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### PRIVATELY FINANCED INFRASTRUCTURE PROJECTS

Draft chapters of a legislative guide on privately financed infrastructure projects

Report of the Secretary-General

Addendum

#### Chapter I. GENERAL LEGISLATIVE CONSIDERATIONS

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## **LEGISLATIVE RECOMMENDATIONS**

### **General considerations (paras. 1-15)**

(1) The law should provide the contracting authorities in the host country with the necessary power to award concessions for infrastructure development and operation. It is advisable to review existing constitutional provisions so as to eliminate undesirable restrictions to private sector participation in infrastructure development and operation, or unnecessary limitations to the use of public property by private entities and obstacles to private ownership of infrastructure.

### **Scope of authority to award concessions (paras. 16-25)**

(2) The host country may wish to consider adopting legislative provisions that:

(a) Authorize contracting authorities in the host country, including, as appropriate, national, provincial and local authorities, to award concessions for the construction and operation of infrastructure of new infrastructure facilities or systems or for maintenance, repair, refurbishment, modernization, expansion and operation of existing infrastructure facilities and systems, or only for the management and delivery of a public service falling within their competence;

(b) Authorize the granting of concessions that extend to the entire region under the jurisdiction of the contracting authority or only to a geographical subdivision thereof, with or without exclusivity, as appropriate, in accordance with laws, regulations and policies applying to the sector concerned;

(c) Authorize the contracting authority or other agencies of the Government to transfer or make available to the concessionaire such public land or existing infrastructure that may be required for the execution of the project.

### **Administrative coordination (paras. 27-32)**

(3) The host country may wish to consider adopting legislative provisions requiring:

(a) That contracting authorities interested in developing a privately financed infrastructure projects, within their sphere of competence conduct a preliminary assessment of its feasibility, including economic and financial aspects such as expected economic advantages of the project, estimated cost and potential revenue anticipated from the operation of the infrastructure facility, as well as the environmental impact of the project;

(b) That the contracting authority concerned review existing statutory or regulatory requirements relating to the operation of infrastructure facilities of the type proposed with a view to identifying the main governmental bodies that have to give approvals, licences or authorizations or whose input will be otherwise required for the implementation of the project and take the necessary measures for coordinating their input to the proposed project.

**Authority to regulate infrastructure services (paras. 33-55)**

- (4) The host country may wish to consider adopting legislative provisions for the purpose of:
  - (a) Separating operational and regulatory functions and entrusting regulatory competence to legally and functionally independent bodies;
  - (b) Granting the regulatory body a sufficient level of autonomy to ensure that its decisions are taken without political interference or inappropriate pressures from infrastructure operators and public service providers.
- (5) The host country may wish to consider adopting legislative provisions that:
  - (a) Require the publication of rules governing regulatory procedures;
  - (b) Require that regulatory decisions state the reasons on which they are based and be accessible to interested parties through publication or other means;
  - (c) Provide for appeal procedures against decisions of regulatory bodies and adequate remedies to protect public service providers from arbitrary decisions of regulatory bodies.

## **NOTES ON LEGISLATIVE RECOMMENDATIONS**

### **A. General remarks**

1. The successful implementation of privately financed infrastructure projects requires a legal framework that provides contracting authorities in the host country with the necessary power to award concessions for infrastructure development and operation. According to the legal and political traditions of the country, this power may be derived from existing constitutional rules, laws, regulations or case law, or it may need to be established by new provisions. This section deals with some general issues which domestic legislatures may wish to consider when setting up the legal framework for privately financed infrastructure projects. Firstly, it is important for the legislature to consider the possible implications that the constitutional law of the host country may have for the implementation of these projects. Secondly, a choice has to be made regarding the level and type of instrument or instruments that need to be enacted and their scope of application. Lastly, it is important to consider how privately financed infrastructure projects are received in the legal tradition of the country, in particular which legal regime would apply to them.

#### **1. Constitutional law and privately financed infrastructure projects**

2. The constitutional law of a number of countries refers generally to the duty of the State to ensure the provision of public services. Some of them list the infrastructure and services sectors which come under the responsibility of the State, while in others the task of identifying those sectors is delegated to the legislator. Under some national constitutions, the provision of certain public services is reserved exclusively to the State or to specially created public entities. Other constitutions, however, authorize the State to award concessions to private entities for the development and operation of infrastructure and the provision of public services. In some countries, there are limitations to the participation of foreigners in certain sectors, or requirements that the State should participate in the capital of the companies providing public services.

