

# Dispute Prevention approaches in PPP's Practical Issues

Serge Y. Bodart

Dipl. Ing. /MSc. EPFL - SIA

Partner at PMG Consulting Engineers and Economists  
Prevention and Resolution of Disputes

Rue du Centre 72, CH-1025 St-Sulpice/Lausanne  
Switzerland

# Dispute Prevention approaches in PPP 's

## Practical Issues

1. The growing share of PPP Projects
2. PPP Contracts and recent trends
3. Potential sources of disputes under PPP Contracts
4. Dispute Prevention approaches - Overview
5. Dispute Prevention in PPP Projects
6. Conclusions

# 1 The growing share of PPP Projects

- The number of Public Private Partnership Contracts (PPP's) have grown significantly in recent years
- Financing of PPP's by the EIB in Europe grew from 250 million € (1990) to 1.3 billion € (2012)
- PPP's involve large complex public infrastructure and long term arrangements with multiple goals and interrelated parties => Increased risks of potential disputes
- Mechanisms to prevent and resolve disputes become a major part of the PPP contract risk's assessment and negotiations process

## 2 PPP's and recent trends

- In PPP's the Contractor (Private Partner) will not only build an infrastructure for the Client (Public Partner) but also design, finance, operate and maintain it for a period of 25 to 50 years before handing it back to the Client
- By taking into consideration the whole life cycle of the infrastructure, the Private Partner is in a better position to efficiently optimize not only the project construction quality, costs and delays but also the project functionality
- One of the key point for a optimized and successful PPP is a balanced allocation of project risks between the Partners (Public and Private)

## 2 PPP's and recent trends

- A typical risk allocation between the Partners

Risks	Public Partner	Private Partner	Risks	Public Partner	Private Partner	Risks	Public Partner	Private Partner
<b>General and Development Phase</b>			<b>Construction Phase</b>			<b>Operation and Maintenance Phase</b>		
<b>General risks</b>			<b>Construction Phase</b>			<b>Operation and Maintenance Phase</b>		
General change in law		X	Existing site conditions		X	Doc. For permits and authorisation		X
Specific change in law (Specific to project)	X		Existing energy networks		X	Issue of authorisations and permits	X	
<b>Development Phase</b>			Geotechnical risks	X	X	Revenue risk	X	X
Land expropriation for the project	X		Archaeological risks	X	X	Availability payment	X	X
Documents for permits and authorisation		X	Existing contamination risks	X	X	Lump sum O&M fee		X
Issue of authorisations and permits	X		Construction works including equipment		X	Major replacement and repair		X
Design (cost and delays)		X	Lump sum fix price		X	Technology changes		X
Private financing / Financial close		X	Working program / Construction delay		X	Availability and performance criteria		X
			Force majeure	X	X	Force majeure	X	X
			Construction guarantee and insurances		X	O & M guarantee and insurances		X
						Hand back requirement		X

## 2 PPP's and recent trends

### Recent trends in PPP Contracts

- Public Procurement Authorities tend to require from the bidders a 2 to 3 steps competitive dialogue before contract award in order to promote project optimization
- Banks and financial institutions are becoming more reluctant to finance a Private Partner carrying 100 % of the revenue risk without some guarantees from the Public Partner
- Growing share of Availability PPP's versus Concession PPP's with pure revenue risks
- Growing share of Refurbishments / Brownfield PPP's

### 3 Potential sources of disputes under PPP's

#### During the bid and financial close phases

- Interruption of the procurement process by the Public Partner during bid phase => Disagreement on the interruption justification and level of compensation
- Bad anticipation by both Partners of a bankable risks allocation => Impossibility of reaching financial close date
- Drastic change of economic conditions between the contract award and the planned financial close date
- Excessive optimism at the signature of the Contract => risks of having to renegotiate the PPP Contract and to have potential disagreements

## 3 Potential sources of disputes under PPP's

### During the construction phase

- Delays / Costs overruns for lands to be expropriated
- Delays in obtaining authorizations and permits
- Unpredictable archaeological discovery and geotechnical difficulties
- Unpredictable level of pollution and required level of environmental treatment measures
- Potential disagreements due to the multiple interfaces
- Poor or inadequate PPP scope limitation and risks allocation between the multiple parties



### 3 Potential sources of disputes under PPP's

#### During the operation and maintenance phase

- Disagreement on justification and level of penalties for non-compliance of performance criteria
- Change in law risks which impacts performance of the infrastructure => Disagreement on level of compensation
- Changes in the competitive environment which impacts performance of the infrastructure => Disagreement on level of compensation
- Potential disagreements from multiple interfaces and inadequate PPP scope limitation and risks allocation between multiple parties
- Disagreement on Hand Back requirements fulfillment

