meets the best international standards.

The legislation clearly defines the process of initiating PPP projects for state and municipal assets, the obligations of public authorities to consider proposals for PPP implementation, including those submitted by private companies, as well as the time frame for deciding on the implementation or inappropriateness of implementing a PPP in relation to the project proposed for consideration.

The Law provides for the possibility of using various forms of PPP – concessions, PPPs with state participation and hybrid models, for the structuring of which a mixed contract can be used. The latter makes it possible to create innovative models for the implementation of infrastructure projects, taking into account projects' specifics, as well as wishes and limi-

tations of the public and private parties for organising their interaction within the framework of the creation or modernisation and operation of infrastructure assets.

The Public-Private Partnership Law¹ and the Concession Law² provide for a broad arsenal of forms of government support for the implementation of PPP projects including availability payments, the purchase from a private partner of goods, works, services provided under a PPP agreement, the sale of goods to a private partner, works, services necessary to implement a PPP project, creation of related and important infrastructure for the implementation of the PPP project.

All PPP projects, including those in the form of concessions, are awarded through an open competitive procedure, regardless of their initiator. For concession projects the competitive dialogue procedure, as well as the direct negotiation process for projects initiated by the tenants of the assets proposed to be transferred to concession, is possible too. For concession projects, e-procurement can also be conducted. Proponents of unsolicited proposals (hereinafter referred to as USP) must also participate in tenders. For them, however, the law³ provides benefits that encourage the private sector to prepare such proposals. In particular, the initiator of a USP has the right to sign a PPP agreement, including a concession agreement, on the terms of the best bid. If he considers this unacceptable, the winner of the tender shall reimburse the initiator of the PPP proposal for his expenses of preparing such proposal after the PPP agreement has been signed. This compensation must not exceed 2.5% of the cost of the proposed PPP project.

The procedure of replacing a private partner (so called 'step-in-right' procedure) at the initiative of the public partner and at the initiative of the creditor is

DOI: tba

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1 The Public-Procurement Law of Ukraine <<https://zakon.rada.gov.ua/laws/show/2404-17#Text>> accessed 1 October 2021.

2 The Concession Law of Ukraine <<https://zakon.rada.gov.ua/laws/show/155-20#Text>> accessed 1 October 2021.

3 The Public-Procurement Law and the Concession Law of Ukraine.

clearly regulated in the legislation. Moreover, when a direct agreement is signed, it is possible to pledge to the creditor all the rights of the private partner under the PPP agreement. International arbitration is possible for companies with foreign founders.

The legislation provides for the possibility for the public authorities to call in independent experts to assist them in conducting competitive tenders, as well as advisers to prepare proposals for the implementation of PPP projects and tender documentation. If the cost of the project exceeds UAH 250 million (approximately €8 million), the public authority is obliged to engage advisers.

Despite this, two years after the adoption of the new legislation, no one has used it yet to prepare and submit a PPP proposal (two concession projects concluded in 2020 for the seaports of Kherson and Olvia were prepared by the Ministry of Infrastructure with the assistance of the International Finance Corporation (IFC) and the EBRD before the adoption of the new PPP/concession legislation). To some extent, this was influenced by the COVID-19 pandemic, but this is not the main reason for the lack of PPP projects in Ukraine. These reasons are elaborated in detail below.

II. Legal Regulation

Despite a comprehensive PPP legislation in Ukraine, there are still some issues that require changes in the legal regime. The main problem that must be solved as soon as possible is the imperfect budgetary regulation. The Budget Code of Ukraine⁴ defines an exclusive list of cases in which public authorities can assume long-term budgetary obligations (ie obligations for more than three budget years). The implementation of PPP projects, including in the form of a concession, is not one of these cases.

As a result, a public partner does not have the right to make long-term financial commitments to the private partner / concessionaire in the PPP / concession agreement. Accordingly, practically none of the forms of government support for PPP implementation stipulated by the law can be applied in real life. This leads to the fact that today in Ukraine only commercially attractive projects that do not require government support can be implemented as PPPs. In addition, it is not yet possible to implement 'government-pays' PPPs. This severely limits the possibilities of using this mechanism for infrastructure de-

velopment. On the one hand, in Ukraine there are very few commercially attractive projects that could be implemented as a PPP. On the other hand, the PPP mechanism cannot be applied to the most demanded projects in the sphere of life support (water supply and sanitation, electricity and heat supply, urban transport, household waste management, etc). It is unrealistic to implement all these projects without the government support, given the low effective demand for services that will be provided using the corresponding infrastructure assets.