3. For countries wishing to promote private investment in infrastructure it is important to review existing constitutional rules so as to identify possible restrictions to the implementation of privately financed infrastructure projects. In some countries, privately financed infrastructure projects have been delayed by uncertainties regarding the extent of the State's authority to award them. Sometimes, concerns that those projects might contravene constitutional rules on State monopolies or on the provision of public services have led to judicial disputes, with negative impact on the implementation of the projects.

4. It is further important to take into account constitutional rules relating to the ownership of land or infrastructure facilities. The constitutional law of some countries contains limitations to private ownership of land and certain means of production. In other countries, private property is recognized, but the constitution declares all or certain types of infrastructure to be State property. Prohibitions and restrictions of this nature can be an obstacle to the execution of projects that entail private operation, or private operation and ownership, of the relevant infrastructure.

5. Irrespective of the choice made by the Government regarding the ownership of infrastructure, it is important for a country wishing to attract private investment in infrastructure to ensure that the State is authorized to make available to the concessionaire such land or existing infrastructure as may be required for the execution of infrastructure projects. In some countries it has been found necessary to amend the constitution so as to provide the State with that authority.

## **2. Choice of a legislative approach**

6. Legislation frequently plays a central role in promoting private investment in public infrastructure projects. The law typically embodies a political commitment, provides specific legal rights and may represent an important guarantee of stability of the legal and regulatory regime. In most countries the implementation of privately financed infrastructure projects was in fact preceded by legislative measures setting forth the general rules under which those projects are awarded and executed.

7. In some countries, as a matter of legislative practice, it has been considered appropriate to adopt specific legislation regulating the execution and operation of one or more individual projects. In other countries with a well-established tradition of awarding concessions to the private sector for the provision of public services, the State is authorized by general legislation to award to the private sector any activity carried out by the public sector which has an economic value that makes such activity capable of being exploited by private entities. General legislation of this type creates a framework for providing a uniform treatment to issues that are common to privately financed projects in different infrastructure sectors. Countries that consider it desirable to adopt general legislation may wish to determine what issues are suitable for being dealt with at this legislative level, and what issues should be left for specific legislation, regulations or for the project agreement.

8. By its very nature, general legislation is normally not suitable to address all the particular requirements of different sectors. This is why the provision of certain public services is in several countries subject to special legislation governing specific infrastructure sectors (e.g. telecommunications, power generation and distribution, road and railway transportation). One of the arguments in favour of the adoption of sector-specific legislation, even in countries that have adopted general legislation addressing cross-sectoral issues, is that it allows the legislator to take into account the market structure in formulating rules governing the activities of service providers in each infrastructure sector (see above, "Introduction and background information on privately financed infrastructure projects", \_\_\_\_).

9. Sector-specific legislation typically sets forth the policy of the Government for the sector concerned, lays down the mechanisms for implementing such policy and provides the general rules for the provision of the relevant services. In many countries, sector-specific legislation was adopted at a time when a significant portion, or even the entirety of the national infrastructure constituted State monopolies. Recent national strategies for promoting private sector investment in infrastructure were often based on the results of extensive studies that analysed questions such as the extent of competition that could be introduced in the market as a whole or within specific segments of it, and considered the potential economic costs and expected benefits of abolishing legal monopolies or retaining them in full or in part (see, "Introduction and background information on privately financed

infrastructure projects”, \_\_\_\_). For countries interested in promoting private sector investment in infrastructure it is advisable to review existing sector-specific legislation so as to ascertain their suitability for privately financed infrastructure projects.

10. Sector-specific legislation may further play an important role in establishing a framework for the regulation of individual infrastructure sectors (see below, paras.33-55). Legislative guidance is particularly useful in countries at the initial stages of setting up or developing national regulatory capacities. Such legislation is also useful to reassure the lenders and the concessionaire that the regulators do not have unlimited discretion in the exercise of their functions, but are bound by the parameters provided by the law. However, it is generally advisable to avoid rigid or excessively detailed legislation, which in most cases would not be adequate to the long-term nature of privately financed infrastructure projects.

