



## Legal system influence: Common law vs. Civil-administrative law

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# Introduction

- Comprehensive long term contracts in the road sector may take various forms. I intend to focus on new forms of long term contracts which are currently discussed in many countries *inter alia* due to the lack of public funds to meet the future needs in the road sector.
- Those contracts are contracts where the private party is requested to finance, build and operate a road or a highway.

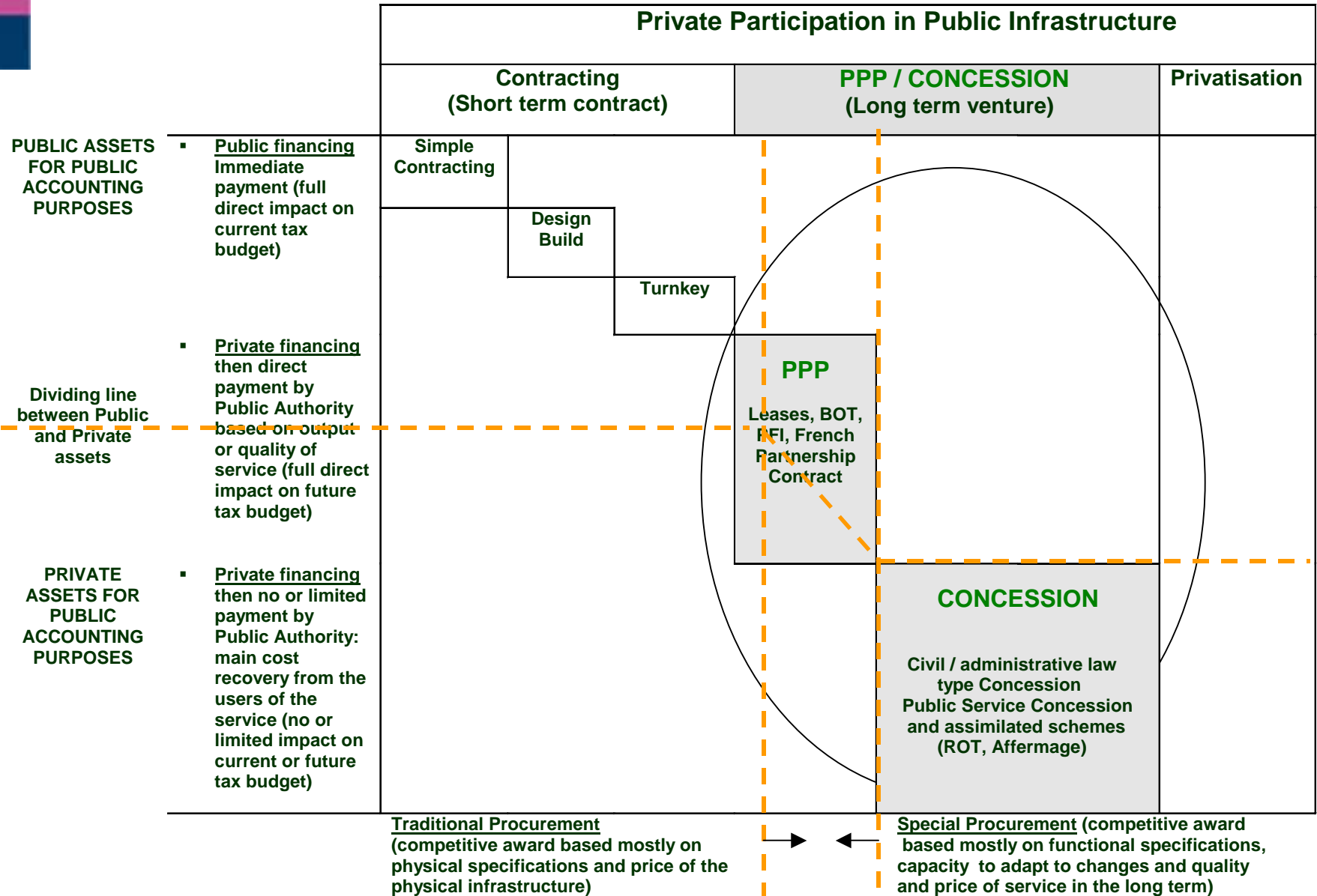
# Introduction (cont'd)

- They can take many forms but they belong generally to the PPI family (Private participation in Public Infrastructure) which is itself composed of two distinctive branches: the PPP and the Concession branch.
- Since these two contractual frameworks are sometimes considered as more or less similar or only divided by a risk border, it is useful to clarify the matter in a chart.

# Outlook of the PPI family

MINIMUM PRIVATE RISKS  
AND BENEFITS

MAXIMUM PRIVATE RISKS  
AND BENEFITS



## Recent history: a poor track-record

- In the last fifteen years, there has been a major impetus for PPP and Concessions around the world.
- However, it is generally recognized that the outcome is not satisfactory since:
  - many intended deals did not materialize
  - many deals which have been signed have experienced problems during the operation phase
- Unfortunately, renegotiation is a common feature and this casts a cloud on the sustainability of many of the PPP or Concession schemes in the public infrastructure sector.