The draft law amending the Budget Code⁵ regarding long-term obligations for PPP projects has been under consideration by the Ukrainian Parliament for more than a year. It is still impossible to predict when and in what form it will be adopted.

The second issue that should be provided for in the legislation on PPP issues concerns administrative sanctions against representatives of public authorities for violation of the legally binding deadlines for the implementation of activities provided at all stages of the PPP process. Today, such sanctions are not envisaged. As a result, the deadlines for the examination of PPP proposals, in particular unsolicited proposals, as well as of the adoption of appropriate decisions based on the results of their analysis, and the implementation of certain stages of organising of tender procedures and negotiations on the results of their completion, are seriously violated. In many cases they are exceeded dozens of times. Given this, a private business is obviously not in a hurry to prepare its proposals for the implementation of a PPP, and the public authorities either cannot, or will not (or both) prepare proposals for the implementation of PPPs.

The legislation does not provide for special procedures for contesting the results of PPPs or concession tenders by bidders. Therefore, participants do not feel themselves sufficiently protected in this kind of competition. The situation is complicated by the fact that despite the strict requirements of the legislation regarding the disclosure of information on PPP issues, including during competitive bidding, in prac-

4 The Budget Code of Ukraine <<https://zakon.rada.gov.ua/laws/show/2456-17#Text>> accessed 1 October 2021.

5 Draft Law on Amendments to the Budget Code of Ukraine Concerning the Settlement of Budget Relations during the Implementation of Agreements Concluded in the framework of a Public-Private Partnership, including Concession Agreements, No 5090 dated 17 February 2021 <http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=71124> accessed 1 October 2021.

tice, bidders do not have sufficient information neither about the PPP project itself nor about the decision-making ground for the results of the bids review. Since the legislation does not clearly define what information can be considered as a confidential, a significant part of the information on PPPs has the status confidential. In this regard, it would be useful to regulate the procedure of challenging the results of a PPP tender by its participants and establish the grounds for recognizing information as confidential.

III. Institutional Capacity

One of the most important reasons for the underdevelopment of PPP practice in Ukraine is the low institutional capacity and the lack of experience of public authorities in the field of PPPs. The PPP mechanism is quite new in Ukraine. There are very few PPP projects, and there are practically no successful ones (the last two concession agreements concluded in 2020 are still in a transition period; and among the existing ones, there are no successful concession agreements).

In 2021, within the framework of the World Bank's project 'Strengthening the use of Public-private partnerships through better public capital investment management in Ukraine', a detailed PPP manual⁶ was prepared. This manual consists of six volumes providing detailed explanations on the use of the Ukrainian PPP legislation; best practices in using this mechanism in different countries were also given. The World Bank specialists conducted a series of trainings on this manual, but this does not seem to be enough. There is a need for serious training programmes for public authorities on PPP issues and they should become mandatory for those entrusted with the authority to make decisions in this area. Without this, even the best legislation in the world will have no effect in practice.

IV. Pessimism Bias

At different seminars, conferences, trainings, people often talk about 'optimism bias' in the preparation

of PPP projects leading to the failure of some of them, causing negative fiscal impact and undermining the image of PPPs among the population and public authorities.

This question is, of course, very important. Nevertheless, in Ukraine there is also the opposite problem, which can be called 'pessimism bias'. Many people believe that the PPP mechanism cannot be effectively applied there, especially when it comes to the implementation of complex large-scale infrastructure projects.

The population does not believe in this because for more than 20 years of 'attracting' private business to infrastructure development, there has not been a single successful project. At the same time, there are a lot of failed projects. Therefore, people are more likely to perceive PPP negatively than positively.