11. Each instrument has its specificity which makes it more or less appropriate for given circumstances. Legislative provisions may be difficult to change. Many countries have used them to establish the general principles for the organization of infrastructure sectors and the basic policy, institutional and regulatory framework. However, the law may not be the best instrument to set detailed technical and financial requirements. Many countries have preferred to enact regulations setting forth more detailed rules to implement the general provisions of domestic laws on privately financed infrastructure projects. Regulations are found to be easier to adapt to a change in environment, whether the change results from the transition to market-based rules or from external developments, such as new technologies or changing economic or market conditions. Whatever the instrument used, clarity and predictability are of the essence. However, this does not imply that all matters have to be clearly settled up-front.

### **3. Legal regime of privately financed infrastructure projects**

12. In some legal systems, in particular those belonging to the civil law tradition, the provision of public services is governed by a body of law known as “administrative law”, which covers a wide range of State functions. In most of those countries there are well-defined concepts of administrative law that may cover certain forms of infrastructure projects, such as “public works concession”, “public services concession”, or “delegations”, “licences” or “permissions” for the provision of certain forms of public services. Various rights and obligations of the parties may derive from statutory provisions, judicial precedent or general principles of law, according to the type of the project and the nature of the instrument of award (e.g. whether a bilateral agreement or a unilateral act).

13. In some of those legal systems, for instance, the Government generally has the right to revoke administrative contracts or to modify their scope and terms, for reasons of public interest, usually subject to compensation of loss caused to, or additional cost incurred by, its contractors. Additional rights of the Government might include extensive monitoring and inspection rights, as well as the right to impose sanctions on the private operator for failure to perform (see chapter V, “Infrastructure development and operation”, \_\_\_\_). In some countries, there are special provisions for the settlement of disputes arising out of Government contracts, and there may be limitations to the right of governmental agencies to agree on non-judicial procedures for settlement of disputes (see

chapter VIII, “Settlement of disputes”, \_\_\_\_). At the same time, some legal systems recognize certain implied conditions in all Government contracts that afford a certain level of protection to Government contractors, such as the right to review the terms of the contract following unforeseen changes in the circumstances for the purpose of restoring its economic and financial balance (see chapter V, “Infrastructure development and operation”, \_\_\_\_).

14. The existence of a special legal regime applicable to infrastructure operators and public service providers is not limited to the legal systems referred to above. In several countries belonging to the common law tradition special rules have been developed for Government contracts, often through the extensive use of standard forms and terms. Those special rules typically give the Government certain powers of termination or modification balanced by an obligation to indemnify the contractor against the damage sustained by reliance on the contract. In some common law jurisdictions detailed rules have been developed to govern the activities of operators of public utilities (e.g. telecommunications, railways, electricity).

15. In countries where Government contracts are subject to a special regime, it may be advisable for the legislature to review the adequacy of the existing regime for privately financed infrastructure projects and to identify possible difficulties that might result from its application. For purposes of transparency and to avoid doubts by potential foreign as well as domestic investors, it may be useful to incorporate into special legislation pertaining to privately financed infrastructure projects those rights and obligations that are implied or are not treated systematically in the legal system and which are found to be appropriate in connection with those projects (see chapter V, “Infrastructure development and operation”, \_\_\_\_). By the same token, the enactment of general legislation may provide an opportunity for introducing new rules to facilitate privately financed infrastructure projects or to exclude the application of those rules of law which are found to pose obstacles to their execution.

## **B. Scope of authority to award concessions**

16. The implementation of privately financed infrastructure projects may require the enactment of special legislation or regulations authorizing the State to entrust the provision of public services to private entities or decentralized entities wholly or partially owned by the State. Besides being sometimes needed to satisfy national constitutional and other requirements, the enactment of express legislative authorization may be an important measure to foster the confidence of potential investors, national or foreign, in a national policy to promote private sector investment in infrastructure. In many countries, legislative provisions on the authority to grant concessions for infrastructure projects are not limited to identifying the agencies of the Government which are vested with such authority. They would typically determine the scope of concessions that may be granted by the contracting authorities and define the ownership regime of the assets related to the project.

### **1. Authorized agencies and relevant fields of activity**

17. In some legal systems where the State is directly responsible for the provision of public services this function may not be delegated without prior legislative authorization. For those



countries that wish to attract private investment in infrastructure, it is therefore particularly important that the law states clearly the authority of the Government to entrust to entities other than governmental agencies the right to provide certain public services and to charge a price for them. Such a general provision in the enabling legislation may be particularly important in those countries where public services are State monopolies, or where it is envisaged to engage private entities to provide certain services that used to be available to the public free of charge. In some countries, the absence of prior legislative authorization has given rise to judicial disputes challenging the concessionaire's authority to require the payment of a price for the services provided.