# How to design sustainable comprehensive long term contracts?

- Colin Jordan has indicated in a recent interview that PIARC was concerned and eager to explore this area in an attempt to identify the conditions of success of PPPs.
- Nowadays, it is fair to say that the conditions of success are to a large extent dependant upon the quality of the “legal infrastructure” underlying a Concession or PPP scheme.
- For various reasons, the two main legal systems in the world are not currently equal in this regard. This deserves some explanations.

# How the legal system can influence the development and sustainability of Concessions and PPPs?

- Common law vs. civil law are often opposed.
  - Common law, based on case-law, is often considered to be more creative to develop complex transactions.
  - Civil law, based on written codes, appears more rigid at the outset, but also more secure in the long-run due to the easy reference to superior legal principles widely accepted.

# Influencing the development and sustainability (cont'd)

- Both systems give priority to the principle of freedom of contracts and on the *pacta sunt servanda* principle. In civil law, it is the codes which generally state that a contract amounts to a law as between the contracting parties.
- The real issue in Concessions and PPPs is whether a particular system has developed legal principles or best practices of general use for the various stakeholders and recognized by the courts.





# The civil-administrative law influence on facilitating comprehensive long term public service contracts

- It appears that the experience in long term public infrastructure contracts for financing, building and operating a public service infrastructure has been, in the recent history, far more developed in some civil law countries than in common law countries, for historical or economical reasons.
- Comprehensive and long term contractual schemes involving private party for the operation of a public service and having achieved a full circle over many decades are far beyond the figure of 10,000 in France only.

## Facilitating comprehensive long term public service contracts (cont 'd)

- The same is to a lesser extent true for France and other civil-law countries having an administrative law background similar to France (about forty countries in the world).
- In those countries, contractual schemes where a private party is entrusted with the operation of public services of various kind (water, power, railway, ports, airports, highways, etc.) became progressively regulated by a core of legal principles different from the general law of contracts.

# Facilitating comprehensive long term public service contracts (cont 'd)

- These developments did not come from the lawmaker but from administrative courts not limited by the Civil code principles. In essence, those courts are authorized to rule in equity when this is justified for the benefit of the user of the service.
- As a result, in many countries of the civil law world, a very pragmatic court system has regulated over the years public service contracts and more particularly public service Concession contracts.
- This has been essential to overcome the dilemma of most long term public service contracts entered into between a Public Authority and a private developer / operator.

# The comprehensive long-term contract dilemma

- The public authority wants to be satisfied that a highway or a road will be built and maintained for decades for best value for money and will remain always adapted to the needs of the end users.
- The private partner and the financial world will only agree to consider the venture if various risks, *inter alia* financial risks, are limited or under reasonable control by the private party. Any future uncertainty is a danger, and considering the adaptation to future conditions dictated by the need of the end user is a nightmare.
- In traditional legal terms, the dilemma amounts to a conflict between « *pacta sunt servanda vs. rebus sic stantibus* ».



# Overcoming the dilemma and the pragmatic solutions of administrative law

- Case after case, the administrative courts of some civil law countries have developed underlying principles applying to all public service contracts.
- They have been carved in such a way that they are easy to refer to. In addition, those principles often supersede contractual provisions to the contrary.
- Most of those legal principles are widely accepted and can be referred to as best practices, even outside of the civil law world.

# Overcoming the dilemma (cont 'd)

- They are often restated in the long term public service contracts.
- They facilitate the contract negotiations:
  - avoiding too many smart clauses developed by sophisticated lawyers having often little chance of meeting the test of sustainability, and
  - avoiding too detailed clauses attempting to foresee any situation which, in the public service sector, is in fact a dream.

# Conditions of success of comprehensive long term contracts

## 1. BEFORE CONTRACT AWARD: APPROPRIATE LEVEL OF STUDIES AND ECONOMIC MATRIX

- When, for instance, a private Concessionaire contracts for a highway and bears the demand risk, the following economic conditions must be ascertained.
  - The contract cannot be entered into at the outset unless it is demonstrated that there is an overall financial equilibrium foreseen for the whole venture permitting to a good Concessionaire to make a reasonable profit, and
  - It must be demonstrated that the scheme will provide a better value for money throughout the Concession period, for the end users.
- As a result, very detailed analysis on traffic forecasts and affordability of tariffs must be conducted. Half of the success of the venture lies in those analyses prior to awarding the contract.

## 2. UNDERLYING LEGAL AND CONTRACTUAL CONDITIONS

- Those conditions apply in order to supplement a contract. Sometimes they also supersede any clause to the contrary.

