12. BITKOM Forum Recht

Juristische Einbindung der Geschäfts- und Projektfinanzierungsmodelle PPP und BTO in internationale Großprojekte und IT-Standardverträge

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Forewarning

Yes, these charts are in English!

- They are based on charts I drafted already in English.
- Translating them back takes more time and sense out of them then leaving them in English.
- Partly because many of the terms exist only in English
- I trust you can cope with that …

… denn der mündliche Vortrag erfolgt auf Deutsch!

Just a Short Overview

- Once upon a time … or a little history
- What is it all about
- Some terms worth knowing
- PPP types and business models
- Questions & Answers
- How to put all this into practice

Project Finance is an Old Hat

Already used since Middle Ages. Famous examples:

- Construction of the Suez Canal by a special purpose corporation (*Compagnie universelle du canal maritime)* under a 99 years concession
- Construction of the Panama Canal by a special purpose corporation (*Société Civile Internationale du Canal Interocéanique*, later *Compagnie de Panama*) under a 99 years concession

=> First and typical BOOT models (build, own, operate and transfer)

Failure of Project Finance is an Old hat, Too …

Panama Canal exemplifies the difficulties of project financing:

- Huge disaster due to false estimations and bad preparation
- First Project company went bankrupt, project suspended, completion by new project company

Recent spectacular financial failures:

- Channel Tunnel linking frogs and limeys
- EuroDisney theme park near Paris
- Dabhol power project in India
  (Dabhol power company owned by Enron, GE and Bechtel)
- Local and smaller example: BOB (Bayerische Oberland Bahn)

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Typical Setting (1)

- Large-scale, capital-intensive project requires
- large, indivisible up-front investments in single-purpose assets
- joint effort of several related parties
- with high risk of co-ordination failures, conflicts of interest and free-riding
- Revenues to cover their costs generated only in the long term

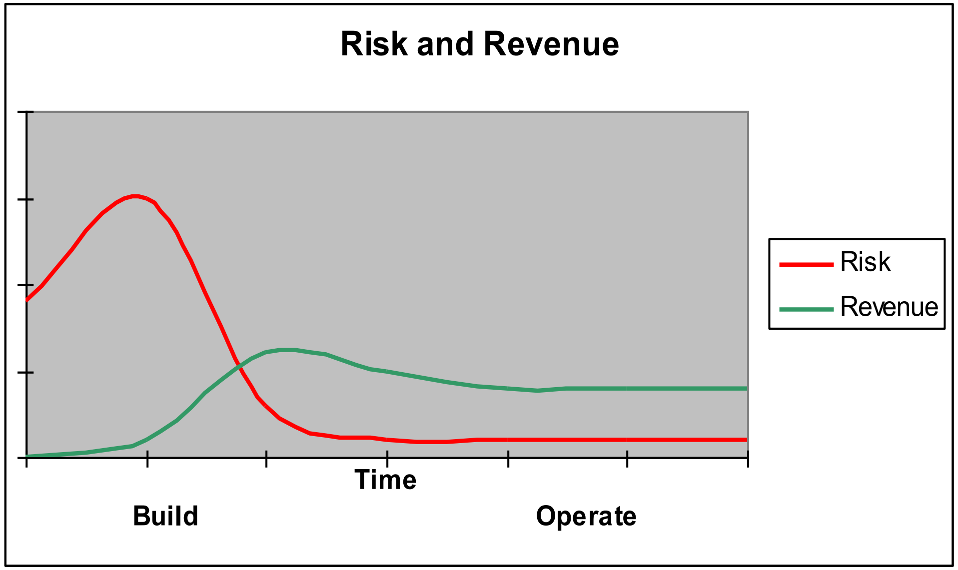
Typical Setting (2)

Typical allocation of risks and cash flow patterns:

- Completion risk, technological risks, environmental risks, capital expenditures: *Build Phase*
- Market risks, political risk, revenues: *Operation phase*

Provides this challenge:

- Matching the time profile of debt service and project revenue cash flows



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Some Terms Worth Knowing

BOT (build-operate-transfer):

Grantor provides a private company (invariably an SPV – special purpose vehicle) with a concession to build and operate a project for a certain term, to receive revenues from the sale of the project output combined with the obligation to transfer the project assets to the grantor at the end of the concession

BOO (build-own-operate):

Same as above, just without transfer of title to the state

BTO (build-transfer-operate):