18. Furthermore, where general legislation is adopted, it is advisable to indicate clearly the agencies or levels of government competent to award infrastructure projects to the private sector. It may be useful to consider the extent of powers that may be needed by authorities other than the central Government to carry out projects falling within their purview. For clarity purposes, it may be also advisable to identify in such general legislation those fields of activity in which concessions may be awarded. These provisions may be instrumental to ensuring an adequate level of administrative coordination (see further below, paras. 26-32).

## **2. Purpose and scope of concessions**

19. It may be useful for the law to define the nature and purpose of privately financed infrastructure projects for which concessions may be awarded in the host country. One possible approach may be to define the various categories of projects according to the extent of the rights and obligations assumed by the concessionaire (e.g. "build-operate-transfer", "build-own-operate", "built-transfer-operate", "build-transfer"). However, given the wide variety of schemes that may come into play in connection with private investment in infrastructure, it may be difficult to provide exhaustive definitions of all of them. As an alternative, the law could generally provide that concessions may be awarded for the purpose of entrusting an entity, private or public, with the obligation to carry out infrastructure works and deliver certain public services, in consideration for the right to charge a price for the use of the facility or premises or for the service or goods it generates, or for other payment or remuneration agreed to by the parties. The law could further clarify that concessions may be awarded for the construction and operation of a new infrastructure facility or system or for maintenance, repair, refurbishment, modernization, expansion and operation of existing infrastructure facilities and systems, or only for the management and delivery of a public service.

20. Another important issue concerns the nature of the rights vested upon the concessionaire. One of the central questions arising in connection with privately financed infrastructure projects is whether the right to provide the service is exclusive or whether the project company will face the competition from other infrastructure facilities or service providers. Exclusivity may concern the right to provide a service in a particular geographical region (e.g. a communal water distribution company) or embrace the whole territory of the country (e.g. a national railway company); it may relate to the right to supply one particular type of goods or services to one particular customer (e.g. a power generator being the exclusive regional supplier to a power transmitter and distributor) or to a limited group of customers (e.g. a national long-distance telephone carrier providing connections to local telephone companies).

21. The decision whether or not to grant exclusivity rights to a certain project or category of projects should be taken in the light of the host country's policy for the sector concerned. As discussed earlier, the scope for competition varies considerably in different infrastructure sectors. While certain sectors, or segments thereof, have the characteristics of natural monopolies, in which case open competition is usually not an economically viable alternative, other infrastructure sectors have been successfully opened to free competition (see "Introduction and background information on privately financed infrastructure projects", \_\_\_\_).

22. Therefore, it is desirable to deal with the issue of exclusivity in a flexible manner. Rather than excluding or prescribing exclusive concessions, it may be preferable for the law to authorize the Government to grant exclusive concessions when it is deemed to be in the public interest, such as in cases where the exclusivity is justified for the purpose of ensuring the technical or economical viability of the project. The contracting authority may be required to state the reasons for granting an exclusive concession for each particular case. Such general legislation may be supplemented by sector-specific laws regulating the issue of exclusivity in a manner suitable for each particular sector.

### **3. Ownership and use of infrastructure**

23. A number of countries have provisions on the preservation and protection of State property, including special procedures and authorizations required for transferring the title to such property to private entities or granting to private entities the right to use governmental property. Whatever choice is made by the Government regarding the ownership of the infrastructure facility to be built, modernized or rehabilitated, it is important to ensure that the contracting authority has sufficient powers to transfer or make available to the project company, as appropriate, any land or existing infrastructure required for the execution of the project for a period not less than the duration of the project agreement.

24. The ownership regime for a particular project may be the result of practical considerations, such as the operational life of the infrastructure or the interest of the Government in retaining title to it. Moreover, in some projects the parties may wish to distinguish between assets that are to be owned by or reverted to the Government at the end of the concession period, and other assets acquired by the concessionaire during that period and which remain the concessionaire's property. In any event, the concessionaire would need assurances that its rights in respect of the project assets, no matter what form they may take, are based on sufficient legislative authority and that it will be able to enforce them against third parties. The same concern will be shared by the lenders and other project investors. Furthermore, in view of the legal restrictions that apply in many countries to the use of public property by private entities, the Government may necessitate prior legislative authorization to allow the concessionaire to use any additional public property that may be needed for the execution of the project, such as adjoining land, roads and other facilities.

