

## **7<sup>th</sup> Annual Meeting of the Infrastructure Consortium for Africa**

**(Paris, 17 and 18 May 2011)**

**Session 3 (Wednesday, 18 May, 9:00-11:00)**

### ***Legal and political conditions for private investment in infrastructures Business climate and governance, legal security, credible sectoral mechanisms***

There is a **considerable infrastructure gap** in African countries, especially the least advanced African countries, which puts a major break on development and growth of the continent. This bottleneck translates into average prices that are twice as high as in the rest of the world, low quality service, and inadequate supply (energy shortages).

The 2009 Africa Infrastructure Country Diagnostic (AICD) demonstrated that annual investment spending covers less than 50% of needs (\$45 billion of the **\$93 billion required**). This gap could be reduced by a third with **efficiency gains of \$17 billion** (servicing, maintenance, management). However there is still a need for an increase in investments of \$31 billion. The **public sector**, which supports two-thirds of current financing, **cannot address this problem alone**. The involvement of **private partners** is crucial.

Since the early 1990s, many African countries have sought to involve the private sector in the development and management of public service infrastructures for the well-being of peoples, development and poverty alleviation. However, only 10 to 15% of the private financing needed has been raised. Situations vary widely from sector to sector. Investments in service infrastructures where risks are more easily controlled and where there are faster returns, with few public service constraints, easily attract investors. Examples include the mobile telephone industry and container terminal management. Yet core sectors, meaning those of basic public services, particularly transport, urban services, power, water and public facilities, are less attractive.

We can observe an **erosion of the involvement and commitment of certain private stakeholders** that began working in Africa in the 1990s. Although this can also be attributed to economic reasons that will be studied in the second round table, the inability of the institutional and legal framework to attract investors and secure investments are determining factors. Extremely important work to improve the institutional, legal and contractual framework which is at the heart of governance progress now seems to be a priority. The Public Private Infrastructure Advisory Facility (PPIAF) and ICA guide “Attracting Investors to African Public-Private Partnerships” provides ample proof of this.

## **1) Improving institutional and legal frameworks**

A wide range of situations can be seen across the continent. South Africa has a sophisticated institutional and legislative framework for certain types of investments and private management of public infrastructures. Some sub-regions have high quality transnational legislation for general business law (Organization for the Harmonization of Business Law in Africa-OHADA), but legislation that is adapted to the development of public-private relationships in the public service infrastructure sector has yet to be drafted. At the other end of the spectrum, many countries emerging from conflict are penalized by inadequate or outdated legislation and by endemic legal instability and insecurity.

However, the application of laws is as important as the existence of a coherent and predictable legal framework. Arbitrary or inappropriate implementation of rules by administrations that do not have sufficient capacity in which certain staff are motivated by personal interest or are seeking very short term financial gains are a major disincentive to investors.

This legal insecurity is a reason why a number of African countries are poorly positioned in international rankings. A total of 25 African countries are ranked among the 30 worst countries in the 2011 Doing Business Report. To a lesser extent, 8 African countries hold the last 11 positions in the Logistics Performance Index published by the World Bank.

## **2) Providing effective dispute settlement procedures**

Effective recourse to address possible abuses of the administration and other economic players is crucial. The private sector often complains that the national justice system lacks integrity or is not independent, which is a disincentive to investment. Judges' economic and financial competence is generally extremely limited in economic and legal relationships between the public and private sectors.

Various solutions are possible:

- Step up efforts to provide specific training and technical assistance for judicial staff (judges, court clerks) in the economic and financial area.
- Establish regional jurisdictions, like the OHADA Common Court of Justice and Arbitration in the area of business law or jurisdictions linked to regional organizations, which could see their competence expand. Such regional courts could help pool rare technical expertise and provide guarantees of independence vis-à-vis national political powers that are necessarily farther away.
- Develop mediation and arbitration within a framework that is adapted to local traditions and particularities: simplify administrative arbitration procedures and put quality control bodies like the OHADA Arbitration Centre Secretariat in charge of arbitration administration. However, it is equally important that such bodies be given the necessary means and that they

be close enough to those involved in the legal dispute to demonstrate their effectiveness on a daily basis in an economic and legal environment that is acceptable to everyone.

### **3) Being pragmatic in the promotion and selection of public-private partnership models**

Beyond the pure privatization of public services, which often does not seem very sustainable in the long term for basic public services, there are several categories of private sector involvement in the management of public service infrastructures that maintain both government ownership and private interests.

Common law countries traditionally use partnership contracts (private finance initiative) whereby the State pays the company throughout the course of its operation, in return for providing the service with new equipment. This system has proven to be very efficient in launching certain investments, and its advocates consider that it takes advantage of the private sector's better ability to adhere to contracts and to optimize costs. In addition, it helps improve governance. Critics claim that there is no real transfer of risk. They have also criticized the cumbersome financing costs and procedures. They also claim that there is a risk of speculative profit, very limited scope to adapt to the public service, artificial reduction of government debt and more. Above all, this type of system has proved to be disadvantageous for public finances because the public sector has contracted new debt spanning many years, especially in African countries.

