

PUBLIC-PRIVATE PARTNERSHIP (PPPs) IN ECUADOR AND CHINA

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ABSTRACT

Nowadays, many developed and developing countries are opening their doors for the application of the public-private partnerships, more commonly known as (PPPs), which is a model that provides a framework for the delivery of public services. The PPPS is a form of collaboration between the public and private sectors for the purpose of providing public services which have been traditionally provided only by the public sector. In countries, such as Ecuador and China, PPPs projects plays a significant role in the development of the economy. This new relationship between public and private sector can bring benefits and limitations. Hence, the importance of studying this new form that different countries have been taking.

This paper will first describe the reasons why PPPs start to be used, definition of PPPs, and its characteristics and functions. Followed by, the history of Ecuador PPS and its legal framework. As well as, the history in China and the characteristics of the PPPs model. Therefore, this paper will analyze the present conditions of this law in Ecuador and the future trends of the PPPs model application in China.

Keywords: PPPs, Regulation, Definition of PPS, development of the economy, projects

INTRODUCTION

Traditionally, governments have been in charge of building, maintaining and rehabilitating physical infrastructure such as roads, ports, airports, telecommunication and electricity. In fact, spending on investment for infrastructure, used to be one of the main activities of the state. Even though, over the past three decades, public spending on infrastructure, as a proportion of GDP, has been declining worldwide (Akitoby, Hemming & Schwart, 2007). Consequently, the improvement of public infrastructure, is one of the basic and urgent requirements for the development of the society. Caused by different reasons, such as insufficiency of public resources, economic crisis and the growth of cities (Bratos, 2011).

The government needs to increase investments in public infrastructures, such as facilities of transportation, education, health, and environmental protection. Furthermore, the collaborative projects between PPPs in different spheres of action gives the chance to develop the economy of a country (Vieitez, 2016). As a result, the State goes from being a direct provider of public goods and services to be a regulator that imposes rules and conditions for partnerships projects.

It is vital to recognize that the governmental investment alone can no longer meet the needs of public infrastructures and services. Therefore, as a form of cooperation and horizontal interaction approach among various societal actors, the PPPs model has been introduced and discussed widely in Ecuador and China.

DEFINITION

There is no a international accepted definition of PPP. Due to the fact that the term is used to describe a wide range of types of agreements between PPPs sector entities (Baldeon, 2016). On the top of that, each country have adopted different definitions of PPP. It adopts different names, types and modalities, but in general the doctrine considers it as an alternative for the provision as the design, construction, operation and maintenance and financing of public infrastructures (Ysa, 2009). Consequently, interactions between public and private, expressed in concrete forms of public-private collaboration. Which means that the PPPs scheme, is based on the framework of joint decision making by the public and the private sectors.

In Ecuador, the Organic Law of Incentives for Public-Private Associations and Foreign Investment in article 8 established that “the PPP is a delegated management modality, through which the Central Government or Decentralized Autonomous Governments entrust the private manager to execute a specific project and grant total or partial financing in the provision of goods, works or services” (LOIAPP, 2015). This is the definition that Ecuador used for PPP and it gives a clear idea of how it should be used. By contrast in China, a clear definition of the meaning of PPP does not exist.

Taking this into account, Public and Private Partnerships, as its name suggests is the association of public and private capital for the development of a common good. Basically, it is the creation of a project, between a public body and a private subject, by mutually agreed contributions. The participation of the public and private partnerships can be varied. For example, through capitalization, issuance of securities, securitization, know-how, goodwill, among others (Baldeon, 2016). All these for the purpose of generating some positive outcome.

FUNCTION AND CHARACTERISTICS OF PUBLIC-PRIVATE PARTNERSHIPS

The private entity commits with the contracting public entity to design, construct, expand and rehabilitate a public infrastructure, including its equipment. Moreover, to operate such infrastructure, including its maintenance and conservation (Baldeon, 2016). As a result, the private party’s objective is to receive a return on their investment through payments throughout the life of the contract either from fees or tariffs to users (Marisol, 2006). Thus, the principle of the notion of partnership is the collaboration and mutual supporting among participants, and the sharing of resources, risks, responsibilities and rewards among the actors involved.