25. Therefore, it is advisable that the relevant law clarify the nature of the property rights, if any, that may be granted to the concessionaire, taking into account the type of infrastructure concerned. Furthermore, it might be useful for the law to authorize the Government to grant to the concessionaire the right to use land, roads and other supporting facilities not directly related to the

project, as required for the construction and operation of the infrastructure, under the terms and conditions to be provided in the project agreement.

### **C. Administrative coordination**

26. Depending on the administrative structure of the host country, privately financed infrastructure projects may require the involvement of several governmental agencies, at various levels of Government. For instance, the competence to lay down regulations and rules for the activity concerned may rest in whole or in part with a governmental agency at a level different from the one that is responsible for providing the relevant service. It may also be that both the regulatory and the operational functions are combined in one entity, but that the authority to award Government contracts is centralized in a different governmental agency. For projects involving foreign investment, it may also happen that certain specific competences may fall within the mandate of the agency of the Government that is responsible for approving foreign investment proposals.

#### **1. Coordination of preparatory measures**

27. One important measure to ensure the successful implementation of privately financed infrastructure projects is the requirement that the relevant governmental agency conduct a preliminary assessment of the project's feasibility, including economic and financial aspects such as expected economic advantages of the project, estimated cost and potential revenue anticipated from the operation of the infrastructure facility and the environmental impact of the project. The preliminary conclusions reached at this stage will play a crucial role in conceiving the type of private sector involvement that is sought for the implementation of the project, for instance, whether the infrastructure facility will be owned by the Government and temporarily operated by the private entity, or whether the facility will be owned and operated by the project company.

28. Following the identification of the future project, it is for the Government to establish its relative priority and to assign human and other resources for its implementation. At that point, it is desirable that the Government review existing statutory or regulatory requirements relating to the operation of infrastructure facilities of the type proposed with a view to identifying the main governmental bodies whose input will be required for the implementation of the project. It is also important, at this stage to consider the measures that may be required in order for the contracting authority and the other governmental agencies involved to perform the obligations they may reasonably anticipate in connection with the project. For instance, the Government may need to make advance budgeting arrangements to enable it to meet financial commitments that extend over several budgetary cycles, such as long term commitments to purchase the project's output (see below, chapter IV, "The project agreement", \_\_\_\_). Furthermore, a series of administrative measures may be needed to implement certain forms of support provided to the project, such as tax exemptions and customs facilitation (see chapter II, "Government support", \_\_\_\_), and the time required may be considerable.

## **2. Arrangements for facilitating the issuance of licences and permits**

29. The legislation may play a useful role in facilitating the issuance of approvals and licences that may be needed in the course of a project (such as licences under foreign exchange regulations; licences for the incorporation of the concessionaire; authorizations for the employment of foreigners; registration and stamp duties for the use or ownership of land; importation licences for equipment and supplies; construction licences; licences for the installation of cables or pipelines; licences for bringing the facility into operation; spectrum allocation for mobile communication). The required licences and authorizations may fall within the competence of various organs at different levels of the administration and the time required for their issuance may be significant, particularly when the approving organs or offices were not originally involved in conceiving the project or negotiating its terms.

30. By the time the project agreement is signed, the concessionaire will normally have spent considerable time and invested significant sums in the project (e.g. preparation of feasibility studies, engineering design and other technical documents; preparation of bidding documents and participation in the bidding process; negotiation of the project agreement, loan agreements and other project-related contracts; hiring consultants and advisers). The possibility of not obtaining the licences needed for the construction of the facility may dissuade serious investors from competing for the award of the project. Furthermore, delay in bringing an infrastructure project into operation as a result of missing licences is likely to compromise the project's financial viability or cause considerable loss to its investors. Where the additional financial cost cannot be recovered by means of an extension of the concession period, or by raising the tariffs or charging higher prices, the concessionaire might turn to the Government for redress or support. The consequence would often be an increase in the cost of the project and in its cost to the public.

31. Thus, an early assessment of licences needed for a particular project may help to avoid delay in the implementation phase. A possible measure to enhance the coordination in the issuance of licences and approvals might be to entrust one organ with the authority to receive the applications for licences, to transmit them to the appropriate agencies and monitor the issuance of all licences listed in the request for proposals and other licences that might be introduced by subsequent regulations. The law may also authorize the relevant agencies to issue provisional licences and provide a time period beyond which those licences are deemed to be granted unless they are rejected in writing.