Public authorities have no experience in the preparation and implementation of PPP projects and they are not in a hurry to take them on – there is a lot of work, the responsibility is high and the outcome is not clear. Almost all innovative proposals in this area are either categorically rejected or reviewed extremely carefully and for a very long time. No one is ready to take responsibility for the decisions that has not been made before: only conventional decisions are adopted, no space for innovations is left. When considering a proposal for a PPP, any official first of all will try to find the reasons why the project cannot be implemented, and will not suggest how it can be done the most effective way. Any proposal amending special legislation, which would allow the implementation of project important for the society, are perceived with hostility, even when it concerns by-laws, not to mention laws. As a result, having inherently innovative legislation in the field of PPP, Ukraine has not yet implemented a single innovative institutional solution for PPP projects.

Private business also does not believe in the success of its investments in PPP projects in Ukraine, but for different reasons. Firstly, it has not seen successful cases of implementation of such projects. Secondly, its experience of communicating with officials is not effective and comfortable. Therefore, it is important for Ukraine not only to warn officials against ill-considered decisions on PPP projects (to avoid the optimism bias), but also to give them confidence that complex large-scale projects can be effectively implemented using this mechanism (to warn against pessimism bias).

⁶ The PPP Manual <<https://bit.ly/31ze6Su>> accessed 1 October 2021.

V. Conclusions

Currently the PPP mechanism is in high demand in Ukraine. Most of the transport and essential public infrastructure is morally outdated. Some types of infrastructure are almost completely absent (eg infrastructure for handling household waste), a significant part of infrastructure uses outdated technologies that have a negative impact on the environment and is characterised by excessively high resource consumption. It is unrealistic to solve the existing problems exclusively at the expense of public budgets and within the framework of international borrowing. Therefore, the government and local authorities are interested in attracting private investment.

In theory, Ukraine is ready for the implementation of PPP projects in various areas— there is good legislation and an institutional basis for the consideration and implementation of PPP projects in priority areas of the country. But in practice, the process moves very slowly. The reason for this is a low institutional capacity of public authorities, a lack of experience in PPP project implementation and too ‘relaxed’ attitude to the observance of the deadlines provided by the legislation.

PPP projects in Ukraine are interesting to both domestic and foreign businesses: a large scope of work, the opportunity to get a significant outcome from the introduction of resource-saving technologies, the country’s favourable location and well-educated labour force. However, this interest is so far merely theoretical. To make this a practical matter, the ‘state machine’ should operate more efficiently. The fulfilment of contractual obligations between all parties and, above all, the obligations of public authorities, should become the norm, not an exception. Investors should become partners of public authorities, in deeds, not merely in words.

So far, social and environmental projects, as well as infrastructure projects for water supply, sewerage, heat supply, waste management, urban transport, etc, have little chance to be implemented in Ukraine through the PPP mechanism due to budgetary constraints. Therefore, the government is still mainly fo-

cused on commercially attractive projects which are awarded as concessions.

In the context of limited opportunities for government support for PPP implementation, mainly large foreign companies that are able to attract reputable foreign financial institutions or banks to finance their projects can count on serious guarantees of the fulfilling public partners’ obligations under PPP agreements. The step-in-rights mechanism and a well-designed direct agreement will provide strong protection for their rights under PPP or concession agreements. Both when the public authorities are considering their proposals and during the implementation of PPP agreements, domestic companies, especially not very large ones, are not yet able to protect their rights in the field of PPP. If a company does not have a large international or foreign bank supporting it which, on the one hand, will be able to provide it with attractive lending conditions, and, on the other hand, can receive the rights of the private partner under the PPP agreement as collateral, and also will be able to challenge the violation of the PPP or concession agreement by the public partner in the international arbitration, its risks in participating in the PPP project will be unreasonably high. In the current situation, it seems optimal for domestic companies to participate in PPP projects only as a part of consortia together with large foreign companies. A local company knows the market and the legislation, it understands the governmental institutional structure and the existing business practices. A foreign large company can ensure the use of modern technologies, attract cheap money, and provide for the protection of the rights of the consortium in the PPP or concession project.

Today, Ukraine cannot afford to implement poorly prepared and ineffectively managed PPP projects as the credit of the society and business confidence in this mechanism are extremely low. Therefore, in order to accelerate the implementation of infrastructure projects as PPPs, highly qualified specialists are needed in the authorities responsible for reviewing and implementing PPP projects, as well as successful PPP projects prepared by them.