Other categories were widely used throughout the world during the industrial revolution and have continued to evolve and develop mainly in civil law countries practicing administrative case law. Such countries have gradually developed contract law for balanced public-private relationships that are part of the public service delegation model (concession, leasing). In this connection, public entities use a contract to entrust the entire management of a basic public service to a private company which is paid directly by the user. The viability of the system is based on establishing a service that is adapted to how much users can contribute, its evolution and its needs. In practice, with regard to the extent to which peoples' basic needs are met thanks to the improvement of such public services and with regard to the improvement of governance and other external factors, public investment fulfilling a number of requirements is justified if it enables a project to be carried out that otherwise would not exist.

Contrary to popular belief, the two categories do not conflict, but rather can be seen as a continuum. The selection of a certain category for a given project is determined by very pragmatic considerations that are now well known and based on whether a project is economically sound, government fiscal capacity and the amount of real security provided to the parties by the institutional, legal and contractual framework of the country.

It is therefore a good idea to promote the entire range of public-private partnerships that international experience has produced, in developed and developing countries alike, in order to increase the number of PPP projects that are easily acceptable to everyone without having

to increase the dissuasive transaction costs for everyone to the same extent. It will then be easy to make pragmatic decisions for similar projects based on the model that most effectively integrates past experience, while using an approach that corresponds to the type of infrastructure and user concerned.

It seems to be particularly important to use benchmarking and share best practices, especially with other southern countries (Latin America, Asia), in order to make more informed decisions. Meetings to share experience and education exchange programmes, like those funded in the 1990s by donors for African experts, could therefore also be revitalized.

#### **4) Drafting appropriate regulations**

This round table will address the regulation issue from a legal and contractual standpoint, with sharing risks as the focus on the round table on the economic and financial conditions for private investment.

The intervention of a credible regulator that is independent from government and lobbies may likewise provide guarantees to private investors. This also protects users from possible abuse of monopolies on the part of service providers.

Several types of regulators or regulations are possible:

- A sectoral or multi-sectoral external regulator, setting tariffs or acting within the framework of more or less administrated tariffs. Promoting regional sectoral regulators could be advantageous in terms of pooling rare technical expertise and in terms of independence.

The regulation body can also come up with a user consultation mechanism. This would be easy to do for companies. It requires, if the customers vary (water, power) a degree of civil society structure (consumer associations).

Beyond this institutional regulation, an independent investigatory press with economically qualified journalists, ready to denounce abuse, also has a role in this regulation.

- Contractual regulation: it is important not to underestimate how difficult it is to create an institutional framework that produces objective high quality external regulation where the three PPP parties (private sector, public sector, users) are all satisfied throughout the entire project cycle.

A contractual regulation framework providing objective references to regulate and adapt a contract along with bodies to facilitate or conduct ad hoc mediation may in some cases be extremely effective and transparent as long experience in civil law countries has shown.

Here again, it would be a good idea to be pragmatic in assessing beforehand and regulating to a minimum degree the most adapted options for different types or categories of projects.

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## Questions

### 1. Bolstering the legal and regulatory framework

- *Can we assist States in acquiring a comprehensive and stable legal framework, drawing on the most effective existing norms?*
- *How can we reinforce training for judicial staff when it comes to economic and financial issues?*
- *How can we promote, create or strengthen a sphere of action for dispute settlement mechanisms at regional level?*
- *How can we promote recourse to mediation and arbitration within a framework that is adapted to local realities?*
- *How can we raise awareness of the conditions required for effective regulation?*
- *Should we explore the possibility of regional regulatory mechanisms if there is a regional market?*

### 2. Promotion focused on Public-Private Partnerships

- *How can we raise awareness of all the advantages and potential of the different PPP categories, which are crucial to reaching the Millennium Development Goals and conditions required for them to work in Africa?*
- *How can we promote a process of selecting types of public-private partnerships that are adapted to the cost-effectiveness of the projects and their role in economic development, to production output and to the national and sectoral particularities?*

### 3. South-South cooperation and the role of the press

- *Should we revitalize exchanges of expertise and research missions especially in the South-South context?*
- *How can we build economic and financial expertise of the independent press?*

## Possible Guidelines for ICA work

- Study the possibility of establishing regional regulatory mechanisms
- Promote a process of selecting types of public-private partnerships that are adapted to the cost-effectiveness of the projects and their role in economic development, to production output and to the national and sectoral particularities
- Promote South-South cooperation by organizing seminars/conferences focused on sharing experience.