32. However, it should be noted that the distribution of administrative authority among various levels of government (e.g. local, regional and central) often reflect fundamental principles of a country's political organization. Therefore, there are instances where the Government would not be in a position to assume responsibility for the issuance of all licences or to entrust one single body with such a coordinating function. In those cases, it is advisable to consider alternative measures to counter the possibility of delay that might result from such distribution of administrative authority, such as, for instance, measures intended to make the process of obtaining licences more transparent and efficient. Furthermore, the Government might wish to consider providing some assurance that it will as much as possible assist the concessionaire in obtaining licences required by domestic law, for instance by providing information and assistance to bidders regarding the required licences to be

obtained, as well as the relevant procedures and conditions. From a practical point of view, in addition to coordination among various levels of government and various governmental departments, there is a need for ensuring consistency in the application of criteria for the issuance of licences and for the transparency of the administrative process.

#### **D. Authority to regulate infrastructure services**

33. The provision of certain public services is in a number of countries subject to a special regulatory regime. The regulatory regime in a given country and sector defines the rights and obligations of service providers, consumers, regulatory bodies and the Government. This framework consists of substantive rules, procedures, instruments and institutions and it represents an important instrument to implement the governmental policy for the sector concerned (see “Introduction and background information on privately financed infrastructure projects”, \_\_\_\_). Depending on the institutional structure of the country concerned and on the allocation of powers between different levels of Government, provincial or local legislation may govern some infrastructure sectors, in full or concurrently with national legislation.

34. Regulation of infrastructure services involves a wide range of general and sector-specific issues, which may vary considerably according to the social, political, legal and economic reality of each host country. While occasionally discussing some of the main regulatory issues that are encountered in a similar context in different sectors (see, for instance, chapter V, “Project execution”, \_\_\_\_), the *Guide* is not intended to exhaust the legal or policy issues arising out of the regulation of various infrastructure sectors.

35. The *Guide* assumes that the host country has in place the proper institutional and bureaucratic structures and human resources necessary to the implementation of privately financed infrastructure projects. Nevertheless, as a contribution to domestic legislatures considering the need for, and desirability of, establishing regulatory bodies for monitoring the provision of public services, this section discusses some of the main institutional and procedural issues that arise in that connection. The discussion contained in this section is illustrative of different options that have been used in domestic legislative measures to set up a regulatory framework for privately financed infrastructure projects, but the *Guide* does not thereby advocate the establishment of any particular model or administrative structure. Practical information and technical advice may be obtained from international financial institutions which carry out programmes to assist their member countries in setting up an adequate regulatory framework (such as the World Bank and the regional development banks).

##### **1. Regulatory bodies**

36. The term “regulatory bodies” refers to the institutional mechanisms required to implement and monitor the rules governing the activities of infrastructure operators. Because the rules applicable to infrastructure operation often allow for a degree of discretion, a body is required to interpret and apply them, monitor compliance, impose sanctions, and settle disputes arising out of the implementation of the rules. The specific regulatory tasks and the amount of discretion they involve will be determined by the rules in question, which can vary widely.

**(a) Sectoral attributions of regulatory bodies**

37. Regulatory responsibilities may be organized on a sectoral or cross-sectoral basis. Countries that have opted for a sectoral approach have in many cases decided to place closely linked sectors or segments thereof under the same regulatory structure (e.g. a common regulatory body for power and gas or for airports and airlines). Other countries have organized regulation on a cross-sectoral basis, in some cases with one regulatory entity for all infrastructure sectors, and in others with one entity for utilities (water, power, gas, telecommunications) and one for transport. In some countries the attributions of regulatory bodies might also extend to several sectors within a given region.

38. Regulatory bodies whose competence is limited to a particular sector usually foster the development of technical, sector-specific expertise. Sector-specific regulation may facilitate the development of rules and practices that are tailored to the needs of the sector concerned. However, the decision between sector-specific and cross-sectoral regulation depends in part on the country's regulatory capacity. Countries with limited expertise and experience in infrastructure regulation may find it preferable to reduce the number of independent structures and try to achieve economies of scale.

**(b) Institutional mechanisms**

39. The range of institutional mechanisms for the regulation of infrastructure sectors varies greatly. While there are countries which entrust regulatory functions to organs of the Government (e.g. the concerned ministries or departments), other countries have preferred to establish autonomous regulatory bodies, separate from the Government. Some countries have decided to subject certain infrastructure sectors to autonomous and independent regulation while leaving others under ministerial regulation. Sometimes, powers may also be shared between an autonomous regulatory body and the Government, as is often the case with respect to licensing. From a legislative perspective, it is important to devise institutional arrangements for the regulatory functions which ensure to the regulatory body an adequate level of efficiency, taking into account the political, legal and administrative tradition of the country.