One of the characteristics of this relationship is that the authority in decision-making is generally shared between the public and private sector. That is why there is no single criterion regarding the direction and decisions to be taken. Further, the private partner is involved in the financing of the project and this is perhaps the greatest motivation and the reason why the public sector uses this figure in times of crisis or recession (Vera, 2017). The private company totally or partially finances the project and operates the infrastructure.

Another characteristic is the value for money. On one hand, for the public sector this partnerships represents lower cost, due to the efficiency, experience, specialization, and innovation provided by the private sector. On the other hand, the private sector gain undertake and invest (Chinchilla, 2006).

Additionally, these partnerships must have an adequate distribution of risks. This idea of sharing risk between these parties does not mean, that the public entity can transfer all activities, risks and responsibilities to the private entity (Moreno, 2012). Nevertheless, there are different kinds of risks for these partnerships. For instance, it can be political changes that affect the legislation applicable to the project, changes in tax burdens, delays in scheduled times, or natural phenomena. Also, significant changes in the projected demand for the service, in the price of the currency and in the price of money (Vieitez, 2016).

HISTORY IN ECUADOR

In 1992, President Durán Ballén issued several norms that allowed the concession of certain areas to the private sector. Even though, these reforms did not have a big impact (Robalino, 2010). In 2015, the economic circumstances began to become more complex, with the resounding fall in oil prices, the tariff safeguards and the appreciation of dollar. Which means a world economic situation in general complex that led this public and private initiatives to have greater importance (Oleas, 2017). As a result, the Organic Law of Incentives for PPPs and Foreign Investment were issued to regulate this relationships.

In Ecuador exists different mechanisms of public contracting, such as "traditional" public contracting which satisfies the need for works, goods and services required by the State and generally financed with public resources. An "non-traditional", which includes public-private partnerships (PPPs) that allow the intervention and participation of private management and within it the total or partial financing of projects with private resources. (Baldeón, 2016). Both forms of public contracting, must observe its guiding principles: transparency, legality, fair treatment, free competition, among the most outstanding, because in any cases it is about the management of public resources.

It is important to understand the differences and similarities between PPP and privatization. In both contracts exists the confluence of public and private party. However, in the case of the privatization, the ownership is transferred to the private sector. Whereas, in a PPP model, there is a continuous contractual relationship between the public and the private sector, in which the asset could be privately owned and remains as such or not once the contractual term has expired (Vieitez, 2016).

LEGAL FRAMEWORK IN ECUADOR

The Constitution of Ecuador in article 284 established among the objectives of the economic policy, “to stimulate national production, productivity and systemic competitiveness; to promote the incorporation of added value with maximum efficiency; to promote full employment; and, to maintain economic stability, understood as the maximum level of sustainable production and employment”. Furthermore, article 285 of the Constitution of Ecuador prescribes as objectives of fiscal policy, among others, “the financing of services, investment and public goods and the generation of incentives for investment in the different sectors of the economy and for the production of socially desirable and environmentally acceptable goods and services”. Therefore, the government should try to stimulate employment, the production of goods and services and responsible ecological, social and economic conduct.

Article 314 of the Constitution of Ecuador, establishes the responsibility of the State in the provision of public services of drinking water and irrigation, sanitation, electric power, telecommunications, roads, port and airport infrastructures, and others to be determined by the law. With respect to the above, article 313 of the Constitution states that “the State reserves the right to administer, regulate, control and manage strategic sectors, being those that by their transcendence and magnitude have decisive economic, social, political or environmental influence”. However, article 316 of the Constitution of the Republic of Ecuador also quotes that the State may, exceptionally, delegate to private initiative and the popular and supportive economy the exercise of these activities, in cases established by the law.

In accordance with those constitutional principles, the organic code of Production, Trade and Investments, in its article 100, determines that the mode of delegation may be of concession, association, strategic partnership, or other contractual forms according to the law, following, for the selection of the delegate, the procedures of public bidding determined by the regulation. For the implementation of the constitutional provisions the Organic Law on Incentives for Public-Private Partnerships and Foreign Investment was issued in 2015. Moreover, some additional aspects were issued in the Regulations of the Public-Private Collaboration Regime through Executive Decree No.582 in 2016. The objective of this laws is to establish incentives for the implementation of projects in the form of Public-Private Partnership and guidelines and institutional framework for its implementation (LOIAPP, 2015).