Similar as above with earlier transfer of title

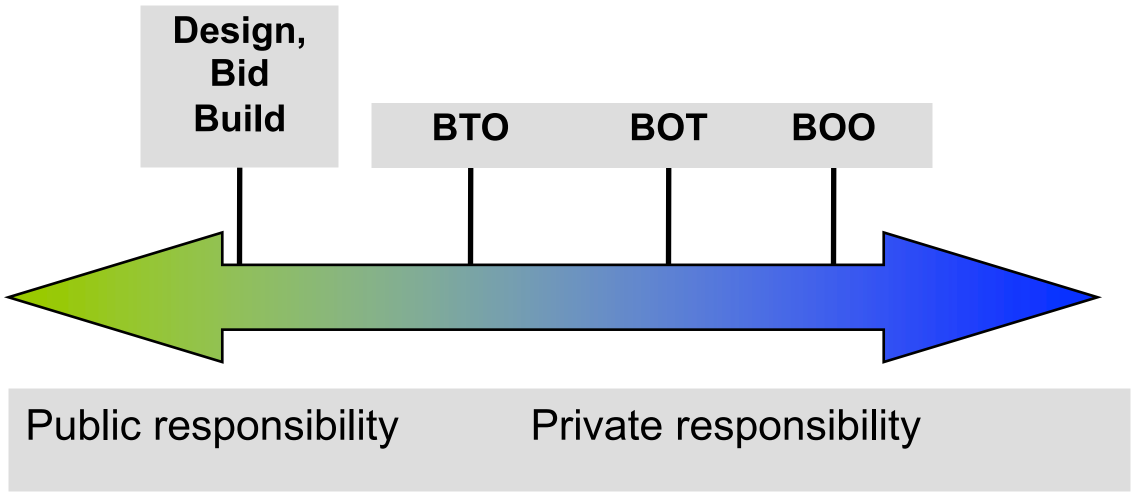
Some More Buzzwords to Boast

BBO	Buy, Build, Operate
BLT	Build, Lease, Transfer
BLOT	Build, Lease, Operate, Transfer
BOD	Build, Operate, Deliver
BOL	Build, Own, Lease
BOM	Build, Operate, Maintain
BOOST	Build, Own, Operate, Subsidise, Transfer
BOS	Build, Operate, Sell
BOTM	Build, Operate, Transfer, Maintain
BRT	Build, Rent, Transfer
CAO	Contract, Add, Operate
DBO	Design, Build, Own
DBOM	Design, Build, Operate, Maintain
DBOT	Design, Build, Operate, Transfer
DBOOT	Design, Build, Own, Operate, Transfer
FBOOT	Finance, Build, Own, Operate, Transfer
FOT	Finance, Operate, Transfer
LDO	Lease, Develop, Operate
LOM	Lease, Operate, Maintain
MOO	Modernise, Own, Operate
ROL	Rehabilitate, Operate, Lease
ROM	Rehabilitate, Operate, Maintain
ROO	Rehabilitate, Own, Operate
ROT	Rehabilitate, Operate, Transfer, Operate, Transfer
SPC	Special Purpose Company
SPV	Special Purpose Vehicle
VIA	Very Important Abbreviation

Having Read All That, You Might Feel Confused …

Don’t take all these terms too serious!

- Scientists are eager to create new forms or abbreviations each day
- They are just slightly different project delivery schemes
- Most of them can be combined module-wise
- They vary in the degree risks and services are outsourced:



PPP = Public-Private Partnership

- Basically a co-operative venture set up by a public and a private partner in order to fully or partially transfer public tasks to private stakeholders
- Not a selective definition, but rather a collective term for certain models of public-private co-operation
- Or, in other words, risk-sharing
- Introduced into scientific discourse in the mid-80s

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The term PPP does not tell much.

- It is necessary to look at the typical business models for P3s which have emerged on the market.

Two structural categories:

(i) Contractual PPP setups (basically financing models)

- leasing,
- sale and leaseback,
- hire-purchase
- or just private pre-financing

(ii) Institutionalised PPP (= organisational PPP) setups

- require the set-up of an incorporated company, called special purpose vehicle (“SPV”)

Typical Business Models Used in Institutionalised PPPs

Operator model (Betreibermodell)

- Government charges private company with operating a public facility.
  Private sector operator gets **pre-agreed remuneration** (mostly comprised of fixed annual basic fee for covering of fixed cost shares + operating rate) from Gvt. customer
  Typical example: German passport production by Bundesdruckerei
  => **low sales risk for private partner**

Concession model (Konzessionsmodell):

- Private sector operator provides certain services directly to the citizen. In return he receives the right to **finance his costs via fees levied from users** (in form of a concession, user fees sometimes supplemented by availability fee)
  Typical example: Italian motorways, A6 motorway in Spain
  => **higher sales risk, incentive to raise efficiency and to minimise the risks**

Management model (Betriebsführungsmodell):

- Government plans, builds and owns facility itself. It only assigns the **facility management to a private partner**, who receives payments for this.