40. The efficiency of the regulatory regime is in most cases a function of the objectiveness with which regulatory decisions are taken. This, in turn, requires that regulatory bodies should be able to take decisions without interference or inappropriate pressures from infrastructure operators and public service providers. To that effect, legislative provisions in several countries require the independence of the regulatory decision making process. In order to achieve the desired level of independence it is advisable to separate the regulatory functions from operational ones by removing any regulatory functions that may still be vested with the public service providers and entrust them to a legally and functionally independent entity. Regulatory independence is supplemented by provisions to prevent conflicts of interest, such as prohibitions for staff of the regulatory body to hold mandates, accept gifts, enter into contracts or have any other relationship (directly or through family members or other intermediaries) with regulated companies, their parents or affiliates.

41. This leads to a related issue, namely the need to minimize the risk of decisions being made or influenced by a body that is also the owner of enterprises operating in the regulated sector, or a

body acting on political rather than technical grounds. In some countries it was felt necessary to provide the regulatory body with a certain degree of autonomy vis-à-vis the political organs of Government. Independence and autonomy should not be considered solely on the basis of the institutional position of the regulatory function, but also on the basis of its functional autonomy (i.e. the availability of sufficient financial and human resources to discharge their responsibilities adequately).

**(c) Mandate of regulatory bodies**

42. The law setting up a regulatory mechanism often stipulates a number of general objectives that should guide the actions of regulatory bodies, such as the promotion of competition, the protection of users' interests, the satisfaction of demand, the efficiency of the sector or the public service providers, their financial viability, the safeguarding of the public interest or of public service obligations, and the protection of investors' rights. Having one or two overriding objectives helps clarify the mandate of regulatory bodies and establish priorities among sometimes conflicting objectives. A clear mandate may also increase a regulatory body's autonomy and credibility.

**(d) Powers of regulatory bodies**

43. Regulatory bodies may have decision-making powers, advisory powers or purely consultative powers or a combination of these different levels of powers depending on the subject matter. In some countries, regulatory bodies were initially given limited powers, which were expanded later as the regulatory bodies established a track record of independence and professionalism. The legislation often specifies which powers are vested with the Government and which ones with a regulatory body. Clarity in this respect is important to avoid unnecessary conflicts and confusion. Investors, as well as consumers and other interested parties, should know to whom to turn with various requests, applications or complaints.

44. Selection of public service providers, for example, is in many countries a process involving the Government as well as the regulatory body. If the decision to award a project involves broad judgment of a political rather than technical nature, which may often be the case in the context of infrastructure privatization, final responsibility often rests with the Government. If, however, the award criteria are more technical, as may be the case with a liberal licensing regime for power generation or telecommunications services, many countries entrust the decision to an independent regulatory body. In other cases, the Government may have to ask the regulatory body's opinion prior to awarding a concession. On the other hand, some countries exclude direct involvement of regulatory bodies in the award process on the basis that it could affect the way they later regulate the provision of the service concerned.

45. The jurisdiction of regulatory bodies normally extends to all enterprises operating in the sectors they regulate, with no distinction between private and public enterprises. The use of some regulatory powers or instruments may be limited by law to the dominant public service providers in the sector. A regulatory body may, for example, have price policing powers only vis-à-vis the incumbent or dominant public service provider, while new entrants may be allowed to set prices freely.

46. The matters on which regulatory bodies have to pronounce themselves range from normative responsibilities (e.g. rules on the award of concessions, conditions for certification of equipment) to the actual award of concessions; the modification of such instruments; the approval of contracts or decisions proposed by the regulated entities (e.g. a schedule or contract on network access); the definition and monitoring of an obligation to provide certain services; the oversight over public service providers (in particular compliance with licence conditions, norms, performance targets); tariff setting or adjustments; vetting of subsidies, exemptions or other advantages that could distort competition in the sector; sanctions; and dispute settlement.

#### **(e) Composition of regulatory bodies and their staff**

47. When setting up a regulatory body, a few countries have opted for a regulatory body comprised of a single officer, whereas most others have preferred a regulatory commission. A commission may provide greater safeguards against undue influence or lobbying and may limit the risk of rash regulatory decisions. A one-person regulatory body, on the other hand, may be able to reach decisions faster and may be held more accountable. To improve the management of the decision making process in a regulatory commission, the number of members is often kept small (typically three or five members). Even numbers are often avoided to prevent a deadlock, though the chairman could have a casting vote.