In Ecuador, the regulatory and control capacity is exclusively in the State, which is responsible for issuing legal norms as well as the exercise of supervisory and control activities. However, management can be exercised by delegation. There is two forms of delegation existing. First form of delegated management, is when the State delegate participation to private sector, but the State has a majority shareholding. This is known as mixed enterprises. The second form of delegation is in favor of private initiative. In this form, the private sector send a project that need to have minimum requirements and be qualified in accordance with the Law (Baldeon, 2016). It is important to mention that this projects have to be approved and accepted.

In order to manage this, the Interinstitutional Committee of Public-Private Partnerships created by law, is the organ in charge of the coordination and articulation of policies, guidelines and regulations related to public-private partnerships. This organ is responsible to approve public projects under the Public-Private Partnership modality (LOIAPP, 2015). They check whether the initiatives comply with the minimum elements.

Within the minimum essential elements of PPP projects are fined by these ones: a) Adequate distribution of risks, b) A clearly identified private manager, c) A pattern of long-term bilateral obligations, d) Performance indicators, service levels or other equivalents with emphasis on quality of service to users, e) The form of paid, g) The regime of incentives and benefits (General Regulations for the Application of the Organic Law on Incentives for Public-Private Associations and Foreign Investment, 2016). When the projects has accomplished all the

minimum requirements the Interinstitutional Committee shall issue a general resolution. It will regulate the procedure, the deadlines to be met and any aspect requiring special regulation.

In case of controversy the private manager will have the obligation to exhaust internally the administrative procedure. Once the administrative way has been exhausted, the private manager will have 30 working days to sue by arbitration. In the case that national arbitration has agreed, the process must be administered in an arbitration center of recognized trajectory, of not less than 10 years of experience. The decisions of the court will be in law, the applicable law will be Ecuadorian, the awards will be final and binding on the parties, following the provisions set out in the Arbitration and Mediation Act. The international arbitration will be in law, in Spanish language and the applicable rules will be the Ecuadorian law (General Regulations for the Application of the Organic Law on Incentives for Public-Private Associations and Foreign Investment, 2016)

In Ecuador, sectors focused on public and private partnerships are more in construction, social housing and development projects. Also, rehabilitation, equipment, operation and maintenance of public works for the provision of public services. Projects in the hydroelectric sector and the alternative energy sector. Other projects catalogued as priorities (Baldeon, 2016). Further, the Minister Coordinator of Strategic Sectors gave a conference promoting 94 investment projects for more than \$37 billion. The projects include potential investments in mining (44), oil (21), electricity (13), basic industries (10), water (3), bioenergy (2) and telecommunications (1) (Gallegos, 2019).

Even public and private partnerships are good for the development of the economy. This model has not been used so much in Ecuador. Therefore, CAF which is the Development Bank of Latin America (2018) has developed “the Guide on Public-Private Partnerships for Regional and Local Governments”, that is a tool to promote understanding of the public-private partnership model and to define how they should fit into strategic planning instruments of urban settings. The document presents basic notions for a better understanding of PPPs, how to evaluate the use of the PPP project and how to deal with the process of structuring a model contract, designed for urban projects, typically with a high social component.

BENEFITS

Public-Private Association has several relevant benefits. It allows promoting the coordination and joint management of projects between the private and public sectors, and promotes the compatibility of interests between the public and private sectors (Oleas, 2017). Allows the coexistence of the strengths of the public and private sectors. Promotes the sustainability of projects, avoiding extreme reactions against the private sector or the public sector (Baldeon, 2016). Moreover, the State is the main beneficiary of the application of these collaborative systems as a result of the reduction of public spending (Vera, 2017). The levels of management and operational skills of the private sector are higher than those of the public sector.

These alliances are usually expressed in long-term contracts that guarantee the stability of the agreement and the provision of a public service. In Ecuador, projects in the public-private partnership modality obtain exemptions on the income tax for 10 years, (Manya, 2017). All these benefits have been made to encourage the use of partnerships.

LIMITATIONS

Among the main limitations is possible to observe the lack of political will, lack of power for the development of public-private association, lack of legal security, rejection of mercantile mechanisms of association and financing. It is important for governments to work on these constraints.