## 4 Dispute Prevention approaches - Overview

- The main approaches in Dispute Prevention for conventional contracts are applicable to PPP Contracts
- They all have the common goal of preventing disputes at a very early stage and providing formal or informal assistance with the aim of avoiding potential disputes and preserving the relationship between the parties
- These main approaches include partnering, claims appeal committee, early neutral evaluation and Dispute Boards which may not only serve the purpose of resolving but also preventing disputes

## 5 Dispute Prevention in PPP's

### Overall context

- Disputes analysis shows that under a PPP's disputes sources are comparable with other forms of conventional contracts (Turnkey contracts , D&B contracts, EPC, etc..)
- PPP Contracts are more complex because of their multi parties and multi goals structures
- But some of the PPP features may improve Dispute Prevention
- The following review aims to provide some initial thoughts on Dispute Prevention approaches under PPP's based on practical experience

## 5 Dispute Prevention in PPP's

### Project validation before implementation:

Because of long term commitments, PPP's undergo an intensive validation and review before contract award

### The project risk analysis:

- The Private Partner performs an in depth risk analysis for all phases during the entire PPP contract period. This analysis includes the risks identification, the potential impact evaluation (occurrence probability and cost impact) and the search for risk mitigation measures
- Based on this analysis, the Private Partner develops downside scenarios in order to anticipate potential difficulties while evaluating its impact on the PPP feasibility

## 5 Dispute Prevention in PPP's

### The project optimization / Competitive dialogue:

- Because of its life cycle nature, the project will undergo a project optimization process => This process favors a deeper review of the project while identifying areas of potential optimization and risks
- Increasing PPP bid processes include a competitive dialogue. This process will also favor a deeper review of the project not only by the Private Partner but also by the Public Partner who takes part to these dialogues
- The competitive dialogue is usually a 2 to 3 steps process where the project is at each step optimized and again scrutinized in details by both Partners

## 5 Dispute Prevention in PPP's

### Financial institution / Lenders involvement / Project Rating:

- The Private Partner in a PPP commits to provide the project finance (Mix of equity, bank loans, bonds)
- In addition to the previous project reviews, the project will undergo a fully independent due diligence managed by the Lenders and undertaken by its own advisors for all aspects of the PPP (legal, technical and commercial)
- In case of bond financing, the investment institution will require a bond rating. The PPP will undergo a due diligence by the bond guaranteeing institutions
- These processes provide an additional comfort in identifying, verifying and mitigating project risks

## 5 Dispute Prevention in PPP's

The Public and private Partner's close cooperation:

- The PPP contract features, coupled with usually high contract volumes and the fact that in most cases strategical infrastructures are involved, more or less naturally bring the PPP Partners to find pragmatic and acceptable solutions in cases of disagreement
- When PPP procurement procedure include a competitive dialogues process, the Partners learn from the very beginning to communicate and to work very closely together. This process provides an opportunity to develop communication and confidence between the Partners

## 5 Dispute Prevention in PPP's

### Contract Guarantees and Penalty regimes:

- The Private Partners have to provide guarantees during all phases on the project. Considering the usually high PPP contract volume these guarantees can rapidly represent significant amounts (several hundred million)
- Because of the long term nature and the guarantees running during the whole contract period, the Private Partner is encouraged to find pragmatic solutions in case of disagreement with the Public Partner



## 5 Dispute Prevention in PPP's

### Contract Guarantees and Penalty regimes:

#### Typical level of guarantees:

- Construction Performance Bond: 5 to 15 % of D&C amount
- Construction Delay penalties: up to 5 to 10 % of D&C amount
- Liability Cap - Construction scope: 25 to 40% of D&C amount
- O&M Performance guarantee: 3 to 6 months of O&M fee
- O&M penalty regime : 2 to 10 % of O&M Fee
- Liability Cap - O&M scope: 12 to 24 months of O&M fee
- Hand back guarantee: 2 to 5 % of initial construction volume

## 5 Dispute Prevention in PPP's

### Contract Guarantees and Penalty regimes:

- The Public Partner may in some cases provide some guarantees to balance certain risks (e.g. in road projects a minimum traffic /revenue guarantee)
- Practical experiences shows that the major incentive for the Public Partner to prevent disputes is the Public Partner's own reputation and credit rating
- In case of disputes caused by the Public Partner, a potential consequence could be that the Public Partner will have more difficulty of obtaining loans at competitive conditions

## 6 Conclusions

- PPP's are complex with multiple goals and contract layers
- PPP contract volume are significant both in the construction / operation phase. Conflicts can lead to disproportional dispute amounts
- In PPP's the Partners are bound together on a long term basis. A good relationship over these long periods become even more important

## 6 Conclusions

- The level of project analysis and validation before contract award is significant
- The level of cooperation between the Partners all along the contract period is intensive
- These features are of course not by them self a guarantee of not having conflicts and disputes between the Partners. PPP projects will also benefit from conventional procedure of Dispute Prevention
- But these features will improve the communication between the Partners which is essential in preventing disputes