Co-operation model = Participation model (Kooperationsmodell):

- All phases (like planning, constructing, operating and financing of a facility) are carried out by a **mixed private/public sector company**
  Typical example: German municipal water supply and waste disposal companies

What‘s All That Got to do With IT Contracts?

- **Be aware of finding all these schemes among typical IT contracts and even in German tenders!**
  - Renting of newly developed SW is merely a BTO model!
  - Operator model based financing has recently been tendered for software in health business
- **Be aware that BOT is often used to disguise lack of financial ressources!**
  - If customer starts by asking for BOT models, carefully check what is the need behind that before drafting contracts!
- **Sales tends to under-estimate risk exposure by IT projects**
  - Be careful enough to tell him: not all risks can be overcome by smart contracts!

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Why Are BOO/BOT Projects Attractive For Government Clients?

- Low cost of project within a certain timeframe
- Equal instalments instead of huge pre-investments
- Project risk shared by private sector
- Benefit of the private sector's ability to mobilise finances
- Possibility to benchmark Government operations with private sector operations, thus leading to improvements being made in the public sector operations

Why Should a Client Pay More For BOO/BOT Projects?

- **No doubt: perceived cost of BOO/BOT projects are higher than BT projects.**
  => they comprise borrowing cost

- **These extra costs need to be compared to the profit in the equity portion of the financing**
  - possibly higher than private financing due to bad rating
  - + passing off the risk to the supplier.

=> **If the profit element is higher than the debt cost BOO/BOT is attractive to the client.**

Golden Rules For SPC Project Finance

Have much more debt than equity:

- A typical project company is financed with 70 % limited or non-recourse debt and 30 % sponsors' equity.

Concentrate debt and equity ownership

- Enhances project monitoring by capital providers
- Facilitates to enforce project-specific governance rules or decisions

Avoid recourse of lenders to the sponsors

- If lenders do not accept limited or non-recourse debt try to offer hybrid structures between project and corporate finance (like PPP)

Use various forms of credit protection

- Implicit political risk guarantees are cheaper than explicit ones and of similar effectiveness

What Do I Think about the PPP Hype actually fading away already?

German PPP-Beschleunigungsgesetz …

- There are lots of PPP acts in various countries around the globe.
- All of them are more or less unaffected by real practice.
- In Germany, constitutional PPP still remain problematic and troublesome … and mostly not worth setting up

So, what is your advice?

- Continue to do business as before
- Meaning doing BOT, BTO and PPP models as before, often without even mentioning it
- Mind the contractual effects and efforts needed

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What is in for you

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Problem	Model	Advantages	Drawbacks/Risks	Show Stopper
Customer wants to avoid need to raise funds or to share development, sales or financial risks	Mostly BOT	At the end of the operating phase, government will inherit a well-operated project without investing public funds and with little risks	Complex process to set up and manage High financing cost Taking over risks from government can jeopardise return on investment for private partner	No RoI during operating phase
Customer wants to avoid the sales risk or debt collection	BOT with concession model	Low sales risk for Customer	Complex process to set up and manage High financing cost High risk for RoI	No RoI during operating phase
Customer does not want to pay for unused capacities / depreciation	BOO Franchise	Customer does pay for unused capacities / depreciation	Complex process to set up and manage High financing cost High risk for RoI	No RoI during operating phase
Customer requires equal instalments (= avoid high pre-investment)	Hire-purchase (Ratenkauf)	Quick returns for supplier	Suspension of payments without means to enforce returning the supplied goods Financing cost	Insolvent customer Customer does not have continuous stream of revenues
	Leasing		Depending on leasing scheme no risks to suspension of payments Financing cost	Customer needs to gain ownership of goods (e.g. ID cards)
	Purchase using outside ressources (Finanzkauf)	Quick returns for supplier	Mostly none, only if lender wants to share risks Financing cost	Customer does not provide enough securities to lender
Customer wants to pay according to his revenues	BOT Concession model	Calculation does not need to be revealed	Suspension of payments if out-sourced services fail to be used	Missing restraint to purchase supplied goods during operating phase

That‘s it For Today

Thank you for listening!