48. To increase the regulatory body's autonomy, different institutions may be involved in the nomination process. In some countries regulatory bodies are appointed by the Head of State based on a list submitted by parliament; in others the executive branch of the Government appoints the regulatory body but subject to confirmation by parliament or upon nominations submitted by parliament, user associations or other bodies. Minimal professional qualifications are often required of regulatory bodies, as well as the absence of conflicts of interest that might disqualify them for the function. Mandates of members of regulatory commissions may be staggered in order to prevent total turnover and appointment of all members by the same administration; staggering also promotes continuity in regulatory decision making. Mandates are often for a fixed term, may be non-renewable and may be terminated before the expiry of the term for limited reasons only (such as crime conviction, mental incapacitation, gross negligence or dereliction of duty). Regulatory bodies are often faced with experienced lawyers, accountants and other experts working for the regulated industry and need to be able to acquire the same level of expertise, skills and professionalism, either in-house or by hiring outside advisers as needed. They are often allowed to subcontract to outside experts certain regulatory tasks short of the ultimate regulatory decision.

#### **(g) Budget of the regulatory body**

49. Stable funding sources are critical in order for the regulatory body to function adequately. In many countries, the budget of the regulatory entity is funded by fees and other levies on the regulated industry. Fees may be set as a percentage of the turnover of the public service providers, or be levied for the award of licences, concessions or other authorizations. In some countries, the entity's budget is complemented as needed by budget transfers provided in the annual finance law. However, this may create an element of uncertainty that may reduce the regulatory body's autonomy.



## **2. Regulatory process and procedures**

50. The regulatory framework typically includes procedural rules governing the way the institutions in charge of the various regulatory functions have to exercise their powers.

### **(a) Procedures**

51. The credibility of the regulatory process requires transparency and objectivity, irrespective of whether regulatory authority is exercised by a Government department or minister or by an autonomous regulatory body. Rules and procedures should be objective and clear so as to ensure fairness and impartiality. For transparency purposes, the law should require that they be published. Regulatory decisions should state the reasons on which they are based and should be made accessible to interested parties, through publication or other appropriate means.

52. Transparency may be further enhanced, as required by some laws, by the publication by the regulatory body of an annual report on the sector, including, for example, the decisions taken during the exercise, the disputes that have arisen and the way they were settled. Such annual report may also include the accounts of the regulatory body and an audit thereof by an independent auditor. Legislation in many countries further requires that this annual report be submitted to a committee of parliament.

53. Regulatory decisions may impact on the interests of diverse groups, including the concerned public service provider, its current or potential competitors, and business or non-business users. In many countries, the regulatory process includes consultation procedures for major decisions or recommendations. In some countries, this consultation takes the form of public hearings, in others of consultation papers on which comments from interested groups are solicited. Some countries have also established consultative bodies comprised of users and other concerned parties and require that their opinion be sought before major decisions and recommendations are made. To enhance transparency, comments, recommendations or opinions resulting from the consultation process may have to be published or made publicly available.

### **(b) Sanctions and appeals**

54. In many countries, the law gives regulatory bodies some coercive or punitive powers. Such powers may include the authority to modify, suspend or withdraw a concession; the right to set the terms of contracts between public service providers (e.g. interconnection or access agreements); to issue injunctions and orders to public service providers; to impose civil penalties including penalties for any delay in implementing the regulatory body's decision, and to initiate criminal or other court procedures.

55. Legislators have often provided for appeal procedures against decisions of a regulatory body. Appeals procedures are an essential element to protect public service providers against arbitrary decisions by regulatory bodies. However, in order to prevent the regulatory uncertainty that may arise from appeals intended primarily to delay the effect of regulatory decisions, the laws of many countries limit the causes that give ground to appeal. It is therefore desirable to strike a balance

between the protection of legitimate rights of the public service providers and the efficiency of the regulatory system. It is often essential that decisions be made quickly. For instance, withdrawal of a competitor's access to an infrastructure network could drive the competitor into bankruptcy if the matter cannot be resolved expeditiously. Where the right to appeal is granted, it should be to a body that has the required skills and expertise to adjudicate the matter. Some laws give public service providers the right to appeal against certain decisions of the regulatory body to the country's competition authority, others to administrative tribunals or judicial courts.

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