### **A. The general public service theory: underlying public service obligation and performance indicators**

This theory is based on three pillars:

- Non-discrimination between the users of the services (same price of service to everybody in same situation)
- Continuity of the service (service must be rendered in virtually any situation)
- Adaptation of the service to the public needs (service must be extended to additional potential users and the quality standard adapted to the needs)



## B. Particular rights belonging of the Public Authority

- to terminate the venture not only for default if a public service is not properly performed, but also for convenience almost at any time with prior notice, if such termination is in the public interest.
- to modify the original agreement in order to adapt the service to the best interest of the public.
- to impose other coercive measures, in case of substantial breach of obligations by the private partner (such as an automatic lien on the property and use of its workforce and equipment).

### C. Particular rights of the Developer / Operator

→ right to fair indemnification when the Public Authority exercises various sovereign rights in the interest of the public, based on the principle of full compensation, including not only the costs incurred but also loss of profits (“*damnum emergens*” and “*lucrum cessans*”).

→ right to adequate compensation when an unforeseen impediment (“*sujétions imprévues*”) occurs, i.e. in cases of unforeseen conditions of technical nature either during the construction phase or during rehabilitation or maintenance of the works.

## Conditions of success (cont 'd)

- right to reinstate the equilibrium of the contract conditions when a hardship (“*imprévision*”) situation arises, i.e. when the surrounding economic circumstances prevailing at the date of signature have substantially changed in an unforeseen manner (in a concession the financial equation or the concession matrix play a major role in simplifying any quantification in the long term).
- right to indemnification, when an action taken by the Public Authority results in an increase in the obligations of the private partner and such action was not reasonably foreseeable (provided, the private partner is not in default).



# Structuring successful long term public service contracts in the road and highway sector - Lessons learnt in the civil/administrative law world

**A.** Do not proceed with contract and negotiation if the Concession economic matrix based on provisional accounts is not sufficiently reliable and acceptable by all the parties involved.

For highway, for instance, focus on traffic forecast, acceptable tariffs, macro-economic issues (ex: overall economic development forecast and forecast of increase of cars and trucks) as well as investment costs, operation costs, amortisation etc. This matrix should indicate the potential for a reasonable rate of return and profits

## Lessons learnt (cont 'd)

**B.** Focus on functional specifications in terms of description and quality of services including some performance indicators not too detailed in order to remain valid many years down the line and avoid too detailed technical specifications.

Example for highway :

- ◆ availability time
- ◆ traffic capacity
- ◆ toll gate capacity and waiting time
- ◆ role and authorised activities in service areas

## Lessons learnt (cont 'd)

**C.** Prepare a risks and opportunities chart taking into account the well-tested administrative legal principles, and allocate the rights and obligations of each partner accordingly.

Example for highway :

- ◆ environmental issues and related authorizations, costs
- ◆ sub soil issues and related obligations: contamination, unforeseen conditions
- ◆ land use and right of way, expropriation, resettlement and related authorizations and obligations
- ◆ foreseeable changes of circumstances: competing infrastructures diverting the traffic, new safety requirement, currency fluctuation etc.
- ◆ reasonably unforeseeable changes of circumstances: clarify the scope of the changes of outside economic circumstances and of their impacts in the economic matrix which could trigger restoration of the financial equilibrium within certain limits.

## Lessons learnt (cont 'd)

**D.** Prepare a risks and opportunities chart taking into account the well tested administrative law principles and allocate the rights and obligations of each partner accordingly.

Example for highway:

- ◆ environmental issues and related authorization and cost
- ◆ sub soil issues and related obligations : contamination or unforeseen conditions
- ◆ land use and right of way, expropriation, resettlement and related authorizations and obligations
- ◆ foreseeable changes of circumstances : competing infrastructures diverting the traffic, new safety requirement, currency fluctuation etc
- ◆ reasonably unforeseeable changes of circumstances : clarify the scope of the changes of outside economic circumstances and of their impacts in the economic matrix which could trigger some sort of compensation to be negotiated or some sort of sharing to be negotiated with the objective of restoration of the financial equilibrium beyond certain parameters. 23e Congrès mondial de la Route - Paris 2007

# Conclusion

- Based on a long history of pragmatic case-law balancing public and private interest, and, allocating or reallocating risks and benefits, the administrative case-law of many civil law countries has developed well-tested legal principles and best practices for long term public service contracts where the private party bears in principle demand risk and is requested to adapt the contract to the public needs.



## Conclusion (cont 'd)

- Those schemes are known as public service Concession schemes and they are sometimes referred to by Public Authorities as a «magic recipe» because a Public Authority is then able to develop an efficient public infrastructure service such as a toll highway at no or very little cost for the tax budget.

## Conclusion (cont 'd)

- For other types of PPP schemes, where the private party does not bear the demand risk and where the Public Authority has to pay for the infrastructure from the tax budget over the life of the venture, the civil-administrative law system has no sufficient tested practices which could be proposed as underlying conditions for the success of such ventures. It may well be that in this area, the common law system under which those schemes have been recently developed may have more useful and practical answers.

## Conclusion (cont 'd)

- The future certainly lies in more cross-fertilization between the two legal systems in the interest of the development of sustainable comprehensive long term contracts in the road sector