HISTORY IN CHINA

Since the mid-1990s, the public-private partnerships (PPPs) were adopted in China. Even though, since the end of 2013, the Chinese authorities have explored the financing of infrastructure and public works through the PPP model. Over the past two years, the PPP model has expanded to finance projects in energy, transport, and environmental services (Liu & Yamamoto, 2009). Additionally, in 2008 when the Olympic Games took place, the Chinese government has to invite foreign companies and domestic private capital to participate in

infrastructure construction and the provision of public services. It is obvious that the current public infrastructure cannot meet the demands of these developments.

Further, the National Development and Reform Commission (NDRC) and the Ministry of Finance promoted the PPP model with different understandings. The NDRC takes concession as the main form of PPP model while the MOF adopted the government procurement framework (Zhong, 2019). MOF or NDRC have their own rules that each PPPs project have to follow. These differences have caused confusion in various aspects such as, definitions and scope, legal nature, dispute resolution and partner selection.

In China exists the Contract Guidelines for PPP projects published by the MOF, and the General Contract Guidelines for PPP Projects published by the NDRC. Moreover, PPP contracts follow the principles of contractual legality and compliance, equal government and social capital rights and obligations, public welfare, honesty, fairness, efficiency, and flexibility (Zhong, 2019). It usually contains the project participants, the purpose of the contract, the principle of risk allocation, investment construction, operation and maintenance, transfer, payment mechanism, rights and obligations, breach of contract, dispute settlement and other core and key clauses.

In practice, the content of the PPP contract will vary according to the industry area, project characteristics and operation mode of each project. Additionally, according to the needs of different projects, the administrative authorities for different industries, such as construction, transportation, water resources, environmental protection, health, education, culture, civil aviation, land, agriculture and forestry, are responsible for project guidance, implementation and supervision (Liu & Yamamoto, 2009).

In China, besides following rules and policies issued by central government, the local governments are in charge of promulgating specific policies and carrying out the implementation (Zhong, 2019). Therefore, in China the clarification of the relationship between concession, government procurement, and the PPP model, is the prerequisite of PPP legislation. Further, in some cases, local governments do not fully respect the agreements. For instance, Beijing's subway case where Ren Zhiqiang complained that the government made all the decisions, including pricing, investment and line extension.

In China, the essential issue is how to transform the role of central government and local governments. In other words, the government should redefine its roles and functions. Therefore, “Building Public Service Oriented Government” becomes an important idea which has to be considered (Liu & Yamamoto, 2009). Moreover, the legal framework in China should recognize the main differences between concession and procurement lie in the contestability in the relevant market and scope of application. Consequently, the proposed PPP legislation shall clarify two forms of the PPP model which are concession and public service provision under PPP.

The limits of PPPs in China are the high degree of uncertainty faced by private entities when joining PPP projects. Also, the limited capacity of local governments to conduct proper risk analysis and negotiate with private partners also prevents the development of PPP (Thieriot & Dominguez, 2015).

CONCLUSION

The association between public and private partnerships, represents business opportunities in different areas and provides incentives such as cost reduction and innovation. Since this partnerships have been implemented, it enables the public sector to have the possibilities to improve management and be competitive in sectors open to the free market. Private sectors are able to mobilize their resources and help governments to offer adequate and high quality services to the public. In China and Ecuador, PPPs provide a broad portfolio of opportunities for different societal actors to overcome structural limits.

For proper public investment, the corresponding projects need to be analyzed and evaluated to determine: their socioeconomic relevancy and their priority. In order to benefit the society in the efficient allocation of resources and in the achievement of its integral and long-term development. Moreover, governments do to ensure that PPPs efficiently provide high-quality infrastructure services with a secure legal framework, with a correct processes for selecting and implementing PPPs and the contractual obligations.

Unfortunately, there is not yet centralized or consistent monitoring of PPP projects in China. Hence, it is important for China to have a clear definition of PPPs, the scope of action and its

application, this would generate greater security for the private sector. It is important that clear contracts are established to avoid this figure not being applied in a positive way. To sum up, China and Ecuador should work to encourage the existence of more public and private partnerships.

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